FRAGMENTATION AND SYSTEMIC GOVERNANCE RISK IN INTERNATIONAL ENERGY

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ABSTRACT

In this paper, I develop the concept of *systemic governance risk*. Systemic governance risk refers to the fact that when two issues are linked, international cooperation on one issue can crowd out cooperation on another issue, thereby increasing the risk of cooperative or regulatory failures. Cooperation in one area can inhibit cooperation in other areas by raising the costs of cooperation in other areas or by distorting the incentives for governments and private actors created by another regulatory system. I apply the concept of governance risk to the regime complex for international energy, which includes among other institutions the International Energy Agency ("IEA"), the Organization of Petroleum Exporting Countries, the Gas Exporting Countries Forum, the WTO, the Energy Charter Treaty, regional free trade agreements, bilateral investment treaties, and international and regional climate change regimes.

I. Introduction

In June 2011, governments that are members of the International Energy Agency ("IEA") agreed to release 60 million barrels of oil from their strategic reserves. These reserves and the procedures by which governments agreed to release them are mandated by a treaty, the International Energy Program Agreement ("IEP"), which is open only to members of the Organization for Economic Cooperation and Development ("OECD). The purpose of the release was to reduce oil prices that had been gradually increasing as a result of supply disruptions caused by the Libyan civil war. And reduce oil prices it did. Upon the announcement of the pending release, prices of Brent crude (a benchmark oil price) fell 7.4% in a single day.[2] At least in part, the release appears to have been driven by concern that higher prices and reduced oil consumption might lead the economic recovery to stall, despite the lack of a severe or sudden price shock. IEA member states thus took advantage of the tools created by the IEP to reduce oil prices and boost consumption at a time of economic uncertainty.

This incident is puzzling. IEA membership consists of most of the world's developed countries, including Germany, France, Sweden, the Netherlands, Denmark, and a host of other European countries. These European governments tend to be on the

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[2] Liam Denning, "A Coalition Strike on Oil Markets," Wall Street Journal, at C8 (June 24, 2011).

leading edge of climate change cooperation, urging aggressive measures within the framework of the United Nations Framework Convention on Climate Change ("UNFCCC") and adopting unilateral measures within Europe aimed at spurring reductions in emissions. All of these measures – from taxes and energy-efficiency measures adopted at the national level to emissions trading schemes adopted at the EU level and between nations in the Kyoto Protocol – aim to raise the cost of greenhouse gas-intensive energy sources. Indeed, the international climate change regime is to a large extent an energy regime aimed at *increasing* the price of high-carbon energy sources such as oil in order to encourage switching to low-carbon energy sources such as natural gas and renewable energy. Rising oil prices thus presented European governments with a market event that should have incentivized the exact activity that the climate change regime seeks to encourage – fuel switching away from fossil fuels, and in particular oil. Yet rather than allow the market to work in favor of the climate change objectives for which European governments have bargained so hard within the UNFCCC, IEA member states triggered a cooperative measure under a completely different treaty with the exact opposite purpose, the *reduction* of oil prices. The June 2011 release of oil stocks is thus an example of states cooperating in one international institution – the IEP/IEA – to pursue an objective that is directly contrary to the objectives of another international institution in which they are members – the UNFCCC.

In this Article, I argue that this incident is a symptom of a larger phenomenon in international legal governance that I refer to as *governance risk*. In short, I argue that in crafting institutional jurisdiction, states trade off the risk of allowing holdouts to paralyze governance on issues within a single institution's jurisdiction – *institutional governance risk* – against the costs of coordinating (or failing to coordinate) policies across institutions – *systemic governance risk*.

Since the end of the First World War states have tried to build institutions to solve cooperative problems. After the end of the Cold War, faith in multilateral institutions and their ability to impose order on anarchy peaked. In the few years after the fall of the Soviet Union the World Trade Organization greatly expanded global economic governance, the UNFCCC was created as a forum in which states would bargain over climate change policies, and the UN Security Council – freed from the threat of duelly vetoes from the superpowers – became newly relevant to security affairs. Some even called for global governance by expanding the jurisdiction of an institution like the WTO.[3] Yet today the picture is much starker. Divisions in the Security Council have once again appeared in response to humanitarian crises in the Middle East, the Doha Round of trade negotiations appears on the verge of collapse, and governments have failed to reach an agreement on legally binding emissions reductions to succeed the Kyoto Protocol. These failures have prompted scholars and commentators to reexamine the

[3] *See*, e.g., Andrew T. Guzman, *Global Governance and the WTO*, 45 Harv. Int'l L.J. 303 (2004) (arguing that the WTO provides the best forum for dealing with both trade and non-trade governance issues).

architecture of international cooperation. In particular, what considerations determine the size and jurisdiction of a well-designed international institution?

Economic theory gives several prescriptions for how, for purposes of efficiency, jurisdiction should be allocated among competing regulatory bodies. Geographically, economic theory suggests that power over public goods should be assigned to an institution with the smallest geographic reach necessary to fully internalize to effects of the exercise of regulatory power.[4] From the standpoint of issue linkages, economic theory suggests institutional jurisdiction should be just broad enough to capture the benefits from reducing transaction costs from bargaining across issues and increasing administrative efficiencies.[5]

A survey of international institutions suggests that these prescriptions are regularly flouted. International institutions frequently have less than optimal geographic membership. Because state participation in international institutions is based on consent, states can free-ride on the efforts of other states by remaining beyond the jurisdictional reach of international institutions. Value-creating institutional issue linkages are also frequently foregone. The WTO, for example, has jurisdiction over trade in goods and trade in services, but not trade in capital.[6] Trade institutions frequently undermine environmental governance. Energy governance similarly could benefit from an integrated regulatory scheme. Energy companies are often vertically integrated, from production to transit to trade. International energy governance, by contrast, is a patchwork, with WTO rules technically applicable to trade in energy, the spaghetti bowl of international investment rules applying to investment, transit of natural resources across borders frequently governed by bilateral arrangements, and a host of fuel-specific institutions, such as the Organization of Petroleum Exporting Countries (OPEC) and the IEP dealing with production and energy security issues.

Focusing on international institutions that serve as bargaining fora for states, I argue that institutional jurisdiction – which consists of membership (territorial jurisdiction) and issue jurisdiction (subject matter jurisdiction) – poses significant risks for states. Institutional jurisdiction creates linkages that are costly to change and thus can paralyze governance as much as it can aid governance. When bargaining over legal rules in an ad hoc way, as states do in areas such as extradition or investment law, states are free to exclude holdouts and thus tailor the linkages in a treaty to the particular problem at hand. Once states institutionalize governance, however, they generally lose the ability to exclude holdouts from the institution in which bargaining occurs. Malcontents thus have the ability in institutionalized governance to slow cooperation dramatically or halt it entirely. I refer to the risk that holdouts paralyze an institution in a way that leads to worse cooperative outcomes as *institutional governance risk*.

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[4] Robert Cooter, The Strategic Constitution 107 (2000).
[5] *Id.* at 120-21.
[6] Timothy Meyer, *Codifying Custom*, 160 U. Pa. L. Rev. 995 (2012).

A rational response to institutional governance risk is to create international institutions with narrow jurisdiction. Narrow jurisdiction removes the possibility of holdouts freezing governance across issues. Like other forms of risk, however, governance risk can be systemic, by which I mean that international institutions can raise the cost of cooperating in other international institutions or even cause governance failures in other institutions. *Systemic governance risk* exists where two institutions have jurisdiction over two issues that are functionally linked, meaning that policies adopted in one issue area have direct effects in another issue area. For example, a carbon tax might change consumers' energy consumption patterns, linking climate policy directly to energy markets even if no *de jure* linkage between the climate regime and energy trade regimes is established. Where issues are functionally linked, fragmenting jurisdiction creates costs to coordinating policies across institutions that are not present in a single institution or even in ad hoc bargaining. In effect, where institutions have overlapping memberships, coordinating policies requires the consent of states that are members in only one institution. Thus, in designing institutional jurisdiction states face a tradeoff between the risk of governance failues owing to holdouts and the costs of having to – or failing to – coordinate policies across institutions that operate with different memberships and often under different procedural rules. The absence of anything resembling global government, the retrenchment in multilateralism, and the rise of regional governance all suggest that states prefer systemic governance risk to institutional governance risk.

Unfortunately, systemic governance risk is not be spread evenly among functionally linked institutions. Cooperation on smaller, "club" institutions tends to crowd out cooperation in broad multilateral institutions aimed at the production of global public goods. This crowding out effect is in part a product of institutional architecture. States can more easily design functioning institutions, such as the International Energy Agency, that incentivize contributing to the production of club goods (such as energy trade and security) and that are relatively technocratic and have low domestic political salience. By contrast, institutions aimed at the production of global public goods, such as the UNFCCC, that have high domestic political salience and broad participation from governments, civil society, and industry groups have greater difficulty generating cooperation. Such institutions suffer from higher transaction costs, deeper epistemological and normative divisions, and free riding. Consequently, even states that sincerely wish to cooperate on both energy and climate change end up privileging the former over the latter in part because institutions can more easily be designed to enable cooperation on energy trade and security.

The paper proceeds as follows. Part II reviews the role of institutions in international bargaining and the concepts of regime complexity, fragmentation, and issue linkages in the international legal literature. Part III develops of governance risk: the risk that an institution can produce cooperative outcomes that are worse from a welfare perspective than alternative governance structures. Governance risk

comes in two forms, institutional governance risk and systemic governance risk. In crafting the jurisdiction of international legislative institutions, states trade off these two kinds of risk. Institutionalizing governance makes it much more costly to exclude holdouts relative to the ad hoc rulemaking that characterizes lawmaking in areas such as international investment law. Institutions thus have a serious drawback: they create the possibility that a holdout can prevent, or at least make it more costly for, a coalition of other states to take cooperative action. In designing institutions, states attempt to mitigate this risk through a variety of procedural rules, including supermajority voting and exit clauses.

However, the most common tactic states employ is to give institutions narrow jurisdiction. Narrow jurisdiction animates governance across issues by reducing the ability of a holdout to take issues hostage. At the same time, however, it increases the coordination costs when issues are functionally linked. Functionally linked issues, like energy and climate change, are ones where policies adopted in one area affect behavior in another area, regardless of whether legal rules actually conflict. Where issues are functionally linked, choosing institutions with narrow jurisdiction (i.e., choosing not to institutionally link functionally linked issues) creates governance risks across institutions.

In Part IV, I analyze how governance risk operates in the international energy regime complex. In particular, I focus on how traditional energy institutions such as the IEA and OPEC create governance risks for newer multilateral energy institutions such as the UNFCCC. To date, there have been few studies that have examined the way in which legalized energy governance (as opposed to specific energy policies) interacts with climate governance. This oversight stems in part from the fact that there is no single energy "regime," no UN body or WTO agreement designed to coordinate global energy policies. Indeed, there is no large multilateral institution dealing with energy issues in any sort of comprehensive way at all. Instead, energy governance is a patchwork of partial regimes. Many of these regimes are organized around the priorities of particular participants in the energy trade. OPEC, for example, coordinates oil production among oil exporting nations, while the IEA coordinates responses to disruptions in the oil supply among oil importing nations. Those regimes that aim to bridge the gap between producers and consumers have either failed to gain significant traction, such as the Energy Charter Treaty, or failed to deal with energy in any comprehensive or detailed way, such as the WTO. If anything, energy governance has further fragmented in recent years, with new institutions being formed to govern individual forms of energy. Examples include the International Renewable Energy Agency ("IRENA") and the Gas Exporting Countries Forum ("GECF"). These source-specific energy institutions are linked to each other and to the climate change regime in their effort to control prices in the energy market, although they often try to nudge prices in opposite directions. It is this functional linkage among energy regimes that creates widespread systemic governance risk in international energy.

Part V discusses the ramifications of systemic governance risk for international energy governance. I argue that the existence of systemic governance risk counsels two strategies. First, large multilateral institutions such as the UNFCCC are unlikely to be successful due to the challenges they face from functionally linked energy organizations such as the IEP and OPEC. I therefore argue that holistic energy governance is more likely to emerge from bargaining among traditional energy institutions such as the IEP and OPEC. Cooperation in these institutions provides a more solid foundation for climate change cooperation than does stand alone climate change institutions. Second, institutions can be designed to reduce systemic governance risk by endowing them with narrow mandates and limited lawmaking abilities. Reducing systemic governance risk by creating small organizations that work through bottom-up lawmaking processes can reduce the friction in international cooperation created by systemic governance risk, thereby allowing states both to obtain the insurance benefits of fragmentation as well as cooperative benefits that come with reducing correlated risks of governance failure. The relatively new International Renewable Energy Agency ("IRENA") illustrates how institutions can be designed to reduce governance risk.

II. Regime Complexity and Issue Linkages

One of the key insights in international relations theory of the last twenty years is that international institutions exist to reduce the transactions costs that arise when states attempt to cooperate.[7] The role of transactions costs in the shape of international cooperation is apparent when one considers how states might cooperate over a particular international issue, for example the price of oil on world markets. Basic contract theory – a tool commonly used to analyze international agreements – cannot predict whether states will directly contract over cooperative policies to control the price of oil or whether they will instead contract to commit the issue to an international institution for resolution.[8] Directly contracting over the issue is akin to a market transaction for cooperative policies, while committing the issue to an institution for resolution is akin to choosing a firm for the production of cooperative policies. To illustrate, consider oil-exporting states that wish to coordinate their production of oil in order to ensure a particularly high return on their investment. In theory, these states could sign individual treaties each time they wished to adjust their cooperative policies. Instead, many oil-producing states banded together to create the Organization of Petroleum Exporting States (OPEC). OPEC is created by a treaty, but the organization itself makes decisions about coordinating the production policies of its member states pursuant to rules spelled out in the treaty.

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[7] ROBERT O. KEOHANE, AFTER HEGEMONY: COOPERATION AND DISCORD IN THE WORLD POLITICAL ECONOMY 102 (1984).
[8] Michael J. Gilligan, *The Transaction Costs Approach to International Institutions, in* POWER, INTERDEPENDENCE, AND NONSTATE ACTORS IN WORLD POLITICS 50, 59 (Helen V. Milner & Andrew Moravcsik eds., 2009).

