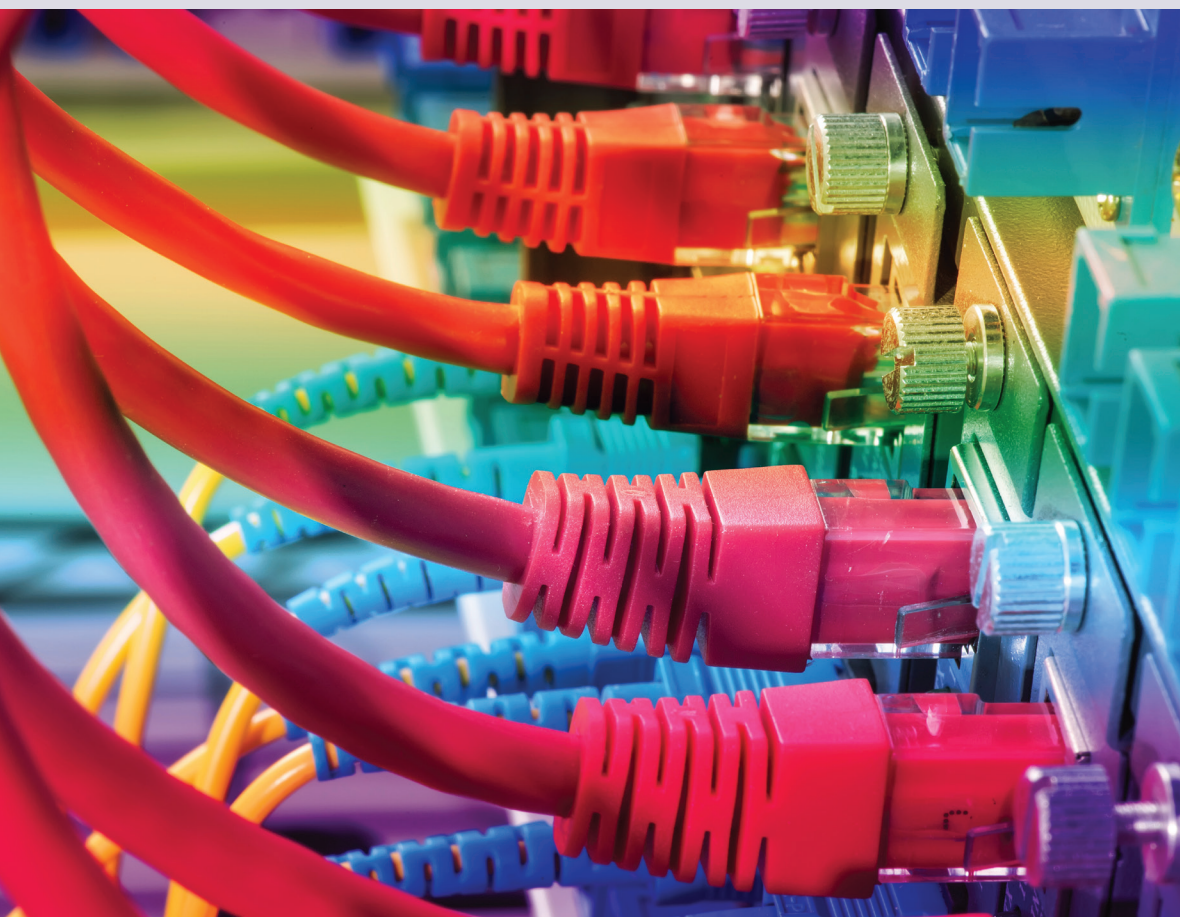


Future of the Global Trade Order

Edited by
Carlos A. Primo Braga and Bernard Hoekman



Future of the Global Trade Order

European University Institute (EUI)

Badia Fiesolana
Via dei Roccettini 9
I-50014 San Domenico di Fiesole (FI)
Italy
www.eui.eu

IMD

Ch. de Bellerive 23
P.O. Box 915
CH-1001 Lausanne
Switzerland
www.imd.org

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ISBN: 978-92-9084-410-5
doi:10.2870/560499
Catalogue number: QM-01-16-444-EN-N

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European University Institute (EUI)

The European University Institute (EUI), located in Florence, Italy, was founded in 1972 by the European Community Member States to provide advanced training to Ph.D. and LL.M. researchers and to promote research in the social sciences at the highest levels.