Like economic actors, then, states face a fundamental choice when they seek to coordinate policies through the creation of international legal rules. They can either produce those policies in a series of market transactions, by which I mean a series of international agreements that set forth substantive cooperative policies, or they can create institutions that produce cooperative policies according to some set of rules. I use the term "institution" here to refer to an agreement that governs transactions; in other words, an international agreement that sets forth rules about the creation of substantive policies.[9]

International law has great variation in these two modes of governance. For example, international investment law is a patchwork of mostly biltateral international treaties (BITs), along with some regional and sectoral agreements and customary international law (itself largely arising from the state practice in BITs) that directly set forth substantive rules of conduct. International investment rules, it is fair to say, are created in the marketplace. Rules about air pollution, by contrast, are largely created within institutions such as the United Nations Framework Convention on Climate Change (UNFCCC), the Vienna Convention on the Protection of the Ozone Layer, or the Convention on Long-Range Transboundary Air Pollution. Each of these agreements establishes a Conference of the Parties responsible for negotiating, in accordance with procedural rules and framing norms such as common but differentiated responsibility, subsequent protocols that set forth substantive conduct rules. Such institutions are, in effect, mini-legislatures, altering bargaining dynamics among states from those that would prevail in ad hoc negotiations.

A. Issue Linkages

Despite the ready parallel between markets and firms, on the one hand, and international agreements and institutions, on the other hand, international legal scholarship has tended to elide the distinction.[10] In particular, although legal scholars have examined the role that iterative negotiations have played in promoting cooperation, they have not focused on the limits of institutionalization.[11] BITs, for example, are not infrequently amended to take into account changed circumstances, a form of iterative negotiations that does not require institutionalization.[12] Instead, international legal scholars have focused on the role

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[9] *Id.* at 14. As Gilligan notes, this is not the ordinary way in which "institution" is used in international relations theory. There, the term is used to refer to any set of rules, norms, or principles that coordinates behavior among states.

[10] *But see* JOSE E. ALVAREZ, INTERNATIONAL ORGANIZATIONS AS LAW-MAKERS 328 (2005); Andrew T. Guzman, HOW INTERNATIONAL LAW WORKS (2008).

[11] *See, e.g.,* John K. Setear, *An Iterative Perspective on Treaties: A Synthesis of International Relations Theory and International Law*, 37 HARV. INT'L. L. J. 139 (1996).

[12] *See e.g.*, Protocol between the Government of the United States of America and the Government of the Republic of
Panama Amending the Treaty Concerning the Treatment and Protection of Investments of October 27, 1982, June 1, 2000, 106 S. Treaty Doc. No. 46, *available at* http://www.bilaterals.org/IMG/pdf/US-PA_BIT_amendment.pdf (US-Panama BIT was amended to

of issue linkages and regime complexity in determining the shape of cooperation. In so doing, scholars have neglected the importance for the success of international cooperation of whether issue linkages are made within international agreements or within international institutions. I here briefly review the literature on the role of linkages in international cooperation.

There are at least three different kinds of linkages: 1) direct or functional linkages, as when action in one area affects economic activity in another area (for example, a carbon tax may change consumption and production patterns); 2) issues that are linked at the bargaining table; and 3) issues linked institutionally, as when trade measures are used to enforce environmental obligations.[13] A particular linkage may of course be described as being of more than one type. For example, a bargaining linkage may occur within an institution, as when OPEC links funds for adapting its economy to non-petroleum based activity to support for climate change initiatives within the UNFCCC.

In international legal scholarship, the study of linkages largely rose with the World Trade Organization ("WTO"). During 1990s and early 2000s, as the WTO emerged as one of the most highly functional international organizations to ever exist, the so-called "trade and . . ." literature arose, considering how trade and issues such human rights and the environment might interact.[14] Legal scholarship has emphasized institutional linkages in which the "slack" enforcement authority in one regime (typically the trade regime) can be used to enforce the rules in another regime.[15] Scholars have, for example, analyzed the effectiveness of trade sanctions as a device to enforce the Montreal Protocol's ban on CFCs.[16] Similarly, the WTO authorizes cross-retaliation in certain instances in which retaliating on the specific issue in dispute would be insufficient to deter an ongoing breach.[17]

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provide each Party's consent to intensure that investors continue to have access to binding international arbitration of investment disputes before the International Centre for the Settlement of Investment Disputes, following Panama's 1996 accession to the ICSID Convention); *See also* Understanding Concerning Certain U.S. Bilateral Investment Treaties, signed by the U.S., the European Commission, and acceding and candidate countries for accession to the European Union, September 22, 2003, *available at* http://www.state.gov/s/l/2003/44366.htm (assisting acceding EU States in the process of adapting existing BITs between themselves and the US so as to remove incompatibilities with the obligations which those States would have undertaken by joining the EU).

[13] *See* John Whalley & Ben Zissimos, *Trade and Environment Linkage and a Possible World Environmental Organisation*, 5 ENV'T AND DEV. ECON. 510 (2000); Oren Perez, *Multiple Regimes, Issue Linkage, and International Cooperation: Exploring the Role of the WTO*, 26 U. PA. J. INT'L ECON. L. 735 (2005); David W. Leebron, *Linkages*, 96 AM. J. INT'L L. 5, 16-24 (2002).

[14] See e.g., Leebron, *supra* note 13; Symposium, *The Boundaries of the WTO*, 96 AM. J. INT'L L. 1 (2002).

[15] Perez, *supra* note 13, at 747 (noting that linkages are thought desirable for their ability to boost enforcement).

[16] *See, e.g.*, Scott Barrett

[17] *See* Kym Anderson, *Peculiarities of Retaliation in WTO Dispute Settlement*, WORLD T.R. 2002, 1(2), at 123, ## (examining the economic features of temporary trade retaliation that WTO may permit under certain conditions); Joost Pauwelyn, *Enforcement and Countermeasures in the WTO: Rules are Rules-Toward a More Collective Approach*, 94 AM. J. OF INT'L L. 335 (2000). *See e.g.*, EC Measures Concerning Meat and Meat Products (Hormones), Report of the Appellate Body, W.T.O. Doc.

Where bargaining linkages are concerned, scholars have widely believed that the best solution to a public goods problem is to link participation and contribution to a "public good" to the provision of a "club good."[18] Conditioning access to a club good – such as market access, technology transfer, or foreign assistance – on contribution to a public good can deter free-riding by providing states an additional incentive to take costly measures that confer benefits on others. Relatedly, economists have shown that in many instances linking trade and environmental obligations at the bargaining table produces the welfare maximizing result.[19] For example, Bidishi Lahiri has shown that negotiating trade and environmental cooperation together can maximize welfare even if it leads to higher trade barriers on environmentally sensitive goods.[20] The intuition is that, while trade barriers erected in the name of environmental protection may reduce welfare from trade, the gains in environmental protection can outweigh the losses in trade.[21] Negotiating trade and the environment together thus improves overall welfare as against negotiating each issue individually.

To be sure, the literature recognizes limits on the uses of linkages. But those limits have not been well-explored. Theories of institutional design tend to posit that institutional scope should be broadened up until the point at which the marginal benefit from including additional issues equals the marginal cost from additional transaction costs.[22] While the benefits from broadening institutional scope often come in the form of facilitating bargaining across issues and the use of slack enforcement authority on one issue to induce compliance on another issue as

WT/DS26/AB/R (Jan. 16, 1998) (US & Canada sought retaliation against European Communities for EC's prohibition on the placing on the market and the importation of meat and meat products treated with certain hormones); European Communities—Regime for the Importation, Sale and Distribution of Bananas, Report of the Panel, W.T.O. Doc. WT/DS27/RW/EEC (Apr. 12, 1999), available in 1999 WL 216742 (Ecuador, Mexico and others sought retaliation against EC for EC's regime for the importation, distribution and sale of bananas); United States—Import Prohibition of Certain Shrimp and ShrimpProducts, Report of the Appellate Body, W.T.O. Doc. WT/DS58/AB/R (Oct. 12, 1998), available in 1998 WL 720123 (India, Malaysia and others sought retaliation against US for US's import prohibition of shrimp and shrimp products from countries that had not used a certain net in catching shrimp).

[18] Mancur Olson, THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS __ (1971); Perez, *supra* note 13, at 747 (noting this benefit of linkages).

[19] *See, e.g.*, Bidisha Lahiri, *The Welfare Synergy of Bundling International Environmental Agreements with International Trade Treaties*, 19 REV. INT'L ECON. 909 (2011).

[20] *Id*. at 917.

[21] *Id*.

[22] *See* Barbara Koremenos, Charles Lipson, & Duncan Snidal, *The Rational Design of International Institutions*, 55 INT'L ORG. 761, 787 (2001) [hereinafter "Koremenos et al."]; *see also* ROBERT COOTER, THE STRATEGIC CONSTITUTION 198 (2000).

described above,[23] the bargaining and institutional costs of issue linkages have been understudied.[24] Below, I list some of the prominent concerns with issue linkages.

First, creating international institutions entails agency costs. States surrender some measures of control to an IO, and once created, international institutions often often exert power beyond their initial mandate.[25] This expansion of power can come at the expense of founding states, leading states to try to limit their exposure to IO drift by creating organizations with narrow jurisdiction.[26]

Second, linking club and public goods together generally requires that states be prepared to deny a state that does not contribute to the public good access to the club good. In many instances, states will be unwilling to actually deny access to the public good. For example, after the United States elected not to ratify the Kyoto Protocol some scholars considered the possibility of linking American participation to technological cooperation.[27] These scholars ultimately concluded that such a linkage would not be feasible because the threat to deny the United States access to technological cooperation is not a credible one.[28]

The reverse is also true. Providing the club good or being prepared to deny access to it is often costly for states that are enforcing contribution to the public good. Most obviously, contributing to a global fund for climate adaptation is costly for developed countries. Institutional linkages of this kind thus often divide states into two groups. One group of states, what we might call the target group, has utility functions that look like those above. Access to the club good causes them to wish to contribute to the public good. States that provide the club good, though, have a different utility function. In the simplest case, such as the provision of foreign assistance through an institution like the adaptation fund, the cost of contributing the public good rises. Provision of the club good is part of the cost of providing the public good. Arguably, climate change adaptation funds are characterized by this kind of second-order public goods problem. While they in theory solve the incentive problem for developing states by linking climate change mitigation to foreign

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[23] Koremenos et al., *supra* note 22, at 785-787; Paul Poast, *Does Issue Linkage Work? Evidence from European Alliance Negotiations, 1860 to 1945*, 66 Int'l Org. 277, 282-83 (2012).

[24] Certain costs related to issue linkages have been explored. For example, Andrew Moravcsik argues that issue linkages will be unpopular with domestic constituencies that stand to lose from the linkage, and so will only be employed when the domestic constituency which loses out on the linked issue is not politicall influential. *See* Andrew Moravcsik, The Choice for Europe: Social Purpose and State Power from Messina to Maastricht (1998). James Morrow argues that in security situations issue linkages will be underutilized because they signal weakness to a potential enemy. *See* James Morrow, *Signaling Difficulties with Linkage in Crisis Bargaining*, 36 Int'l Stud. Q. 153 (1992).

[25] Andrew T. Guzman, *Doctor Frankenstein's International Organizations*, at *12 (2012), available at: http://works.bepress.com/cgi/viewcontent.cgi?article=1058&context=andrew_guzman.

[26] *Id*.

[27] Barbara Buchner et al., *Back to Kyoto? US Participation and the Linkage between R&D and Climate Cooperation*, *in* THE COUPLING OF CLIMATE AND ECONOMIC DYNAMICS 173 (A. Haurie and L. Viguier eds., 2005).

[28] *Id*. at 193.

assistance, the cost of that foreign assistance is itself a public good that developed states have seemed unwilling to provide in significant amounts.[29]

Third, institutional linkages also have the possibility to be destructive.[30] For example, market access may be enough to enforce environmental obligations in some instances, but in other instances the costs of compliance with the environmental obligations may cause states to breach their environmental obligations notwithstanding the associated trade sanctions. In such instances, issue linkages cause otherwise sustainable trade cooperation to collapse under the weight of undeterrable breaches of environmental obligations.

B. Fragmentation and Regime Complexity

A fourth concern with the usual story about issue linkages is basically empirical: although issue linkages are readily observable throughout international law and evidence suggests that they do indeed expand the ability of states to cooperate,[31] scholars in recent years have begun to listen for the dog that didn't bark. Put differently, the optimism about the ability of issue linkages to promote cooperation suggests that we should see issue linkages everywhere, and yet we don't. On this view what needs explaining is not those linkages we observe, but rather those that we do not observe. Scholars engaged in this inquiry have generally not framed the question in precisely this way. Instead, they have focused on the phenomena of fragmentation and regime complexity.

Fragmentation refers to "the emergence of specialized and (relatively) autonomous rules or rule-complexes, legal institutions and spheres of legal practice."[32] For example, trade law, the law of the sea, and multilateral environmental agreements governing climate change are all largely independent areas of law that have evolved without significant interaction, each with its own web of agreements and its own tribunals authorized to resolve disputes. Given this dispersion of authority, concern about fragmentation has often focused on the methods through which conflicts of norms should be resolved. In 2006, the International Law Commission ("ILC") Study Group convened to consider the fragmentation of international law issued a report that focused on legal rules for determining the priority of conflicting norms. In particular, the ILC Study Group emphasized rules such as *lex specialis derogat legi generali* (the principles that the

[29] Barrett, *supra* note 16, at __.
[30] Perez, *supra* note 13, at 776.
[31] *See* Poast, *supra* note 23.
[32] U.N. Int'l Law Comm'n, Fragmentation of International Law: Difficulties arising from the Diversification and Expansion of International Law, P 6, U.N. Doc. A/CN.4/L.702 (July 18, 2006) (finalized by Martti Koskenniemi) [hereinafter "ILC Report"].

specific trumps the general)[33] and *lex posterior derogat legi priori* (the principle that more recent treaties take precedence over earlier treaties).[34]

The notion of regime complexes is related to fragmentation, although with somewhat different origins. A regime complex is "an array of partially overlapping and nonhierarchical institutions governing a particular issue-area."[35]

> Regime complexes are marked by the existence of several legal agreements that are created and maintained in distinct fora with participation of different sets of actors. The rules in these elemental regimes functionally overlap, yet there is no agreed upon hierarchy for resolving conflicts between rules.[36]

Like "fragmentation," the notion of regime complexity emphasizes the fact that a particular policy space may be occupied by different legal regimes with no rules established to resolve conflicts. While fragmentation and regime complexity are closely related, scholars working with these concepts have tended to ask different questions. Regime complexity is a concept drawn from regime theory in international relations theory. Thus, while studies of fragmentation often focus on establishing rules to resolve conflicts among treaties, studies of regime complexity tend to be concerned with the behavioral incentives overlapping and nonhierarchical sources of authority create.[37]

Hypotheses about the fragmentation of international law – or in other words, the kinds of linkages that are not made – abound. One strand of thinking emphasizes the distributive implications of issue linkages.[38] On this view, issue linkages are made by powerful states when they serve their interests,[39] and when the powerful are not served by issue linkages they try to fragment international law.[40] For example, as Benvenisti and Downs have argued, powerful states may often actively seek to prevent issue linkages from emerging because bargaining issue by issue

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[33] *Id*. Conclusions (5) at 8-9

[34] *Id*. Conclusions (24)-(30), at 17-19; *see also* Vienna Convention on the Law of Treaties art. 30, May 23, 1969, 1155 U.N.T.S. 331 (entered into force Jan. 27, 1980).

[35] Kal Raustiala & David G. Victor, *The Regime Complex for Plant Genetic Resources*, 58 INT'L ORG. 277, 279 (2004).

[36] *Id*.

[37] *See* Karen J. Alter & Sophie Meunier, *The Politics of International Regime Complexity*, 7 PERSP. ON POL. 13 (2009) (hypothesizing how international legal actors may respond to regime complexity). This distinction is not exact, as some studies of fragmentation of course consider behavioral incentives and studies of regime complexity consider ways to establish hierarchy. For example, Benvenisti & Downs use the term "fragmentation" to describe the behavioral incentives for powerful states to forum shop. *See* Eyal Benvenisti & George W. Downs, *The Empire's New Clothes: Political Economy and the Fragmentation of International Law*, 60 STAN. L. REV. 595, 610-19 (2007).

[38] *See* Benvenisti & Downs, *supra* note 37; Robert O. Keohane & David G. Victor, *The Regime Complex for Climate Change*, 9 PERSP. ON CLIMATE CHANGE, no. 1, Mar. 2011 at 7, 8-9.

[39] Keohane & Victor, *supra* note 38, at 8-9.

[40] Benvenisti & Downs, *supra* note 37, at 604-9.

allows them to obtain their most preferred outcome across a range of issues.[41] International investment law is a prime example of this phenomenon. Unlike trade in goods and services, which has been linked both in bargaining and institutionally at the WTO, investment law has primarily developed through a series of bilateral and regional negotiations.[42] A similar strand of thinking argues that the uncertainty created by fragmented legal rules works to the advantage of the powerful by allowing various kinds of forum shopping.[43] Forum shopping, although in theory available to any state, in reality benefits primarily those states with the resources and ability to move effective governance between institutions.[44] While theoretically appealing, this first-best world neglects the fact that states rarely negotiate against a blank slate. Rather, negotiations are path dependent and influenced by existing institutions and legal rules.[45] Another important viewpoint sees fragmentation less grounded in the power-driven interests of states and more in the notions of what counts as law among different epistemic communities.[46] This argument sees fragmentation as the result of notions of the sources of legal rules varying within communities working in different areas of international law.[47]

In what follows, I present a complementary explanation to these views of fragmentation and regime complexity. The theories discussed above, while explaining a substantial amount of the complexity we observe in international legal rules and institutions, generally do not make a distinction between the role that different modes of rulemaking play. In particular, these theories do not capture the way in which the incentives to organize the production of legal rules through international institutions distorts the incentives of states to make broad issue linkages. Since the end of the Second World War, the story of international institutions has been a story of organizing and regularizing cooperation in an efficient manner in an effort to avoid costly conflicts like those that marred the first half of the twentieth century. However, the very choice of institutional form – with its many advantages in terms of lowering transaction costs through administrative efficiencies, the provision of dispute resolution bodies, and information production, to name but a few – counterintuitively has the effect of limiting the incentives for states to create broad issue linkages. As I explain below, issue linkages within institutions in the form of broad jurisdiction create holdup power for states that does not exist in ad hoc bargaining. Creating institutions with broad jurisdiction thus creates the risk that governance across issues will be paralyzed by holdout

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[41] *Id*. at 610-612.
[42] *Id*. at 609-612; Timothy Meyer, *Codifying Custom*, 160 U. Pa. L. Rev. 995, 997-98 (2012).
[43] Mark A. Pollack & Gregory C. Shaffer, *Hard vs. Soft Law: Alternatives, Complements, and Antagonists in International Governance*, 94 MINN. L. REV. 706, 741 (2010); Alter & Meunier, supra note 37, at ##.
[44] *Id*.; *see also* Benvenisti & Downs, *supra* note 37, at 628.
[45] Raustiala & Victor, *supra* note **Error! Bookmark not defined.**, at 279-80; Keohane & Victor, *supra* note **Error! Bookmark not defined.**, at 9.
[46] Harlan Grant Cohen, *Finding International Law, Part II: Our Fragmenting Legal Community*, 44 N.Y.U. J. INT'L L. & POL. (forthcoming 2012) (manuscript at 7), *available at* http://ssrn.com/abstract =1843566.
[47] *Id.*

states that would not be able to impede cooperation but for the existence of the institution. It is to this risk, which I refer to as governance risk, that I now turn.

III. GOVERNANCE RISK

In this Part, I develop the concept of governance risk, by which I the risk that institutionalized bargaining over the creation of legal rules produces worse outcomes relative to the alternative. Governance risk comes in two forms, institutional governance risk and systemic governance risk. Institutional governance risk refers to the risk that an institution becomes gridlocked or unable to perform the functions for which it was created due to holdouts. Systemic governance risk refers to the risk that an institution will not be able to function as intended because of the policies or actions of other institutions. Systemic governance risk is thus a kind of negative externality in which one institution's policies intrude into the policy space of another institution.[48] In creating linkages within institutions, which states do by expanding the issues an institution is empowered to deal as well as by expanding an institution's membership, states are often in the position of trading off these two kinds of governance risk.

In describing these two kinds of governance risk, I reorient the discussion of issue linkages in international legal relations. Issue linkages have generally been seen as a tool to enhance legal cooperation. Although scholars have recognized that issue linkages must have limits in their ability to facilitate cooperation due to the transaction costs they impose within an institution or as a matter of domestic politics, these limits remain undertheorized.[49] The concept of governance risk explains why we do not see a movement towards international institutions with broad jurisdiction – why we do not see more prevalent use of issue linkages within institutions in the form of institutions with broad jurisdiction – and why those institutions with relatively broad jurisdiction such as the WTO and the UNFCCC have stalled. Issue linkages *created within institutions*, rather than ad hoc issue linkages, increase the likelihood of cooperation but they also increase the risk of failure across linked issues by conferring holdup power on member states that does not exist in ad hoc negotiations. On the other hand, dividing jurisdiction among institutions where issues are functionally linked – that is, where policies in one area

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[48] *Cf.* Jody Freeman & Jim Rossi, *Agency Coordination in Shared Regulatory Space*, 125 Harv. L. Rev. (2012).

[49] *But see* Michael McGinnis, *Issue Linkage and the Evolution of International Cooperation*, 30 J. OF CONFLICT RESOL. 141 (1986); Barbara Koremenos, Charles Lipson & Duncan Snidal, *The Rational Design of International Institutions*, 55 INT'L ORG. 761 2001 (frivolous or extraneous use of linkage can create "brittle" agreements, whereby failure in one area can 'unravel' an entire agreement); T. Clifton Morgan, *Issue Linkages in International Crisis Bargaining,* 34 AM. J. OF POL. SCI. 311, 328 (1990) (linkage provision could prove politically unpopular with domestic audiences); Andrew Moravcsik, THE CHOICE FOR EUROPE: SOCIAL PURPOSE AND STATE POWER FROM MESSINATO MAASTRICHT 65 (1998) (blaming failure of issue linkage on domestic distributional implications; though linkages may create benefits, they also create domestic losers who, if highly concentrated, tend to generate more political pressure than winners). *See also* Paul Poast, *Does Issue Linkage Work? Evidence from European Alliance Negotiations, 1860 to 1945*, 66 INT'L ORG. 277, (2012).

have a direct effect on behavior in another area – can increase the risk of failure across institutions by raising the costs to coordinating policies. In designing international institutions, states thus face a critical tradeoff between the hold up power that can arise from linking issues within an institution and the increased coordination costs that arise from failing to institutionally link issues that are functionally linked.

A. The Logic of Institutional Issue Linkages

When contracting for legal rules, states have a spectrum of options from which to choose. On the one hand, states can engage in ad hoc contracting over legal rules in the same way that businesses negotiate arms-length commercial contracts. The parties can sit down at a table and negotiate a set of legal rules to govern a particular problem. Ad hoc bargaining is in many ways the most flexible sort of bargaining. It allows parties and issues to be added or subtracted until the right mix of both is reached.

At the other end of the spectrum, states can shift the production of legal rules to international institutions such as the United Nations Security Council, the World Trade Organization, or the Conference of the Parties to the UNFCCC. Rather than resembling the creation of legal rules through contract, this form of bargaining resembles legislative ordering. These legislative institutions have defined jurisdiction and often divide states into committees; they create chairmanships that exercise agenda power; and they are subject to voting rules for the adoption or bringing into force of legal rules. For example, the UNFCCC establishes a number of subsidiary bodies, the most notable of which are the Ad Hoc Working Group on Long-Term Cooperative Action under the Convention and the Ad Hoc Working Group on Further Commitments for Annex 1 Parties under the Kyoto Protocol.[50] These subsidiary bodies act in a manner similar to legislative committees, conducting negotiations outside the pressures of the full COP and acting as an agenda-setter. As for jurisdiction, I conceive of institutional jurisdiction as consisting of two elements: membership (akin to territorial jurisdiction) and issue jurisdiction (akin to subject matter jurisdiction). In its most extreme form, these legislative institutions would have plenary jurisdiction over their members and have universal membership. They thus would have jurisdiction to make legal rules over any issue confronting any one of its members. This broad jurisdiction is a form of issue linkage, because it allows member states to bargain across issues within the institution's jurisdiction. If all states were members and all issues within the institution's jurisdiction, the institution would have the maximum number of possible agreements before it.

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[50] For a graphical demonstration of the various institutions within the UNFCCC, *see* UNFCCC "Bodies" Chart, *available at* http://unfccc.int/bodies/items/6241.php (UNFCC organizational structure); *see also* WTO Organization Chart, *available at* http://www.wto.org/english/thewto_e/whatis_e/tif_e/organigram_landscape_e.pdf.

In the middle are institutions that have limited jurisdiction or membership. In reality, of course, we do not have a world legislature and so all international institutions are limited in terms of issue jurisdiction, membership, or both. The question is how do states decide what mix of issues and members should fall within an institution's jurisdiction if an institutional form of governance is selected at all?

To begin answering this question, it is useful to have an understanding of the advantages of institutions over ad hoc negotiations. International institutions lower the transaction costs to bargaining over legal rules in a number of different ways. First, international institutions generally provide fora in which states can convene to negotiate and secretariats to provide administrative support to negotiations.[51] Second, they often provide a ready set of principles, both substantive and procedural, that can be applied to all of the bargaining problems under the institution's jurisdiction.[52] For example, procedurally the COP to the UNFCCC follows the principle of consensus as its rule of decision. Substantively the UNFCCC incorporates the principle of common but differentiated responsibilities in Article 4 and institutionalizes a division between developed and developing states.[53] This division continues to play a major role in climate change negotiations, as developing states insist that developed states move first to reduce greenhouse gas emissions, while states like the United States insist that any agreement on legally binding emissions targets must include developing nations such as China and India. Regimes also provide information that can reduce uncertainty, thereby facilitating bargaining.[54]

This conventional story about the advantage of institutions fails to explain the variation we observe in institutional forms. If institutions are so advantageous, why don't states move all bargaining over legal rules into international legislative bodies? More specifically, given the role issue linkages can play in expanding possible cooperative solutions, why don't we observe a single world legislature with plenary jurisdiction and universal membership?

Frank Knight and Ronald Coase posed this same question many years ago in the context of firms: "Why can't a large firm do everything that a small firm can do and more?"[55] In the international context, the question could be reformulated as: why don't we have a single international institution with jurisdiction over all global cooperative problems, rather than a series of agreements that deal with issues singly or in small groups? Scholars such as Oliver Williamson and others, working in the tradition of transaction costs economics, posited that the "all-purpose superiority of larger firms" requires two assumptions. First, the merged firms operate collectively just as they would have operated individually (a condition

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[51] Keohange, *supra* note __, at 90.
[52] *Id*.
[53] UNFCCC art. 4.
[54] Keohane, *supra* note __, at 92-95.
[55] OLIVER E. WILLIAMSON, THE ECONOMICS INSTITUTIONS OF CAPITALISM 467 (1985).

known as replication), except when the acquiring firm selectively intervenes in the acquired firm's production process.[56] The second assumption is that such selective intervention occurs always, but only, when the expected net gains from intervention are positive (selective intervention).[57] These two conditions assure that a large firm always does at least as well as two smaller firms, and sometimes does better because the larger firm behaves just as the collection of smaller firms would have except when changed behavior is welfare-creating.[58]

The logic of replication and selective intervention is powerful in explaining the variation we observe in how states craft the scope of international institutions' jurisdiction. Like corporate ordering, international legal relations can be viewed at base as a system of contract.[59] Thus, any international agreement – whether it establishes substantive rules of behavior directly or establishes an international institution to negotiate those rules – must be in expectation Pareto improving for members as against their next best alternative.[60] Put differently, states must expect to do at least as well with the agreement as they would do without it.

Replication and selective intervention are assumptions that assure this condition is met. When these assumptions are satisfied, institutional bargaining only differs from ad hoc bargaining when the institutional form allows for Pareto improvements. These assumptions thus recognize that under standard assumptions about rational behavior, states are uninterested in the general welfare.[61] They are interested purely in their own welfare and governance and institutions are merely a means to increasing that welfare. Theories that seek to improve upon international governance thus must work within a framework of incentive-compatibility.