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About the Contributors

Nick Ashton-Hart has just concluded several years as the senior Geneva-based full-time representative of the technology sector to the UN, its member-states, and the international organisations in Geneva. He has participated in multilateral policy development since 1992, and international trade policy as it relates to the Internet and traditional industrial transformation for the last seven of those. He is currently an Associate Fellow of the Geneva Centre for Security Policy. Prior to founding IDEA, he was Geneva Representative of the Computer & Communications Industry Association (CCIA), Director at-Large and Senior Director for Participation and Engagement with the Internet Corporation for Assigned Names and Numbers (ICANN) and Executive Director of the International Music Managers Forum (IMMF).

Clemens Boonekamp is an Associate Partner at the IDEAS Centre in Geneva. Previously he was Director of the Trade Policies Review Division and then of the Agriculture and Commodities Division at the WTO. Before that he had been a Senior Economist at the IMF and an Assistant Professor at the University at the University of British Columbia. He holds a Ph.D in Economics from Brown University.

Simon J. Evenett is Professor of International Trade and Economic Development at the University of St. Gallen, Switzerland, and Co-Director of the CEPR Programme in International Trade and Regional Economics. Evenett taught previously at Oxford and Rutgers University, and served twice as a World Bank official. He was a non-resident Senior Fellow of the Brookings Institution in Washington. In addition he served as a Member of the High Level Group on Globalisation established by the French Trade Minister Christine LaGarde, Member of the Warwick Commission on the Future of the Multilateral Trading System After Doha, and was Member of the the Zedillo Committee on the Global Trade and Financial Architecture. In addition to his research into the determinants of international commercial flows, he is particularly interested in the relationships between international trade policy, national competition law and policy, and economic development. He obtained his Ph.D. in Economics from Yale University.

Johannes Fritz is a Ph.D. candidate and a member of the Global Trade Alert team at the Swiss Institute for International Economics and Applied Economic Research, University of St. Gallen, Switzerland. He studied International Affairs in St. Gallen, Geneva and Barcelona, and is currently enrolled in the Ph.D. Program in Economics and Finance at St. Gallen.

Bernard Hoekman is Professor and Director of Global Economics in the Global Governance Programme of the Robert Schuman Centre for Advanced Studies, European University Institute, and a CEPR Research Fellow. Prior positions include Director of the International Trade Department (2008-2013) and Research Manager of the trade team in the Development Research Group (2000-2008), both at the World Bank. He worked as an economist in the GATT Secretariat during the Uruguay Round of negotiations. His research focuses on trade and development, international trade agreements, trade in services and international regulatory cooperation. He is a graduate of the Erasmus University Rotterdam, holds a Ph.D. in Economics from the University of Michigan and is a Senior Associate of the Economic Research Forum for the Arab Countries, Iran and Turkey.

Alejandro Jara, a Chilean national, is Senior Counsel with King & Spalding in Geneva. He joined the Chilean Foreign Service (1976) specializing in trade policy, and served in the Chilean Delegation to the GATT in Geneva (1979-1984). From 1993 to 2000 he served as Director for Bilateral and Multilateral Economic Affairs, and Director General for International Economic Relations; as well as Senior Official to APEC and negotiated several Free Traded Agreements (Mexico, Canada, Colombia, Central America). While Ambassador of Chile to the WTO (2000-2005) he chaired the Services Negotiations of the DDA. Between 2005 and 2013, he served as WTO Deputy Director General.

Carlos A. Primo Braga is currently an Associate Professor at Fundação Dom Cabral, Brazil and Managing Director, Ouchy Consultoria Empresarial Ltda, São Paulo, Brazil. He is also a Visiting Professor at IMD, Switzerland. Over the period 2012-2015, he was Professor of International Political Economy at IMD and Director of the Evian Group@IMD, an international coalition of corporate, government and opinion leaders, united by a common vision of enhancing global prosperity by fostering an open, inclusive and equitable global market economy. Before joining IMD in 2012, he was the Special Representative and Director for Europe, External Affairs (EXT) Vice-Presidency, The World Bank (2011-2012). At the World Bank he was also Director, Economic Policy and Debt (2008-2010) and, in 2010, he was the Acting Vice President and Corporate Secretary of the World Bank Group and Acting Executive Secretary of the IMF/World Bank Development

Committee. He was a Fulbright Scholar (1988-1989) and visiting professor (1988-1998) at the Paul Nitze School of Advanced International Studies, an Assistant Professor of Economics at the University of São Paulo (1984-1991) and Senior Researcher at FIPE, São Paulo. He holds degrees in Economics (Ph.D., University of Illinois at Urbana-Champaign; MA, University of São Paulo) and Mechanical Engineering, ITA; Brazil.