Translated into international institutions, replication and selective intervention would require that states bargain within an institution over each issue within the institution's jurisdiction just as they would have in the absence of the institution, except when availing themselves of the trappings of the institution is welfare-enhancing. These assumptions, in other words, ensure that states are willing to participate in the institution by making it so that any differences in rulemaking brought about by using the institutional form are Pareto improving relative to ad hoc bargaining.

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[56] *Id.*
[57] *Id.*
[58] *Id.*
[59] *See e.g.*, Alvarez, *supra* note 10, at 328; PETER M. HAAS, ROBERT O. KEOHANE, & MARC A. LEVY, INSTITUTIONS FOR THE EARTH 53 (1993); Guzman, *supra* note 10, at ##.
[60] The next best alternative is not necessarily the status quo. Powerful states often have the ability to remove the status quo as an option. *See* Lloyd Gruber, Ruling the World (2000); Timothy Meyer, *Power, Exit Costs, and Renegotiation in International Law*, 51 Harv. Int'l L. J. 379 (2010).
[61] *Codifying Custom*, *supra* note __, at __; Mark A. Pollack & Gregory Shaffer, Hard and Soft Law: What Have We Learned? at * 10, in International Law and International Relations: Insights from Interdisciplinary Scholarship (Jeffrey L. Dunoff & Mark A. Pollack eds. 2012), available at http://ssrn.com/abstract=2044800.

The logic of replication and selective intervention is incredibly powerful in explaining a number of phenomena in international legal ordering that have puzzled scholars. Scholars have long puzzled over both the prevalence of consensus rules in international institutions,[62] as well as the fragmentation of international legal ordering, in which institutions spring up with overlapping jurisdiction.[63] Consensus rules puzzle international lawyers because they prevent welfare-improving changes in the law. Every state essentially has a veto over changes in the law, and although in principal side payments and issue linkages should be sufficient to convert any welfare-enhancing (i.e., Kaldor-Hicks improving) change in the law into a change in the law that makes all states at least as well off as under the status quo (a Pareto improving change), transaction costs often prevent such transfers from actually occurring.[64]

Instead, the logic of replication and selective intervention accounts for the historic dominance of consensus rules. In ad hoc bargaining over the creation of legal rules, no states can be bound by rules to which it has not consented. Importing consensus rules into international institutions recreates the same basic bargaining situation states find themselves in the absence of institutions. As a first cut, then, consensus rules seem as if they should allow bargaining in institutions to occur just as they would outside the institution, but with a whole series of costs – including information costs, administrative costs, and enforcement costs – saved by the creation of the institution itself. Thus, while consensus rules may not allow the adoption of welfare-maximizing rules, they in theory ensure any rules adopted are an improvement – precisely the logic of institutionalizing governance.

The logic of replication and selective intervention suggests that states should be able to create international institutions with broad jurisdiction that improve international governance relative to the patchwork of issue-specific agreements that exist. And indeed, the most common decision rule employed in international institutions -- consensus or unanimity – is used in institutions precisely because it mirrors the decision rule used in ad hoc contracting. So why don't we observe more international legislative institutions with broad jurisdiction?

B. Institutional Governance Risk

The answer is that international legislative institutions have a very difficult time simultaneously satisfying the assumptions of replication and selective intervention. Institutional forms of governance automatically transform bargaining dynamics by creating institution-specific bargaining power. In particular, international institutions have procedural decision rules, such as unanimity or supermajority

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[62] Andrew T. Guzman, The Consent Problem in International Law (June 14, 2011) (unpublished manuscript), *available at* http://www.ssrn.com/abstract=1862354; Laurence R. Helfer, *Nonconsensual International Lawmaking*, 2008 U. ILL. L. REV. 71 (2008).
[63] Raustiala & Victor, *supra* note __; Alter & Meunier, *supra* note __.
[64] Guzman, *supra* note __.

rules, that give the marginal state the power to decide whether the institution adopts the rules or whether they come into force. Critically, unlike ad hoc bargaining, *a holdout state cannot be excluded in order to satisfy the relevant decision rule*. Institutionalizing governance internationally thus gives holdout states the ability to prevent the adoption of legal rules by other states. Moreover, unlike holdouts in domestic legislatures where creating legal rules through contracts between a subset of members is not an available mode of governance, holdouts in international legislative institutions are paralyzing other states that, absent an institution, would be free to adopt rules that simply do not apply to the holdout state. Satisfying the assumptions of replication and selective intervention would thus require states to credibly commit not to use institution-specific holdup power, a commitment that is impossible to make. I refer to the risk that holdouts paralyze international institutions as *institutional governance risk* and here explain the logic of institutional governance risk and institutional rules states adopt to mitigate that risk.

1. Ad hoc Bargaining and Exclusion

When states sit down to negotiate substantive legal rules, they control both the number of issues in the negotiation and the states that will ultimately be bound by the resulting agreement. They can thus both expand or contract the issues on the table and the number or identity of the members in order to reach an agreement that states are both willing to participate in and likely to comply with.[65] During bargaining, states will make demands of each other, and these demands are backed by an implicit (or sometimes explicit) threat that the state in question will not participate in the agreement if its demands are not satisfied. Whether these threats affect negotiations depend on two conditions. First, the threat of the potential holdout state to withhold cooperation must be *credible*, meaning that if the holdout state's demands are not met the holdout state must do better by following through on its threat. Second, the holdout state's participation must be *meaningful*, by which I mean that other states must prefer cooperating with the holdout on its terms (or on some compromise set of terms) to letting the holdout state go its own way. As we will see, this second condition of meaningful participation is critical to institutional governance risk. Even if a state's threat not to participate in governance is credible, in ad hoc bargaining if its threat is not meaningful it cannot prevent other states from proceeding without it.

Issue linkages are useful because when a state's threat not to participate is both credible and its participation meaningful, states are able to expand the set of issues

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[65] International agreements generally have to satisfy both a participation constraint – states must be willing to sign up to the legal rules being negotiated – and a compliance constraint – states must be willing to abide by the rules. *See* Barrett, *supra* note __, at __. Controlling the number and identity of negotiating parties and issues on the table allows states to try to create agreements that satisfy both of these constraints.

under discussion in order to create an agreement in which the potential holdout is willing to participate. Critically, however, the relationship between issue linkage and membership is different in ad hoc bargaining over international agreements and bargaining within institutions. When states bargain over cooperative policies in the absence of institutions, they are free to link issues when linking issues is value-creating and to discard issue linkages and potential cooperative partners when doing so improves the value of the potential agreement to its remaining members.

States can thus negotiate simultaneously over, for example, the distance out to sea that states exercise jurisdiction over economic activity as well as the rights of passage enjoyed by warships. In negotiating the United Nations Law of the Sea Convention,[66] states chose to negotiate over both of these issues simultaneously in part because doing so allowed states to trade cooperative policies across these issues.[67] Military powers such as the United States and Soviet Union were able to obtain favorable provisions on the passage of their warships through waters under the jurisdiction of other states (most notably strategically significant straits), while countries with significant natural resources off of their coastlines were able to extract concessions from economically powerful states (a set of states that overlaps significantly with the militarily powerful states) that resulted in coastal states exercising jurisdiction for economic purposes at a distance of 200 miles out to sea.[68]

If issue linkages are not valuable, states can discard them and negotiate over a single very narrow issue, such as inspection procedures at international ports.[69] The fact that issue linkages can be discarded in ad hoc bargaining when they are not value-creating probably accounts for the intuition many commentators have that issue linkages are generally used to facilitate welfare-increasing trades among states.[70] Selection effects ensure that ad hoc institutional issue linkages are for the most part made when they improve welfare.[71] Where membership is concerned, states

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[66] United Nations Convention on the Law of the Sea, U.N. Doc. A/CONF.62/122 (1982), reprinted in 21 I.L.M. 1261.
[67] Jon D. Carlson et al., The Scramble for the Arctic: The United Nations Convention on the Law of the Sea (UNCLOS) and Extending National Seabed Claims 4-5 (Mar. 30, 2009) (unpublished manuscript), *available at* http://ssrn.com/abstract=1472552.
[68] *Id*.
[69] Paris Memorandum of Understanding on Port State Control, 33rd Amendment, *adopted* May 3, 2011 (effective date July 1, 2011), *available at* https://www.parismou.org/Content/PublishedMedia/0ecbaa48-3c98-4df3-bd26-dc44593b68a1/Paris%20MoU,%20incl%2033rd%20amendment%20(final).pdf.
[70] *See, e.g.*, Joel P. Trachtman, *Regulatory Jurisdiction and the WTO*, 10 J. INT'L ECON. L. 631, 633 (2007).
[71] This is not to say, of course, that all issue linkages are welfare-enhancing. The most notable example of an issue linkage that is thought not to be welfare enhancing is the inclusion of TRIPs under the auspices of the WTO. Commentators have worried that the intellectual property rules enshrined in the TRIPs Agreement actually make developing states worse off than they were under the pre-TRIPs GATT regime because developing states now must pay considerably more for, perhaps most importantly, patented medicines. The logic of issue linkages that do not improve the position of all states relative to the status quo is that some powerful state is able to remove the status quo as an available option. Thus, the United States and the European Union withdrew from the GATT 1947 and acceded to the WTO, forcing states that wished to maintain favorable market access to follow suit.

likewise can be allowed to go their own way when their participation is not necessary or they can have their demands accommodated when their participation is necessary and the threat of exit is credible. Thus, American and EU participation on free trade is very meaningful, and so developing states followed the Americans and the Europeans from the GATT to the WTO.[72] American membership in the Rome Statute of the International Criminal Court is not necessary in the sense in which I use that term here, and so other states preferred to proceed without the United States rather than make concessions that would have induced the United States to ratify the Statute.[73]

Ad hoc bargaining thus allows for the possibility of excluding hold out states rather than making issue linkages necessary to satisfy the holdouts. Put differently, ad hoc cooperation, allows states to shrink the scale of cooperation when doing so improves the value of the agreement to its potential members. Of course, the structure of a problem may make it so that exclusion is not feasible and issue linkages are necessary to create side payments. For example, cooperation on international watercourses generally requires the participation of the upstream state.[74] And cooperation on certain issues will require some minimum level of participation in order for it to be worthwhile for participating states.[75] But in general, ad hoc bargaining allows states greater flexibility in adjusting the number of parties and issues under negotiation, either in the interests of expanding cooperation or narrowing it. The importance of this point cannot be overstated. As governance of major international issues such as climate change and trade has moved from ad hoc contracting to international institutions, states' discretion to shrink the scope of cooperation has been greatly reduced.

2. Institutional Bargaining

Bargaining over the creation of legal rules within institutions changes this dynamic entirely. Most notably, bargaining within institutions fixes the identities of the members because international institutions do not usually allow states to be removed due to bargaining problems. Since states cannot be removed, procedural rules as much as problem structure can dictate which states must consent. To a lesser extent, institutional bargaining also fixes the issues on the table, making it more difficult to add or subtract issues.[76]

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[72] *See* Richard H. Steinberg, *In the Shadow of Law or Power? Consensus-Based Bargainingand Outcomes in the GATT/WTO*, 56 INT'L ORG. 339 (2002).
[73] Ruth Wedgwood, *The Irresolution of Rome*, 64 LAW & CONTEMP. PROBS. 193, 194 (2001).
[74] Treaty to Resolve Pending Boundary Differences and Maintain the Rio Grande and Colorado River as the International Boundary, Nov. 23, 1970, T.I.A.S. No. 7313.
[75] Barrett, *supra* note __.
[76] *See* Gabriella Blum, *Bilateralism, Multilateralism, and the Architecture of International Law*, 49 HARV. INT'L L.J. 323 (2008).

The result is that bargaining within institutions changes whether potential holdout states have credible threats to exit and whether their participation is necessary. On the one hand, institutions generally make the threat of exit less credible by making exit more costly.[77] On the other hand, however, procedural rules in treaties often make state participation more meaningful than in ad hoc bargaining. States can no longer be removed from the bargaining table – the scope of cooperation can no longer be made smaller. Procedural rules that endow states with veto power within institutions thus become an additional consideration. These procedural rules, in effect, are the source of institutional governance risk because they magnify the risk of holdouts.

The UN Security Council is the most obvious example of an institution whose rules transform a state whose threat to withhold cooperation is not meaningful into a meaningful one. France, the United Kingdom, and Russia all wield vetoes on the Security Council that make their assent necessary for collective action under the Security Council's auspices, even though in the absence of the Security Council many security problems could quite easily be addressed without those three nations' participation and even over their objections (which is just another way of saying that those three nations are no longer as powerful as they were when the UN was founded). An even more technical example is the negotiation of the crime of aggression in the Conference of the Parties to the Rome Statute. Although the voting rules of the COP required only a 2/3 vote of the Statute's membership to adopt the proposed aggression amendments, a number of delegations failed to present credentials entitling them to vote.[78] Thus, while in principal the COP's decision rule would have allowed states to adopt a robust definition of the crime of aggression over the objection of the United States and its allies, in practice the decision rule as applied required consensus, making compromise the order of the day.[79]

3. Minimizing Institutional Governance Risk within Institutions

Given the advantages of institutions, one would expect states to try to mitigate institutional governance risk through institutional rules that allow states to eliminate destructive institutionally-created holdup power. As I argue below, the most prominent solution is to give institutions narrow jurisdiction. Narrow jurisdiction allows states to replicate more closely bargaining on a single issue without endowing states with the hold up power that comes with institutional form. But even within institutions there are a variety of devices states have at their

[77] *See* Laurence R. Helfer, *Exiting Treaties*, 91 VA. L. REV. 1579 (2005); Meyer, *Renegotiation*, *supra* note __.

[78] BETH VAN SCHAACK & RONALD C. SLYE, INTERNATIONAL CRIMINAL LAW AND ITS ENFORCEMENT: CASES AND MATERIALS 347 (2007). Beth Van Schaack, *Negotiating at the Interface of Power and Law: The Crime ofAggression*, 49 COLUM.. J. TRANSNAT'L L. 505, 520-21 (2011); Beth Van Schaack, *"The Grass That Gets Trampled When Elephants Fight": Will the Codificationof the Crime of Aggression Protect Women?*, 15 UCLA J. INT'L L. & FOREIGN AFF. (forthcoming 2012) [(manuscript at 32 n.179).

[79] *Id*.

disposal to recreate within an institution bargaining that would occur outside an institution.