Miguel Rodriguez Mendoza is a Senior Associate to the Geneva-based WTI Advisors Ltd, and works as a consultant on a number of projects of the Inter-American Development Bank (IADB), and the UN Conference on Trade and Development (UNCTAD), among others. From 2005 to 2014 he was a Senior Fellow at the International Centre on Trade and Sustainable Development (ICTSD), a non-governmental organization that focus on the relationship between trade policy and sustainable development. He served as Deputy Director-General of the WTO between November 1999 and October 2002. After that, he led the Geneva office of Van Bael & Bellis, a Brussels-based international law firm that specializes in EU and international economic law, and also worked as a Special Adviser to the President of the Andean Development Corporation (CAF), a Latin American development bank. He has been panelist in various WTO disputes, and before establishing in Geneva he was Chief Trade Advisor at the Organization of American States (OAS) and, as such, provided advice to countries during the Free-Trade Area of the Americas (FTAA) negotiations. Between 1991 and 1994, he was Minister of State and President of the Institute of Foreign Trade, Venezuela's governmental body responsible for the country's trade policies.

Giorgio Sacerdoti has been a tenured Professor of International Law at Bocconi University in Milan since 1986, where he currently teaches International Trade and Investment Law, two aspects of international economic law on which he has lectured and written extensively in his career. He was a member of the WTO Appellate Body from 2001 to 2009 and its Chairman in 2007-2008. He was previously the Vice-Chairman of the OECD Working Group on bribery and one of the drafters of OECD Anti-bribery Convention of 1997. He is active as a consultant in trade matters and as an arbitrator, especially in investment disputes, being often appointed as an arbitrator and president of investment tribunals at ICSID and under other arbitration rules.

Foreword

The inability of WTO Members to conclude the Doha Round has led many to question the effectiveness of one of the major pillars of global governance and the commitment of governments to multilateralism. As argued in the contributions to this volume, the performance of the international trade order is in fact much better than it is perceived to be. The WTO has enhanced the rule of law in commercial policy, as exemplified by its effective and unique dispute settlement mechanism. The trade order has also proven capable of accommodating large new trading nations, most notably China.

Major shifts in economic power balances since the creation of the WTO in 1995 lie at the heart of the failure of the Doha Round and the turn by countries towards preferential trade agreements. These increasingly address areas of policy that are not covered, or are covered only tangentially, by the WTO, and raise important questions regarding the future of the world trade order. The contributors to this book make a strong case that it is past time that WTO Members move away from a business as usual approach, but also demonstrate that there are strong incentives for multilateral cooperation on both longstanding policy concerns – such as agricultural support policies – and new challenges associated with the global governance of the digital economy.

The original idea for this book came from debates about the future of the WTO in which the editors have been engaged over the last few years. The book was designed also to serve as a reference text for the International Trading System program offered by IMD, which involves several of the authors that contributed chapters for this publication. Comments and suggestions from Stuart Harbinson, Abdel-Hamid Mamdouh, and Victor do Prado, among many others, were extremely helpful. Last but not least, funding from IMD's Research Department and Philip Morris International, as well as the professional editing provided by Anil Shamdasani, are gratefully acknowledged.

I am very pleased that the Global Governance Programme at the Robert Schuman Centre for Advanced Studies has been a partner in this effort and contributed to bringing this project to completion.

Brigid Laffan
Director, Robert Schuman Centre
European University Institute

CHAPTER 1

Future of the Global Trade Order

Carlos A. Primo Braga and Bernard Hoekman

IMD and Fundação Dom Cabral;
European University Institute

The global economy is going through major economic and geopolitical shifts. The balance of economic power between the established powers of the North and the emerging “new” ones of the South has changed, not only fostering tensions in the global governance structure that has characterized the post-World War II era – centered around the Bretton Woods institutions (the IMF and the World Bank), the GATT/WTO and the Security Council of the UN – but also leading to new alliances among emerging economies.

The typical narrative for economic and geopolitical trends in the 21st century involves considerations about the impact of globalization, the role of disruptive technologies in changing the economic landscape, as well as the terms of international competition, and the growing economic relevance of emerging economies. These economic considerations are often complemented by geopolitical considerations focusing on the relative “decline” of the United States and the rapid economic ascendancy of China.