The most important and probably most frequently used device states have is the use of majoritarian decisionmaking subject to an ex post ratification or opt out procedure. Generally, this procedure allows a set of rules to be adopted by a majority or supermajority of states within an institution, but either requires each state individually to ratify the instrument or provides each state with an opportunity to escape being bound by objecting. The framework/protocol agreement model, such as has been used for the ozone and climate regimes, follows the former model. Members of the framework convention, either the Vienna Convention for the Protection of the Ozone Layer or the UNFCCC, vote on whether to adopt protocols. The protocols themselves do not become binding on individual states unless they ratify the protocol. The latter model is followed by institutions such as the International Whaling Commission (IWC). Member states have an opportunity to avoid being bound by the IWC's decisions by objecting to the rule within 90 days from its promulgation.[80]

Scholars have tended to treat ex post ratification of majoritarian decisionmaking as a backdoor requirement for unanimity.[81] But this conflation of ex post ratification with unanimity fails to appreciate the distinction between rulemaking in ad hoc treaty making and rulemaking within institutions. Ex post ratification is meant to simulate the requirement of consent that exists in ad hoc treatymaking; it is not meant to, and does not have the same effect, of a unanimity rule within an institution. Most importantly, it removes the ability of a state or a small group of states to block the adoption of a set of rules by other states. In effect, ex post ratification recreates the ability of a functioning majority to adopt its own rules. International institutions that operate by consensus in bringing rules into force can actually prevent "coalitions of the willing" from acting on their own. Ex post ratification within institutions reduces this kind of governance risk, although it does not eliminate it. Depending on voting rules, a minority or simple majority may still be able to paralyze the institution.

The second thing states can do by agreement of the institution's members is expand the institution's jurisdiction either by admitting new members or adding new issues. The expansion of jurisdiction can create issue linkages that solve otherwise intractable bargaining problems, in line with the optimistic story about issue linkages. Sequential accession of this kind has been studied as a way to alleviate a

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[80] International Convention for the Regulation of Whaling, art __. The persistent objector doctrine in customary international law (CIL) might also be justified on these grounds. Although CIL is theoretically consensual, no affirmative act of state consent is necessary for a state to be bound by a rule of CIL. CIL is thus importantly different from ad hoc treaty negotiations in the way in which legal rules are made. The persistent objector doctrine makes the process of CIL formation something more akin to the negotiation of a treaty within an institution. While affirmative consensus is removed as the rule of decision, there remains the opportunity to opt out.

[81] Helfer, supra note __; Gilligan, supra note __.

potential breadth versus depth tradeoff.[82] Breadth refers to the number of members an agreement has, while depth refers to the stringency of the legal rules – how far do the legal rules require members to depart from the status quo behavior? In many circumstances, expanding membership will require states to dilute the stringency of the legal rules governing cooperation in order to attract additional members.[83] Sequential accession allows a core group of states to add additional members only when the additional member does not distort bargaining among existing members.[84]

Sequential accession and the expansion of jurisdiction more generally are limited in their ability to solve bargaining problems within institutions. Most obviously, jurisdictional expansion is a one-way ratchet. Cooperation can be scaled up, but it cannot be scaled back down as ad hoc negotiations can be. Again, international institutions lack the ability to completely exclude member states once they are already within an institution. Thus, sequential accession as a strategy to resolve institutional governance risk has built-in limits. Admitting new members to resolve one bargaining crisis may have the effect of admitting the member who exercises institutionally-created holdup power in the next round of bargaining. For example, the Czech Republic, which joined the EU in 2004, has resisted participating in EU-wide measures to bail out nations such as Greece and Spain.[85] Sequential accession also suffers from the problem that in institutions such as the WTO, existing members have to approve a new member's accession.[86] Holdouts can thus sometimes block sequential accession designed to dilute their holdout power. Similarly, holdouts might be in a position to block the inclusion of additional issues if doing so does not benefit the holdout state. For example, an issue might be introduced to divide multiple holdouts.

Finally, institutional governance risk can be mitigated by making it easier to exit from an institution or by facilitating forum shopping. Facilitating exit allows states to unwind the connection between membership and issue linkages that creates the possibility of gridlock. States can exit from a gridlocked institution and either contract in an ad hoc fashion or create a new institution. Similarly, states might move governance of an issue to a rival organization in a sort of forum shopping, as the United States did when it shifted international intellectual property issues from the World Intellectual Property Organizations to the WTO.[87] In either case, exit and

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[82] Gilligan, supra note __.
[83] *Id*.
[84] *Id*.
[85] "Czech Republic Stays Out of Fund," *Prague Post*, May 12, 2010, available at http://www.praguepost.com/business/4409-czech-republic-stays-out-of-fund.html. The Czech Republic is not a member of the eurozone, and thus is not required to participate in the bailout even though it will bear indirect financial costs from the bailout. *Id*.
[86] Marrakesh Agreement Establishing the World Trade Organization art. XII, Apr. 15, 1994, 1867 U.N.T.S. 154, at 162.
[87] Laurence R. Helfer, *Regime Shifting: The TRIPs Agreement and the New Dynamics of International Intellectual Property Lawmaking*, 29 YALE J. INT'L L. 1, 6, 13-18, 53-63 (2004).

forum shopping can substitute for the ability to exclude institutionally-created holdouts. The ability to exit an institution and the existence of overlapping institutions thus serves an important function, allowing states to credibly threaten to exclude holdouts entirely if they do not compromise.[88]

Like other solutions to institutional governance risk, however, exit and forum shopping are imperfect. On the one hand, encouraging exit and forum shopping creates the risk of opportunism. States whose fortunes change may wish to use the threat of exit to renegotiate international agreement[89] States thus have an incentive to make exit and forum shopping costlier to deter renegotiation.[90]

The second problem with using exit to control institutional governance risk is that states are oftentimes locked into dependent relationships. For example, the United States and Canada cannot avoid dealing with each other when it comes to negotiating rules governing the Great Lakes. Exiting from the Boundary Waters Commission would not change the fact that the two countries are neighbors and share the resource. By contrast, international investment law is an area in which there appears to be fierce competition between nations to agree to legal rules that will attract capital. Empirical studies have shown that competition among capital importing countries appears to drive the diffusion of bilateral investment treaties with terms friendly to capital-exporting countries.[91] Capital exporting countries are not dependent on capital importing countries and can freely contract with other states for favorable investment rules should a developing state balk or exit from a BIT, as a handful of Latin American countries have recently done.[92]

In transaction costs economics, this problem of dependency is known as the problem of asset specificity.[93] Like other kinds of assets such as a factory that makes a product for which there is only one buyer, legal rules may not have value outside the context of a specific relationship. Legal rules governing the use of a physical asset, such as the Great Lakes or a river, are the clearest example of asset specific rules. The United States cannot (at least without incurring ridicule) seek another partner to bargain over the creation of legal rules for the Great Lakes. Where assets are specific, organizing the production of legal rules through institutions makes sense because institutions, when properly designed, can deter opportunism in renegotiation that can more easily occur in ad hoc negotiations.[94]

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[88] Meyer, *Renegotiation*, *supra* note __.
[89] *Id*.
[90] *Id*. At the same time, allowing the possibility of renegotiation through the use of exit clauses may facilitate agreement in situations in which power is shifting. *Id*. at __.
[91] Zachary Elkins et al., *Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960–2000*, 2008 U. ILL. L. REV. 265, 280.
[92] *See* Jeswald W. Salacuse, *The Emerging Global Regime for Investment*, 51 HARV. INT'L L.J. 427, 469-70 (2010); Christopher M. Ryan, *Meeting Expectations: Assessing the Long-Term Legitimacyand Stability of International Investment Law*, 29 U. PA. J. INT'L L. 725, 747-48 (2008).
[93] Williamson, *supra* note __, at 29-32.
[94] *Id*. at __.

For example, an upstream state that wishes to build a dam might elect to withdraw from negotiations if governance of a river is done through ad hoc contracting. Where governance is done through an institution with relatively higher exit costs, however, withdrawing from negotiations is costlier and thus a less appealing option. Institutions can also reduce the costs of bargaining through the use of institutional devices such as supermajority voting and agenda setting, in a way that is more difficult in ad hoc contracting because the distributional consequences of agreeing to these procedures for a single negotiations are readily apparent at the time of contracting. Institutions therefore can reduce the costs of opportunism in dependent relationships.[95]

The problem of dependency is generalizable beyond shared physical assets to shared assets of any kind. Most obviously, common pool resources such as the oceans and the atmosphere lock countries into dealing with each other if they wish to establish legal rules governing use of the resource. Where many states share access to the resource, establishing legal rules can still rationally be done with less than universal participation, which reduces dependency on any one state somewhat.[96] But some measure of dependency continues to exist, suggesting that from a bargaining perspective institutions may be superior to ad hoc contracting for legal rules governing common pool resources.[97] The relationally specific nature of legal rules may explain in part the durability of certain international institutions that many feel no longer function in the interests of its members. For example, the International Whaling Commission has since the 1980s imposed a moratorium on commercial whaling that is deeply unpopular with whaling nations such as Norway, Iceland, and Japan.[98] Moreover, the moratorium does not appear to be justified by scientific data on the need to protect whales.[99] As a consequence, whaling nations established a rival organization, the North Atlantic Marine Mammal Commission (NAMMCO) and Iceland withdrew from the IWC.[100] Similarly, whaling nations have tried to shift governance of whaling issues to the Convention on the International Trade in Endangered Species, seeking to have limits on trade in whale meat eliminated or reduced.[101] These efforts have been largely unsuccessful, however, in part because shifting institutions cannot do away with the desirability of a single set of rules governing whaling.

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[95] *Id*.

[96] Barrett, *supra* note __, at __.

[97] Institutions of course have other advantages besides just bargaining advantages, including administrative efficiencies and the ability to promote enforcement. This may explain

[98] *See generally* Steinar Andresen, *The Whaling Regime*, *in* SCIENCE AND POLITICS IN INTERNATIONAL ENVIRONMENTAL REGIMES 35 (Steinar Andresen et al. eds., 2000) (describing the international whaling regime).

[99] *See* Philip Hammond, Letter of Resignation from the Chairman of the Scientific Committee of the IWC, (May 26, 1993), *available at* http://www.highnorth.no/library/Management_Regimes/IWC/le-fr-th.htm (describing the Scientific Committee Chairman.'s resignation as a result of the rejection of the Scientific Committee's advice as a basis of setting whaling quotas).

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[101] DAVID HUNTER, JAMES SALZMAN, & DURWOOD ZAELKE, INTERNATIONAL ENVIRONMENTAL LAW AND POLICY 366-67 (1998).

Legal rules governing resources that are not themselves shared but share a common market may also benefit from institutionalized governance. For example, OPEC establishes legal rules governing the production of oil in member states. The GECF aims to coordinate the production of natural gas in its member states. In theory, of course, rules coordinating production of common commodities could be done through ad hoc negotiations. Indeed, because cartels are illegal in many countries, domestic collusion of this sort is rarely if ever institutionalized. Cartels of nation-states are not per se illegal internationally, although conceivably cartel rules could run afoul of free trade rules, and so organizing the production of legal rules through institutions makes sense as a way to mitigate opportunism in bargaining and perhaps opportunism in compliance as well.

Market access is not generally characterized by dependency (although in certain situations or with respect to certain situations it might be). This may explain the turn away from the heavily institutionalized WTO towards regional free trade agreements that, because they are more thinly institutionalized, resemble ad hoc contracting for free trade.[102] Despite the tradition of multilateralizing trade rules through the most-favored nation obligation and the WTO, legal rules on market access need not be specific to any particular trading relationship because nations can find other trading partners.

C. Systemic Governance Risk

Institutionalizing issue linkages through broad grants of jurisdiction to international institutions thus creates governance risk. By removing the ability of cooperation-minded states to exclude holdouts, institutionalization fundamentally changes bargaining dynamics among states. In particular, it gives states the ability to hold up opportunistically cooperation across a range of issues. As discussed above, states have a number of devices to try to prevent additional hold up power from emerging within institutions. But perhaps the strongest device states have is the ability to fragment jurisdiction among institutions. Fragmenting jurisdiction reduces governance risk across issues and therefore increases participation. At the same time, however, it increases the costs of coordinating legal rules across issues. I refer to the risk that coordination costs across institutions leads to governance failures as *systemic governance risk*. The term "systemic risk" has been used differently in different contexts, but the underlying definition generally involves a market or institutional event that triggers additional institutional failures or makes the institutional operating environment more difficult or costly.[103] In creating institutions, states tradeoff systemic governance risk against institutional governance risk.

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[102] *See, e.g.,*, Chris Brummer, *Regional Integration and Incomplete Club Goods: A Trade Perspective*, 8 CHI. J. INT'L L. 535 (2008).
[103] *Cf.* Steven L. Schwarcz, *Systemic Risk*, 97 GEO. L.J. 193, 198 (2008).

Narrow jurisdiction in international legislative institutions is a response to institutional governance risk. By fragmenting jurisdiction among different institutions, states ensure that if one institution becomes paralyzed, governance of other issues does not necessarily also become frozen. For example, cooperation on reducing greenhouse gases in the atmosphere has been able to continue under the Montreal Protocol because the UNFCCC makes clear that those gases covered by the Montreal Protocol fall outside the UNFCCC's jurisdiction. Even though its membership is virtually identical, consisting of all UN members, the Montreal Protocol is not hostage to the same sort of pressures and divisions that have rendered the parties to the UNFCCC unable to produce a successor agreement to the Kyoto Protocol. Regional free trade agreements, which have proven to be a potent outlet for cooperation on liberalizing market access even as the Doha Round of trade negotiations have stalled at the WTO, provide another illustration of the benefits of narrow jurisdiction.[104]

Perhaps counterintuitively, narrow jurisdiction can animate governance across issues by raising the cost to linking issues. States that wish to block action in a particular institution – for example, OPEC states in the UNFCCC – have a more difficult time linking their opposition to measures that would increase the price of oil to issues governed by other institutions, such as governance of the ozone-depleting substances (ODS) governed by the Montreal Protocol. In part, delinked issues may benefit from indifference. OPEC nations have no significant objections to reducing ozone-depleting substances in the name of climate change mitigation. But if ODS were under the UNFCCC's jurisdiction, proposals to control ODS might well fail simply because the entire institution is gridlocked.