This collection of papers looks into one of the main pillars of global governance: the multilateral trade system, anchored by the World Trade Organization (WTO). Membership at the WTO requires credible market-oriented economic policy credentials – it’s tough to get in and accession by new Members invariably requires significant reforms. In 2016, the WTO will reach at least 164 Members (as the accession of Afghanistan and Liberia are completed), with a number of countries still in the accession process. It is close to reaching universal coverage of trading nations – a stark contrast to the original 23 members of the GATT in the 1940s. The accession of China

to the WTO in 2001 will probably remain as one of the landmark trade developments of the 21st century.

The year China acceded to the WTO is the same year the Doha Development Agenda (DDA) – the first round of multilateral trade negotiations in the WTO era – was launched, following eight earlier rounds conducted under the GATT. Almost 15 years later negotiations are formally still ongoing, but in spite of some progress at the Bali Ministerial in 2013, the conclusion of the negotiations remains a distant goal. The 2015 Nairobi Ministerial Declaration is a noteworthy example of “constructive” ambiguity, underscoring the deep divisions that now characterize the WTO Membership with respect to the DDA. Its Article 30 states that “many Members reaffirm the Doha Development Agenda, and the Declarations and Decisions adopted at Doha and at the Ministerial Conferences held since then, and reaffirm their full commitment to conclude the DDA on that basis. Other Members do not reaffirm the Doha mandates, as they believe new approaches are necessary to achieve meaningful outcomes in multilateral negotiations.”

The long dragging DDA has had a negative effect on the reputation of the WTO. The private sector in particular seems increasingly frustrated with the multilateral trade system, but civil society groups are also disenchanted with lack of progress in addressing issues of interest to them. There is a general perception that WTO disciplines and modus operandi are outdated and have not kept pace with globalization. Unsurprisingly, some observers are even asking whether the WTO is worth “saving.”

This is the wrong question. The DDA talks are just the tip of the “iceberg” that encompasses a much broader set of WTO functions. Even if the DDA were to fail – and as indicated above, some WTO Members take the view that it has failed – the WTO would continue to play an important role in fostering transparency in trade practices, monitoring and enforcement of existing multilateral rules and agreements, and providing dispute settlement services. Notwithstanding the difficulties of the DDA, following the 2008 global financial crisis the WTO made a contribution to the world economy by disciplining trade protectionism and helping prevent the Great Recession morphing into a Great Depression à la 1930s.

One consequence of the DDA deadlock is that trade liberalization and new trade rules are increasingly being negotiated in the context of preferential trade agreements (PTAs). In 1990, there were roughly 70 active PTAs; today there are more than 300. The interest in PTAs is not limited to issues on which the DDA cannot make progress. Many of the matters that are on the table in PTAs are driven by deeper integration objectives that often have WTO-plus

characteristics. This is the case for many policy areas, including protection of intellectual property rights (IPRs), mutual recognition or harmonization of “behind-the-border” regulations, liberalization of investment flows and provisions on investor protection, to name just a few. The new mega-PTAs that are being pursued by major OECD member countries, such as the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP), are better attuned to the needs of transnational corporations and the dynamics of international trade in the 21st century than is the WTO.

This collection of papers looks into possible future scenarios for the multilateral trade system. They focus on some of the major critical issues that confront the WTO Membership and the stakeholders in the multilateral trading system. As mentioned by Miguel Rodriguez in Chapter 2, one could argue that the WTO is currently facing an “adaptability” crisis. This is nothing new in the history of the multilateral trade system. Actually, a similar crisis occurred in the 1980s during the Uruguay Round negotiations (1986-1994), which led to the GATT morphing into the WTO with an associated increase in the number of policy areas covered by multilateral rules of the game.

In a nutshell, the creation of the WTO was made possible by a bargain that involved the inclusion of two new agreements under the multilateral system of trade governance (GATS and TRIPS), a priority for industrialized nation negotiators, in exchange for new disciplines for agricultural trade and the dismantling of the system of quotas that governed textile and clothing trade (the MFA), priorities for most developing countries. The history of the “marriage of convenience” between traditional trade policies and the inclusion of new policy areas such as services and protection of IPRs illustrates the capacity of the multilateral trade system to adapt over time.