Delinking issues can also discourage hostage-taking. Hostage taking is an underappreciated form of issue linkage in international law where a state blocks action on one issue in order to get its way on another issue. When negotiating within an institution, it is easiest to link two issues already within the institution's jurisdiction in order to block undesirable action. At its most basic, this kind of tactic changes how states vote because it may change their preference about the package deal before them. States might vote, for example, to adopt Proposal 1, would vote against Proposal 2, and would vote against a combined proposal. Narrow jurisdiction prevents, or at least makes more difficult, combining proposals subject to different institutions' jurisdiction. Proposals for regulating ODS cannot come before the UNFCCC; proposals regarding changes to investment law cannot come before the WTO. Delinking issues may also affect bargaining dynamics simply by ensuring that different personnel negotiate over different issues, thereby making linkage more difficult at the practical level of negotiations themselves.[105]

[104] Brummer, *supra* note __.
[105] This is not to say that states can't threaten to hold up a proposal in one institution in order to get their way in another institution. It is just to say that dividing jurisdiction makes doing so costlier.

Finally, different institutions may have different rules and different memberships. A state interested in linking two issues may actually lack the ability to do so if two different institutions have different decision rules. For example, the Montreal Protocol allows certain decisions to be made by a two-thirds vote, while the UNFCCC operates by consensus. Thus, even if OPEC states wanted to link regulation of ODS to regulation of other greenhouse gases, they might lack the votes to do so with the Montreal Protocol.

The drawback to fragmenting jurisdiction among institutions is that it raises the cost to coordinating policies across institutions. These increased coordination costs can be problematic for two reasons. First, they increase the costs of making valuable issue linkages. This is hardly surprising. Fragmentation raises the cost of making issue linkages, both beneficial ones and destructive ones. Second, some issues – like energy and climate change – are functionally linked even if they are not institutionally linked. In other words, policies made on one issue may have direct effects on behavior in another issue. For example, a carbon tax might change consumers' energy consumption patterns, linking climate policy directly to energy markets even if no *de jure* linkage between the climate regime and energy trade regimes is established.

The tradeoff between deterring opportunistic issue linkages and encouraging beneficial ones through the jurisdiction of international institutions is a matter of degree. Like the use of exit or escape clauses, narrow jurisdiction raises the marginal cost of linking across issues because it either requires modifying the institutional architecture or going entirely outside that architecture.[106] Such modification typically requires the consent of the institution's members.

Raising the costs of linking issues in order to deter certain kinds of linkages can serve as a commitment device to bargain without introducing extraneous considerations. The introduction of additional issues to bargaining can have a number of distorting effects that states might wish to avoid. Perhaps most importantly, as more issues have to be resolved simultaneously the likelihood of cycling among alternatives – that is, the probability that a single agreement cannot be reached because of the number of issue involved – goes up.[107] Reaching agreement in the presence of cycling requires conferring institutional bargaining power on particular states or individuals, such as through the creation of a strong form of agenda control.[108] By removing the need for institutional (but undemocratic) techniques such as agenda control, narrow jurisdiction acts as a commitment device on the part of states to bargain over a single issue the way they would in ad hoc negotiations, while limiting their freedom to resolve bargaining impasses through linkages. At the same time, it can also have distributional

[106] *Exiting Treaties*, *supra* note __; *Power, Renegotiation*, *supra* note __; Sykes.
[107] Cooter, *supra* note __, at 121. The probability of cycling increases because states may have double-peaked preferences when choosing among alternatives on more than one dimension of choice. *Id*.
[108] *Id*.

consequences, as when powerful states create institutions with narrow jurisdiction to prevent issue linkages from being used to build a coalition among weaker states.[109]

Of more interest here is the coordination costs imposed across functionally-linked but institutionally unlinked issues such as climate change and energy. For many issues, a failure to coordinate is not a problem and thus fragmented jurisdiction makes sense as a device to eliminate holdouts. For example, there is no intrinsic reason to link intellectual property rules to the governance of international watercourses. Rules about intellectual property do not generally affect the sharing of water resources.[110] But where functionally-linked issues are involved, a failure to coordinate legal rules across institutions can make cooperation more costly in a number of different ways. First, rules adopted in one institution may make it costlier for states to take action in another institution. For example, adopting stringent intellectual property rules in the WTO's TRIPs Agreement and TRIPs Plus rules in free trade agreements have made it more difficult for developing states to negotiate favorable provisions for access to critical medicines and have also made vindicating the Convention on Biological Diversity's provisions according rights to developing countries with bio-resources considerably more troublesome.

Second, rules in one institution might change the incentives of market participants in a way that works against compliance with rules coming from another institution. Many modern treaties, particularly environmental treaties, formally regulate states but in fact exist primarily to induce states to regulate their populations and economies in a particular way. This kind of international lawmaking is different from traditional areas of international law. Where market access, diplomatic immunity, or arms control are concerned, it is the state itself that is both promising to take (or refrain from taking) action and is capable of doing so.[111] Making compliance more difficult, of course, may also affect the willingness of states to enter into legal commitments that are likely to result in drastic changes.[112] But states at least directly control their own actions, and thus their ability to comply with legal obligations, in these areas. Where states' international obligations really make them internationally responsible for the actions of private parties within their borders, conflicting incentives become more damaging because there is no single institution such as the state to decide how to accommodate competing directives (although, to be sure, the state can try to incentive market actors to comply with competing international rules). Thus, for example, policies adopted by OECD countries acting through the IEP to reduce oil prices have the effect of boosting oil

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[109] Benvenisti & Downs, *supra* note __, at __.

[110] This is not deny that there might in some instances be connections between these two areas.

[111] Of course, even this picture is not quite so simple. In federal systems, the state remains responsible for the actions of regional or local governments even if the central government lacks the legal authority as a matter of domestic law to control the actions of regional or local governments. *See Medellin*; Argentine Investment Dispute.

[112] *See* DOWNS, ROCKE, & BARSOOM*, Is the Good News About Compliance Good News about Cooperation?*

consumption and making compliance with emissions reduction obligations in the Kyoto Protocol more difficult. In this way, institutions that deal with functionally-linked issues may end up undermining each other through a failure to coordinate policies.[113]

Given the potential to undermine each other, one might wonder why states ever fragment jurisdiction among functionally-linked issues. There are a variety of reasons for delinking functionally linked institutions. First, in certain issue areas failures to coordinate may not be very costly. For example, there is clearly some benefit to coordinating quotas on catches for whales set by the International Whaling Commission and the rules of trade in whale meat under the Convention on the International Trade in Endangered Species. Listing a species of whale as an Appendix II species – a relatively lax form of control – might undermine the IWC's rules by creating more of a market for whale meat. But a failure to coordinate between these two regimes is relatively less costly as most whale meat harvested in alleged violation of the IWC's moratorium is harvested for domestic markets, most notably in Japan.[114] Second, undermining other institutions may be deliberate, as when institutions with different memberships compete to govern a particular issue area. Third, it may be an unintentional byproduct of resolving issues serially rather than all at once. International institutions are often established to resolve particular crises and so may not be granted broad jurisdiction. For example, the international institutions governing the production and consumption of oil – the IEP Agreement and OPEC – were founded in response to changing patterns of market power among oil-producing and oil-consuming nations in the 1960s and 1970s.[115] In light of the era and context in which they were created, it is hardly surprising that they do not deal with environmental issues related to energy, such as climate change.

In order to refine predictions about where states will seek more integrated governance versus fragmented governance, as well as to devise policy prescriptions to facilitate welfare-enhancing cooperation, it is useful to think more specifically about the causes and effects of systemic governance risk. I emphasize here two different kinds of systemic governance risk: 1) inter-club risk and 2) inter-regime risk. The primary difference between the two is the role of membership. Inter-club externalities involve failures to coordinate policies among institutions that have largely separate memberships. Inter-regime risk involves failures to coordinate

[113] The effects of failing to coordinate policies might be likened to "regulatory spillovers." *See* Jack Goldsmith, *Unilateral Regulation of the Internet: A Modest Defense*, 11 EURO. J. INT'L L. 135, 142 (2000) (discussing regulatory spillovers arising from unilateral national regulation of the Internet). The term "regulatory spillover" is often used to describe the extraterritorial effects of national regulation. Regulatory measures adopted in one jurisdiction may have effects in another jurisdiction. Similarly, legal rules and policies adopted by one institution can raise or lower the costs and benefits of cooperation in another legal regime. In this way, legal rules intrude upon the "regulatory space" of a particular regime in a way similar to how national regulatory policies can functionally intrude upon the ability of other states to regulate activity in their own jurisdictions.
[114] Australia v. Japan, 2010 ICJ.
[115] *See infra* Part ___.

among institutions that have overlapping memberships. Overlapping membership is of course a spectrum, and so these two categories are meant to be archetypes rather than hard and fast categories. Nevertheless, they are useful because systemic governance risk works differently depending on the extent to which membership in the institutions overlaps.

1. Inter-club Risk

Inter-club risk arises when two or more institutions have largely distinct memberships and impose costs on each other. The most obvious example of inter-club risk is military alliances such as the North Atlantic Treaty Organization (NATO) and the Warsaw Pact. The establishment of each institution coordinates security policy among member states in a way that creates externalities for the other institution. NATO's creation magnified the security risk felt by Eastern Bloc states during the Cold War, leading to the formation of the Warsaw Pact. Similarly, the rise of OPEC as a major influence on global oil prices led to the creation of the IEP and the IEA among consumer nations in an effort to blunt OPEC's ability to raise prices or reduce oil supplies to IEP member states.[116] Past their creation, policies adopted in each of these institutions, such as strategic decisions about troop deployments in military alliances, make it more difficult for rival clubs to provide the relevant good for its members.

Inter-club risk differs from inter-regime risk because it is essentially externalized. That is, because membership in the different club institutions does not overlap, the costs of failing to coordinate policies in one institution is felt by non-member states. In many cases, this may be exactly what states intend. Cartel-like institutions like OPEC and the Nuclear Suppliers Group are created specifically to implement policies that have effects in third parties. Inviting those third parties into the institution would increase institutional governance risk by introducing likely holdouts. The logic of institutional governance risk thus suggests narrow jurisdiction. Moreover, because systemic risk is externalized onto non-members, there is (at least initially) no countervailing reason for member states to pursue inclusiveness.

Inter-club risk has at least three consequences for legalized cooperation worth discussing. First, as mentioned above, the creation of an institution that externalizes its costs onto non-members may result in the formation of rival institutions. Inter-club risk can these lead to a series of institutions that aim to manage systemic governance risk created by other institutions. Oddly enough, this means that there are many international institutions that exist to mitigate the costs *created by cooperation*. Put differently, institutions such as military alliances or cartel-like institutions do not necessarily enhance welfare when taken together. Instead, inter-club risk creates incentives for a "cooperative arms race" in which states build institutions to manage the costs imposed on them by other institutions.

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[116] *See infra* Part ___.

Second, inter-club competition of the kind described above can spillover into other institutions. To return to the military example, competition between NATO and the Warsaw Pact countries regularly spilled over into the United Nations and impeded cooperative efforts on unrelated issues. Inter-club competition thus creates an additional set of costs to the extent that states prioritize the club institution's goals over priorities in other institutions.

Third and finally, as the costs imposed by inter-club competition rise, states will seek ways to manage those costs. In some cases, this may lead to the formation of meta-institutions that try to internalize the negative externalities created by the club institutions. These kinds of meta-institutions should only be formed when the costs of inter-club competition – the costs of systemic risk – have become so large that they outweigh the risk of paralysis flowing from introducing groups with sharply divergent preferences into a single institution. Alternatively, powerful states make seek to manage the costs of inter-club competition through relationships with member states in the rival institution. For example, the United States has used its close relationship with Saudi Arabia, the most powerful country in OPEC, to influence OPEC's policies in ways favorable to oil-consuming nations

2. Inter-regime Risk

Inter-regime risks differ from inter-club risks in that significantly overlapping memberships are involved. Thus, while the systemic governance risks are externalized from an institutional perspective, they are not fully externalized from the point of view of states. There are two notable features of inter-regime risks that flow from this observation.

First, we would in general expect inter-regime risks to be managed more aggressively by states than are inter-club risks. Because states bear inter-regime risks themselves in other institutions, they should want to mitigate those risks. States have at their disposal a number of techniques to control inter-regime risks. Administrative coordination between institutions can ease some of the burden of inter-regime risks by facilitating institutional dialogue, integrating management, and cooperatively addressing compliance issues. And, indeed, it appears that agreements between the secretariats of multilateral institutions are on the rise.[117] These kinds of arrangements reduce inter-regime risk through negotiated instruments.

States can also delegate the task of imposing coordination on regimes. Dispute resolution bodies can adjudicate between competing institutions and thus impose a form of coordination on functionally-linked institutions. For example, the WTO Appellate Body can assess the relevance of environmental treaties to trade

[117] *See* Karen N. Scott, *International Environmental Governance: Managing Fragmentation through Institutional Connection*, 12 MELB. J. INT'L L. 1 (2011) (discussing agreements and formal cooperation among multilateral environmental institutions).

obligations. The difference between inter-regime and inter-club governance risks may explain in part why so few disputes involving club regimes are submitted to tribunals, while many large multilateral treaties do contain consent to jurisdiction. Delegating a coordination function to a tribunal imposes agency costs on states – the outcome chosen by the tribunal may not reflect the states' desired outcome. States are only willing to bear these agency costs when they also capture the rewards of coordination. Inter-regime risks allow states to capture these benefits, while inter-club risks do not, thereby deterring delegated coordination where institutions such as OPEC, the OECD, the Basle Banking Committee, or the Nuclear Suppliers Group are involved.

Second, where inter-regime risks are concerned states can be forced to choose between two competing priorities without the assurance of being able to coordinate policies across institutions. In these situations, institutional architecture is critical in determining how states will resolve priorities that have been pitted against each other. Institutions with lower institutional governance risks – those less prone to holdouts – will thus be more likely to succeed at the expense of institutions with higher governance risk. To see how detrimental this can be, imagine that a group of states, Group 1, cares equally about two issues and that the two issues have been entrusted to different institutions, A and B. Group 1 controls institution A, but institution B is beholden to a second group of states, Group 2. Coordinating policies across these two institutions thus requires Group 1 to buy off Group 2 in institution B. Where the cost of coordinating between the two institutions – the cost of concessions or side payments to Group 2 – exceeds the gains from coordination, the first group of states will simply adopt its preferred policy in institution A and leave institution B gridlocked. Moreover, the cost of the concessions necessary to coordinate policies across the two institutions depends not only on membership issues, specifically Group 2's membership in Institution B; it also depends on the procedural rules in Institution B. If Institution B operates by a super-majority, then Group 2's ability to hold up the institution is only as strong as the price of buying off the marginal member necessary to obtain a super-majority. On the other hand, if Institution B operates by consensus, each member of Group 2 must be compensated for agreeing to allow coordination between Institutions A and B.