IPRs are territorial by nature (i.e. the rights are awarded and enforced at the national level) and attempts to promote harmonization and coordination across countries can be traced back to the 19th century.¹ International conventions (the Paris Convention in 1883, the Berne Convention in 1886, and so on) in this area typically adopted national treatment provisions as the basic standard for international harmonization. As international trade in knowledge products and foreign direct investment (FDI) flows expanded significantly in the post-World War II era, conflicts between innovators (at the level of countries and enterprises) and imitators began to increase.

1 This section on IPRs relies on Primo Braga (2016).

Already in the 1970s, the United States began to push for the adoption of an Anti-Counterfeiting Code at the level of the GATT. This effort – launched in the final stages of the Tokyo Round (1973-1979) of multilateral trade negotiations – was driven by the lobbying of trademark-holding companies, which were trying to limit counterfeited products in international trade. This attempt did not succeed, but it signaled the way of the future for innovation-leading nations – in particular, the United States. When the eighth round of multilateral trade negotiations (the Uruguay Round) under the GATT started in 1986, the strategy was refined to go beyond anti-counterfeiting with a view to establishing minimum standards of protection and enforcement across a broad array of IPRs instruments. The appeal of this approach was to connect the strengthening of IPRs protection to the broader trade agenda and to provide access to the dispute settlement mechanism of the multilateral trade system. Most developing countries, in turn, preferred the World Intellectual Property Organization (WIPO) as the institutional locus for IPRs discussions. The lack of effective enforcement powers in the WIPO conventions, however, is often presented as the reason behind the US efforts in favor of a GATT-related solution.² This time the strategy succeeded, leading to the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

A similar dynamic occurred with services. As was true for IPRs, there were no multilateral disciplines on trade in services in the GATT. Services were put on the GATT agenda in the early 1980s by the United States, which had a significant surplus in its balance of trade in services, as opposed to running a deficit for trade in merchandise. This led to a process of reflection and the preparation of a series of national studies on the state of play for trade in services and the possible benefits of developing rules for services trade. The suggestion to expand the coverage of the trading system to encompass services was controversial, however, and many developing countries, including Brazil and India, were initially of the view that the Uruguay Round should not address services. At the ministerial meeting that launched the Uruguay Round negotiations, it was agreed – based on a compromise proposed by Colombia and Switzerland – that services negotiations would proceed on a parallel track.

The agreement that was eventually negotiated was innovative in defining trade in services very broadly, including FDI and provision of services through temporary movement of natural persons, and permitting countries to make (or not make) specific commitments for sectors and the different modes of supplying services across borders. The main result was to establish a framework for future rule-making and liberalization. Few commitments were made by

2 See Kastenmeier and Beier (1989) and Primo Braga (1990, 1996).

countries to open their services markets – the main result was to expand the coverage of the trading system but to do so in a way that allowed for great flexibility by countries as to how much to do in the way of making market access opening commitments. This was left to future negotiations, which were to start within five years of the entry into force of the WTO. In the event, new services negotiations became an element of the DDA.

The relative success of those advocating stronger protection of IPRs at the global level via the negotiation of trade agreements, and the expansion of the WTO to include trade in services, however, did lead to reactions from affected countries. This was particularly the case with respect to the impact of TRIPS on access to medicines amid public health crises, as underscored by the HIV/AIDS epidemic. This reaction, in turn, led to some adjustments at the multilateral level as illustrated by the Doha Ministerial Declaration (2001), the related Declaration on the TRIPS agreement and public health, and subsequent decisions/waivers on compulsory licensing with special emphasis on the needs of least developed countries.

Industry groups from innovation-led countries, however, continued to lobby for the inclusion of IPRs chapters in trade agreements, focusing on preferential trade negotiations. As discussed in detail by Fink (2012), the new generation of PTAs negotiated by the United States – starting with NAFTA – typically included “TRIPS-plus” provisions. The European Union also followed a similar track. Moreover, IPRs provisions became standard in bilateral investment treaties entered both by the United States and the European Union with other nations.

The latest major development in this area is the Trans-Pacific Partnership (TPP) agreement recently negotiated – but not yet ratified – by 12 countries in the Pacific Rim. The TPP agreement heralds a new era in terms of trade governance. It can be argued, for example, that at least in the medium term, the mega-regionals are eroding the relevance of the multilateral trade system and the WTO. TPP may also have a significant impact on the organization of global value chains (GVCs), as it will introduce more liberal rules-of-origin (the “accumulation of origin” concept) facilitating the operation of GVCs across its members.