The result of this dynamic is that Group 1 may end up choosing policies in Institution A that are suboptimal from its point of view because institutional architecture makes reaching a better result prohibitively expensive. As we shall see in Part IV, this is the exact situation with regard to climate change and energy governance.[118] Institutional and systemic governance risk interact in a way that pushes states to make policy choices based on the costs of bargaining across institutions. An inter-regime perspective highlights the importance of costs in shaping international cooperation. When faced with inter-regime risk, all else equal states will choose cooperation in the regime with lower bargaining costs over the regime with higher costs. And as cooperation becomes cheaper in one regime,

[118] *See infra* Part IV.

states will be willing to forego potentially larger benefits from cooperation in another regime. This insight is akin to the idea that as production costs fall, resources are more efficiently allocated to the more productive resource. As the costs of cooperation in one institution falls as a function of international architecture, states will reallocate cooperative resources from a potentially more beneficial area of cooperation to one in which net benefits are higher.

Conclusion

The absence of international institutions with broad jurisdiction suggests that in general states prefer systemic governance risk to institutional governance risk. That is, they find that coordination costs across institutions are less detrimental to their cooperative goals than are hold up costs to bargaining across issues within institutions.

IV. Energy Governance

In this Part, I focus on how institutional and systemic governance risk have influenced the development and operation of the international energy regime. International energy governance is one of the most fragmented areas of international law. Part trade regime, part investment regime, and part climate regime, energy governance defies easy characterization. In many respects, international energy governance resembles international financial law – an area of the law that has resisted the multilateral legalization trend that has resulted in institutions like the UN and the WTO, but that has periodically been the source of global conflicts. The Arab oil embargo of 1973 is perhaps the best-known conflict, although more recently disputes over natural gas prices between Russia, Ukraine, and Europe have been flashpoints for geopolitical tensions.

The international energy regime complex consists of a broad mix of institutions. A non-exhaustive list of just the inter-governmental institutions dealing with energy would include OPEC, the International Energy Program Agreement (IEP) & the International Energy Agency (IEA), the Gas Exporting Countries Forum (GECF), the WTO, the Energy Charter Treaty (ECT), the UNFCCC and the Kyoto Protocol, the G8 and G20, the International Atomic Energy Agency (IAEA), the International Renewable Energy Agency (IRENA), bilateral investment treaties and regional free-trade agreements, and regional initiatives put forward by institutions such as the EU, the Economic Community of West African States (ECOWAS) and the Asia-Pacific Economic Community (APEC). These institutions have different purposes and histories. Among the major energy governance institutions in place today, the IAEA – which has a dual mission, encouraging the development and spread of civilian nuclear technology while also establishing "safeguards" desgined to ensure that nuclear technology and fissionable material is not diverted to military purposes[119] –

[119] IAEA Statute arts. III, XII.

has the oldest pedigree, dating back to 1956.[120] The IAEA has a dual mission. The WTO, for its part, establishes general rules that apply to trade in energy-related goods and services but fail to deal comprehensively with energy-specific problems such as limitations on transit, investment, production, and export.[121] The ECT as a legal regime tries to deal more comprehensively with energy-specific issues but has suffered from a lack of support among major energy supplying nations.[122]

In what follows, I focus on two specific aspects of the international energy regime. First, in Section III.A I describe the history of three of the most significant energy institutions: OPEC, the IEP and IEA, and the UNFCCC. In general, energy institutions have opted for systemic governance risk over institutional governance risk across energy issues. In Section III.B, I analyze the effects of systemic governance risk among these three institutions. Specifically, while OPEC and the IEA externalize to each other the costs of their cooperative policies, both undermine the UNFCCC.
They do so by creating competing incentives for consumers to switch to low-carbon fuels. The UNFCCC is an institution designed in part to produce international policies that will raise the price of greenhouse gas emissions (GHG) and therefore induce consumers to switch to low-GHG fuels (what I shall refer to as fuel-switching). Counterintuitively, the very same states that push for policies that produce fuel-switching act in economic energy institutions such as the IEA in ways that create the opposite incentives. I argue that in situations of inter-regime systemic governance risk, states will implement policies in the regime with the lower institutional risks. This reality distorts cooperation over climate change to a much greater extent than has previously been understood. Finally, in Section III.C, I discuss why states would prefer systemic governance risk over institutional governance risk in energy. In short, energy is an area in which the problem of holdouts is sufficiently large that states prefer to animate governance on economic issues through narrow jurisdiction, rather than attempt to link economic and environmental issues institutionally.

A. Energy Institutions

In the middle of the twentieth century, the most important international energy institution was the Texas Railroad Commission. The key driver in stabilizing global oil prices is spare capacity.[123] Spare capacity refers to a producer's ability to hold

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[120] Statute of the International Atomic Energy Agency.
[121] Yulia Selivanova, *Managing the Patchwork of Agreements in Trade and Investment* 52, in GLOBAL ENERGY GOVERNANCE (Andreas Goldthau & Jan Martin Witte, eds., 2010) (discussing how WTO rules were once thought not to apply to energy because they do not single energy out, but now are generally considered applicable to energy as any other good or service).
[122] No significant non-European energy exporters have ratified the ECT and in 2009 Russia, which had signed the ECT and been applying the treaty provisionally, indicated its intention not to pursue ratification. *See* Arunabha Ghosh, *Seeking Coherence in Complexity? The Governance of Energy by Trade and Investment Institutions*, 2 Glob. Pol. 106, 114 (2011).
[123] Robert McNally & Michael Levy, *The Crude Predicament: The Era of Volatile Oil Prices*, 90 FOR. AFF. 100, 102 (2011).

some portion of its production capacity in reserve. This idle production capacity can be activated on short notice to increase the production of oil, thereby adding supply and smoothing out price volatility.[124] With significant low-cost oil resources, Texas, acting through the Texas Railroad Commission, was able to regulate and stabilize global oil prices by holding up to 25 percent of its production capacity in reserve.[125] As a matter of regulation, the Texas Railroad Commission did this by setting production quotas.[126] In coordination with the Interstate Oil Compact Commission (now the Interstate Oil and Gas Commission), a multi-state agency formed on the basis of an interstate compact, and international oil companies based in the United States and Western Europe, the Texas Railroad Commission provided one of the early examples of regulating the supply, and therefore the price, of oil through horizontal agreements among governments, as well as public-private partnerships in international regulation.

By 1972, however, Texas was producing at full capacity and thus was unable to act as an effective price regulator.[127] When the 1973 Arab-Israeli War resulted in an oil embargo against the United States, Texas could not increase production and global oil prices shot up.[128] Into the vacuum stepped the Organization of Petroleum Exporting Countries ("OPEC"), and in particular the Kingdom of Saudi Arabia. OPEC formed in 1960 in response to a collapse in global oil prices. Although OPEC is often described as a cartel, OPEC's origins are found in the fiscal policies of oil exporting countries. The collapse of global oil prices in the 1960s deprived oil-exporting states of a prime source of revenue, namely royalties and income taxes paid from international oil companies operating within their countries.[129] Throughout the 1960s, OPEC's efforts were for the most part not focused on production quotas at all, but rather on negotiating agreements with the international oil companies to increase the share of revenue host governments received.[130] Moreover, OPEC made national sovereignty over oil resources a priority, declaring in its 1968 Policy Declaration that, "except as otherwise provided for in the legal system of a Member Country, all disputes arising between the Government and operators shall fall exclusively within the jurisdiction of the competent national courts."[131] This policy reflected an effort by OPEC nations to implement the Calvo Doctrine, whereby disputes with foreign oil companies would be governed by national law and national

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[124] *Id*.

[125] *Id*.

[126] By statute, Texas banned "[t]he production, storage of transportation of crude petroleum oil or of natural gas in such manner, in such amount, or under such conditions as t constitute waste." Waste was defined as "[t]he production of crude petroleum oil in exces of transportation or market facilities or reasonable market demand. The Commission [was] authorized to determine when such excess production exists or is imminent, and to ascertain the reasonable market demand." *See Brown v. Humble Oil & Refin. Co.*, 83 S.W.2d 935, 938 (Tex. 1935) (describing the statutory powers of the Texas Railroad Commission).

[127] McNally & Levy, *supra* note 123, at 102.

[128] *Id*.

[129] Bernand Mommer, GLOBAL OIL AND THE NATION STATE 140-143 (2002).

[130] *Id*. at 143-146.

[131] Declaratory Statement of Petroleum Policy in Member Countries, Res. XVI.90.

courts, rather than international law and international arbitration tribunals, as had heretofore been the case.[132]

This change in fiscal policy by OPEC nations is what eventually resulted in the nationalization of the oil industry in OPEC countries.[133] The effective rent, in the form of royalties, taxes, and equity interest, that oil companies paid to host governments had become so high that national governments now effectively controlled the oil industry. By some accounts, the oil industry in OPEC countries had been de facto nationalized by 1973, even though the legal niceties would take some further time to resolve.[134]

Thus, by the early 1970s an organization that had formed to coordinate negotiating positions among oil exporting nations in an effort to boost fiscal revenues had become the primary oil governance institution in the world. By setting quotas, a practice that did not formally begin until 1982, OPEC was able to control the volume of oil on the market and thus exert some influence over short-term prices.[135] By controlling investment in oil extraction, investments that necessarily took a longer time to bring additional capacity online, OPEC nations were also able to exert greater influence over medium- and long-term prices.

Not surprisingly, oil-importing nations responded. Although their response has primarily been viewed through a political lens, in fact oil-importing nations' response was to a large extent an attempt to establish legal rules aimed at increasing the supply of oil on the market, and therefore ensuring stable and ideally low oil prices. The oil-importing nations response was two-fold. Most directly, OECD member-states signed the International Energy Program, a treaty that established the IEA. The IEA was a solution to a classic prisoner's dilemma among states. The Arab oil embargo was imposed by the Organization of Arab Petroleum Exporting States, a subset of OPEC states, and not by OPEC itself as is commonly thought.[136] Oil importing states initially responded by individually hoarding oil, a response that only exacerbated the oil shortage.[137] In this way, the oil crisis of the early 1970s bears a remarkable resemblance to the international governance crisis that led to the Great Depression. States individually took action that further decreased the amount of oil on the market, just as states in the 1930s took protectionist action that had the effect of further dampening global trade.

In 1974, the United States convened an international conference to address this governance shortfall, the result of which was the International Energy Program

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[132] Timothy L. Meyer, *Codifying Custom*, 160 U. PA. L. REV. __, __ (2012).
[133] Mommer, *supra* note 129, at 159.
[134] *Id*. at 159-60.
[135] *Id*. at 165-67.
[136] Andreas Goldthau & Jan Martine Witte, *Assessing OPEC's Performance in Global Energy*, 2 Glob. Pol. 31, 33 (2011).
[137] Ann Florini, *The IEA in Global Energy Governance*, 2 Glob. Pol. 40, 41 (2011).

("IEP") and the IEA.[138] The IEP required member states to maintain 60 days of net oil imports in reserve (a number that has subsequently been increased to 90 days). The IEP also required member states to have in place measures that could depress short-term demand in response to a short-term squeeze in oil supplies. Finally, the IEP established an allocation plan whereby strategic reserves would be shared among member states in response to defined threshold events. The IEA secretariat was tasked with determining when the threshold conditions triggering IEP obligations were met, although decisions of the secretariat could be overridden by a majority IEA Governing Board. Over the years, the IEP has been amended to take into account shifts in the structure of the global oil market, which has evolved from a market driven by long-term supply contracts to one driven by a thriving spot market in which prices can be affected by panics not related to underlying dynamics of supply and demand.[139] In response, in 1984 the member-states agreed on the Co-ordinated Emergency Response Measures ("CERM"), which are implemented at the discretion of the IEA Governing Board, rather than in response to specific threshold criteria, with the objective of reducing oil price shocks. CERM measures have been activated three times: in 1991 in response to the first Gulf War; in 2005 in response to severe weather-related production disruptions in the Gulf of Mexico; and in June 2011 in response to the ongoing disruption of oil supplies from Libya.[140]

The climate change regime's history is somewhat different. Beginning in the 1970s and through the 1980s, scientific research began to link the emission of greenhouse gases with changes to the climate and specifically global warming.[141] This research spurred calls for international action and in 1990 the United Nations authorized an Intergovernmental Negotiating Committee on Climate.[142] Negotiations culminated in 1992 with the opening of the Framework Convention on Climate Change, or UNFCCC.[143] While the UNFCCC contains little in the way of substantive obligations, it establishes an institutional framework for negotiating legally binding climate change obligations. It establishes a Conference of the Parties (COP) that effectively acts as an international legislature for climate change matters. The COP is the "supreme body of this Convention," tasked with reviewing implementation of the Convention and "any related instruments that the [COP] may adopt, and shall make, within its mandate, the decisions necessary to promote the effective implementation of the Convention."[144] The COP may choose its own rules of procedure, although

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[138] Florino, *supra* note 137, at 41.
[139] Florino, *supra* note 137, at 41.
[140] *Id*. at 41-42.
[141] Hunter et al., *supra* note __, at 609.
[142] *Id*. at 609-10.
[143] *Id*.
[144] UNFCCC art. 7.2.

such rules must be adopted by consensus of the COP's members,[145] and each member has one vote.[146]

The UNFCCC's stated objective is to incentivize states to adopt policies aimed at the "stabilization of greenhouse gas concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system."[147] In practice, cooperation on so-called climate change mitigation amounts to using binding emissions reduction obligations to encourage states to adopt policies aimed at inducing an economy-wide shift from high GHG fuels to low GHG fuels. The climate change regime is thus, in reality, an energy regime.[148]

Neither the UNFCCC nor the Kyoto Protocol specifies the policies states must adopt to reduce their GHG emissions. Rather, the Kyoto Protocol uses a soft harmonization approach, encouraging emissions trading schemes through its Flexibility Mechanisms. And while the EU's Emissions Trading Scheme has been by far the most successful such program to take hold in the wake of Kyoto, other policy instruments – most notably a global carbon tax – continue to be discussed.

Whatever policy instrument is adopted, the objective is to raise the price of GHG emissions by placing a price on a unit of a GHG itself. For example, one estimate of the amount of carbon per ton of oil equivalent – a normalized measure of the amount of carbon released by burning equivalent amounts of fossil fuel – is 1.076 tons for coal, .837 for oil, and .641 tons for natural gas.[149] The effect of applying a price to carbon is to create a wedge between these prices. Normalizing to oil, putting a price on carbon will result in the cost of coal rising 28.6 percent more than oil, while the price of natural gas will rise by 23.4 percent less than natural gas.[150] Put differently, if an energy consumer pays $1 as the price of carbon in a unit of oil consumed, then she has to pay about $1.29 for the carbon in an equivalent amount of coal, but only about $.77 for the carbon contained in the equivalent amount of natural gas. Carbon-intensive fuels thus become more expensive relative to their low-carbon colleagues, in theory inducing environmentally desirable fuel switching.

Unfortunately, this logic breaks down once one thinks about the way in which energy institutions are functionally linked to the UNFCCC and its objective of pricing GHG emissions. The price of any particular fuel can be influenced by a wide variety of factors, including investment, transit issues, and most importantly for our purposes, legal rules impacting the supply of a particular fossil fuel on the market.

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[145] UNFCCC art 7.2(k).
[146] UNFCCC art 18. Not all institutions give states equal votes. Some, like the World Bank and the IMF, employ weighted voting. *See* Jacob Katz Cogan, *Representation and Power in International Organization: The Operational Constitution and its Critics*, 103 Am. J. Int'l L. 209 (2009).
[147] UNFCCC art 2.
[148] It is of course not exclusively an energy regime, dealing also with adaptation, technical and financial assistance to developing states, and even intellectual property issues.
[149] Garry J. Bertrand, *Carbon Taxation and Unexpected Switching Behavior*, OPEC Review 1, 3(1995).
[150] *Id*.

The climate change regime's ability to induce fuel switching therefore depends critically not only on broader market dynamics, but also on the international institutions that influence the functioning of those markets.

Moreover, unlike the climate change regime, most other energy institutions have either opposed or at least more complicated objectives in relation to the price of fossil fuel. These objectives are the source of systemic governance risk. I first discuss the way systemic governance risk in energy manifests itself. I then turn to examining why states prefer systemic governance risk in energy over institutional governance risk.

B. Systemic Governance Risk in International Energy

During the last several years, oil prices have been volatile and generally high. In 2008, the benchmark price of oil peaked at $146/barrel before subsiding. In response to supply disruptions in Libya in 2011, oil once again began climbing, reaching almost $127/barrel in April 2011 before again falling back nearly 10%. At the same time, market dynamics have kept the price of natural gas very low. It thus appeared in 2011 that market forces were working to encourage the price incentives that the climate change regime was designed to nourish and that would aid developed states in complying with their emissions reduction obligations under the Kyoto Protocol.

As discussed above, however, OECD countries – many of the same countries that urge aggressive action on climate change – are parties to the IEP Agreement, which aims to influence oil prices, especially during emergencies, thus mitigating the externality oil-consuming countries experience from coordinated production and trade governance by oil-exporting countries under OPEC's auspices. The IEP Agreement thus provides an institutional mechanism by which OECD countries can lower the cost of oil in one regime, even as they try to raise the cost of oil in another!

The IEP Agreement and the way it is implemented, increase the cost of compliance with the climate change regime by reducing the price of oil in two ways. First, econometric analysis has shown that higher oil reserves in developed countries tend to reduce the price of oil globally.[151] Thus, the mere fact that the IEP Agreement requires states to stockpile oil has a depressing effect on the price of oil. Second, the activation of CERM and the release of oil from the strategic reserves creates greater liquidity in oil markets, thereby reducing oil's price. The most recent release occurred in June 2011. At that time, IEA members released 60 million barrels, resulting in a single-day drop of 7.4% in the benchmark price of crude oil.[152]

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[151] *See, e.g.*, Robert K. Kaufmann, Stephane Dees, Pavlos Karadeloglou, & Marco Sanchez, *Does OPEC Matter? An Econometric Analysis of Oil Prices*, 25 Energy J. 67 (2004); [OTHER CITES].

[152] Liam Denning, "A Coalition Strike on Oil Markets," Wall Street Journal, at C8 (June 24, 2011). Due to the multiple forces at work in oil markets, forecasting the long-term effect of the release on oil prices can be difficult.

The result is that climate-friendly states such as Germany, Britain, France, and even the United States under the Obama administration, took action under the IEP Agreement that directly undermined the climate regime's price objectives at the same time those nations were working to put in place a successor agreement to the Kyoto Protocol. This is not to say, of course, that anything done under the IEP conflicts with any legal obligations states have under the UNFCCC or the Kyoto Protocol. Rather, both institutions seek to regulate energy markets by influencing the price of fossil fuels in different directions.

Of course, in theory, IEA states could attempt to coordinate their oil supply policies with longer-term climate policies. They could, in other words, try to cooperate across institutions. The division of institutional authority between the UNFCCC and the IEP/IEA complicates such an effort in a number of ways. First, membership between the two institutions does not overlap perfectly. The UNFCCC has 194 members states while the IEA has 28. The UNFCCC operates by consensus; the IEA often makes decisions by consensus although formally it employs a weighted voting system based on oil consumption levels in 1974.[153] Perhaps most importantly, on the issues within its jurisdiction IEA member-states are like-minded, while within the UNFCCC there are enormous epistemic and normative divisions. Collectively, these issues make it extraordinarily difficult for IEA members to obtain coordinated policies across the two institutions that would surpass the benefit they get from making uncoordinated decisions. In effect, trying to coordinate the decisions would impose costs on IEA members that would likely not be justified by the resulting coordinated policy. Second, different domestic agencies may take the lead in different institutions, such that even if membership in the two institutions did overlap perfectly there still could be a failure to coordinate at the domestic level. Although some countries have ministries of energy and climate, countries like the United States bifurcate the Department of Energy from the Environmental Protection Agency and the Department of State

C. Why Choose Narrow Jurisdiction in Energy Matters?

The fact that multiple institutions influence the price of fossil fuels is a critical source of systemic governance risk. Viewing the institutional environment we face today, it may seem obvious that an institution such as the UNFCCC should be created to deal with the environmental side effects of energy consumption. After all, domestic regulatory structures often divide among different agencies direct regulation of an economic activity and the regulation of its environmental consequences.[154] But it is not at all obvious from an initial standpoint that a new institution was necessary.

[153] *Consumer Country Energy Cooperation*, in Global Energy Governance: The New Rules of the Game (Andreas Goldthau & Jan Martin Witte, eds. 2010).
[154] Freeman & Rossi, Harvard Law Review (2012).

Most of the major emitters in the world in 1992 were OECD countries and therefore members of the IEP Agreement and the IEA. A plan to reduce global emissions through binding legal obligations applicable only to developing countries – in other words, an agreement very similar to the Kyoto Protocol – could thus have been worked out through the OECD as an amendment to the IEP Agreement. Such an arrangement would have had the benefit of allowing closer coordination between developed countries' general energy consumption policies and their climate change-specific efforts.

Instead, nations opted for a UN organization open to, and consisting of, all states. There are a number of sensible reasons to have created a new organization to deal with climate change that is open to all states and operates by consensus. Most notably, climate change is a problem that affects all nations to one degree or another, and so universal participation might be thought necessary to confer legitimacy on the institution. Relatedly, solving the climate change problem in the long run requires the participation of developing countries such as China and India that are not members of the IEA. Therefore, a climate change regime based in the OECD might not have seemed a feasible long-term solution due to participation problem. Finally, the architecture of the UNFCCC/Kyoto Protocol was based to a large extent on the successful Vienna Convention/Montreal Protocol framework that governing ODS. Viewing climate change as an environmental problem and an air pollution problem specifically, it was perhaps natural to look for examples of successful air pollution institutions upon which to base the climate change regime.

But part of any decision to create a new organization to deal with climate change must take into account the effect of bargaining within the institution, including considerations of its jurisdiction, both in terms of membership and issues, and its procedural rules. Nations regularly negotiate global accords to exclusive bodies precisely to influence the bargaining process by removing potential holdouts. The OECD has several times tried to negotiate a multilateral agreement on investment, for example, precisely because doing so within the OECD allows member-states to present other states with a take-it-or-leave-it offer.[155] The EU and WTO have expanded in similar fashion. So there is no particular reason that the IEP Agreement could not have been used as a vehicle to negotiate a climate change regime nested within a broader energy institution. Indeed, today there are calls for the IEA to consider expanding to include non-OECD countries such as India and China, based purely on the rise of China and India as energy consumers. Linking climate change to energy consumption with the IEA would thus have complemented, rather than distorted, the historical pressures on the IEA to expand.

The decision not to expand the IEA, either in terms of issue jurisdiction or membership, most likely reflects a preference among IEA members for systemic governance risk over institutional governance risk. Linking climate change policies to general energy consumption policies would introduce distributional

[155] *Codifying Custom*, *supra* note __, at __.

considerations unique to climate change to broader energy consumption policies. Most obviously, if the IEA expanded in membership to allow universal participation, current IEA members would find their ability to cooperate on energy consumption policies hostage to the resistance of OPEC countries to climate change policies. Within the climate change regime, OPEC countries have linked funding for adapting their economies away from oil-production to support for climate change measures. There is no reason to think that if allowed to participate in the IEA OPEC countries would not hold cooperation on energy consumption policies hostage to the same demands. Indeed, since the IEA's emergency stockpiles reduce the price of oil, arguably simply by their existence and certainly when released, OPEC would have a double incentive to be obstructionist. More generally, a key component of the climate change regime has been funding from developed nations to developing nations for adaptation and technical assistance. Many of these developing nations, however, suffer from severe energy poverty. Combining their pressure in the climate change regime for assistance with an energy institution with jurisdiction to coordinate consumption policies could result in IEA members eventually decamping to another institution to coordinate their energy consumption policies.

Even if the IEP Agreement did not expand its membership, including climate change measures within its ambit could disrupt cooperation between major energy consumers. As is well-known, the climate change regime suffers from divisions not only between developed and developing states, but also among developed states. While the European Union is eager to press ahead on climate change measures, the United States insists that no deal for legally binding emissions reduction measures should be struck until China and India are on board. Introducing this division over climate change measures into the IEP Agreement could threaten to embroil cooperation on energy security with disputes about how best to manage the environmental consequences of energy consumptions. Thus, even from the standpoint of developed countries, dividing jurisdiction for energy-related matters between the IEA and the UNFCCC marks a commitment to delink to a large extent bargaining over energy consumption measures from bargaining over climate change mitigation. The costs of coordinating across institutions thus animates governance on energy security at the expense of possible gains in the climate change regime.

Finally, although I have focused on institutions as sites of bargaining, it is significant to note one additional benefit from delinking issues that is related to administrative capacity: where states agree to fund an agency such as the IEA, extracting additional funding for specific priorities can be difficult. States, most notably the United States, are often unwilling to increase support for international organizations. Where international agencies are concerned, funding from governments is thus a major source of institutional governance risk. Delinking issues institutionally is a strategy to increase funding, by creating dedicated funding obligations. Put differently, linking issues within a single institutions supported by a single funding obligation tends to depress funding and can lead to new priorities going unfunded. Delinking issues institutionally allows the creation of separate funding obligations for member

states. Coordination costs across institutions are thereby increased, but institutional governance risk owing to weak funding obligations is decreased.

This logic played out during the creation of the new International Renewable Energy Agency (IRENA). When nations were considering whether to create a renewable energy agency, the question arose whether the "new" agency shouldn't take the form of an expanded mandate for the IEA. Such an expanded mission would also likely have entailed expanding IEA membership in some way. Ultimately, however, states decided to divide jurisdiction for renewable energy among the IEA and IRENA. Once again, this allowed OECD states to avoid the institutional governance risk that might arise from either admitting new states into the IEA or from introducing divisions over support for renewable energy into an institution focused primarily on coordinating consumption policies for fossil fuels. At the same time, however, it also allowed a dramatic increase in funding for renewable energy by providing funding obligations specifically tied to renewable energy priorities. While the IEA had seen virtually zero real growth in its budget over the last 25 years and allocates only about $500,000 to renewable energy policy research,[156] IRENA has already managed to assemble an annual operating budget that totals nearly $28 million in 2012.[157]

V. Conclusion

The fragmentation of international governance is one of the defining features of the international legal system and also one of the main challenges to successful international governance. Nowhere is this more clear than in the area of energy governance, where economic and environmental issues are regularly divided among different institutions. This fragmentation is particularly puzzling in light of the literature on issue linkages, which generally suggests that the jurisdiction of international institutions should be expanded to facilitate bargaining across issues. I have argued in this paper, however, that in many instances states will prefer to animate governance on isolated issues through fragmentation, rather than creating the possibility of comprehensive governance -- and its failure – in a single institution with broad jurisdiction. In short, fragmentation in international energy governance is a response to the possibility of holdout states using linkages institutionalized in the form of jurisdiction as a means of paralyzing governance. The result is that cartelized economic governance on energy issues continues, while comprehensive environmental governance is left behind.

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[156] Ben Block, *Interview with IRENA Director General Nominee Hans J␣rgen Koch*, WORLD WATCH INSTITUTE, http://www.worldwatch.org/node/6172 (last updated Apr. 9, 2012 8:34 PM).

[157] INT' 'L RENEWABLE ENERGY AGENCY, REP. OF THE DIR. GEN.: PROPOSED WORK PROGRAMME AND BUDGET FOR 2012 4 (Jan. 30, 2012), *available at* http://www.irena.org/documents/upload Documents/2assembly2012%2F2012WPB_A_2_1.pdf [hereinafter 2012 WORK PROGRAMME].These figures include IRENA's core budget (just over $13 million and $16 million in 2011 and 2012, respectively) as well as additional voluntary contributions from Germany and the United Arab Emirates. *Id*.