Not surprisingly, one of the most controversial chapters of the agreement concerns its IPRs provisions. The United States put emphasis on longer terms of copyright protection, regulatory changes that would effectively translate into longer patent terms and constrain the entry of generic drugs into these markets, as well as additional rules for biologic medicines (pharmaceutical

products developed from living organisms), including minimum standards for data protection.

The final terms of the TPP agreement did not deliver on all the demands of the US negotiators. Still, several of these “TRIPS-plus” measures were adopted. Some noteworthy measures adopted in the TPP agreement include: trademark terms of protection of no less than 10 years (TRIPS requirement is of seven years) and the removal of barriers for the protection of sound marks; a minimum copyright term of protection of at least 70 years (TRIPS minimum standard is 50 years) and stronger copyright enforcement (including the possibility of criminal prosecution against acts of removal of rights management information and the requirement that TPP countries be signatories of WIPO “Internet treaties”); requirement of enforceable legal means for the protection of trade secrets (TRIPS does not specify these means); protection of undisclosed test data submitted for marketing approvals (at least 10 years in the case of agricultural chemicals and five to eight years in the case of pharmaceuticals, TRIPS does not have such a requirement); the explicit protection of new pharmaceutical products that are or contain a biologic (the TPP is the first trade agreement to do this);³ and adjustment for patent office delays in the granting of patents that will promote harmonization of patent granting practices among TPP parties.

Some of these provisions go beyond the “TRIPS-plus” aspects that the United States had already negotiated on a bilateral basis in the context of its FTA treaties with countries such as Australia, Chile and Peru. In short, TPP – once ratified – will provide for higher standards of IPRs protection that better reflect existing US law.⁴ Inevitably, some of these provisions have generated significant controversy, even among like-minded countries. One concern is that it may “export” to other countries the flaws of the US IPRs system with its emphasis on litigation – as illustrated by the growing role of non-practicing entities, or NPEs (i.e. entities that focus on licensing and litigation of IPRs rather than production and innovation) – and strategic behavior to block the introduction of generic drugs.⁵

3 In the United States, a biological product is defined as a “virus, therapeutic serum, toxin, antitoxin, vaccine, blood, blood component or derivative, allergenic product, protein (except any chemically synthesized polypeptide), or analogous product, or arsphenamine or derivative of arsphenamine (or any other trivalent organic arsenic compound), applicable to the prevention, treatment, or cure of a disease or condition of human beings.” See BIO (2013) for further details.

4 One major exception – reflecting resistance from other TPP parties – was the term of regulatory data protection for biologics. In the United States, this term is of at least 12 years from the date of approval. Article 18.52 of the TPP provides only for an eight-year term of protection. For further details see ITAC-15 (2015).

5 For an excellent discussion of NPEs and strategic manipulation to delay the introduction of generic drugs in the United States, see Feldman (2016).

Other topics that contribute to the “sense of malaise” that currently characterizes the multilateral trade system include the lack of progress in services negotiations at the multilateral level and the perception that the WTO is not well equipped to deal with new themes such as policies affecting the operation of GVCs, digital trade and e-commerce, and environmental issues, to name just a few.

Services figured much less prominently in the DDA than in the Uruguay Round, reflecting a decision by negotiators to first determine what the contours of a possible DDA deal could be for trade in agricultural and industrial products. This in turn can be explained in part by the fact that international businesses were less active in pushing for making the services agenda a priority. The inclusion of services on the Uruguay Round agenda owed much to the proactive efforts of services providers, including large transnational companies such as American Express. Such firms were much less engaged in the DDA. Whatever the reason, services talks made little progress, and at the 8th WTO Ministerial Conference in December 2011 it was agreed that WTO Members should pursue talks in parallel to the DDA with the aim of reaching “provisional or definitive agreements based on consensus earlier than the full conclusion of the single undertaking.” This led to the launch of negotiations in 2012 on an agreement on trade in services (TiSA) outside the WTO.⁶ Thus, services – which represent 70% or more of the GDP of many economies and are the most dynamic category of global trade growth (and trade growth potential) – were essentially taken off the WTO table. They now figure mainly in mega-regionals and in the TiSA negotiations. These efforts do not include most of the major emerging and developing economies, who have the most to gain from policy reforms and that offer the greatest prospects to generate an increase in trade flows. For the global trading system, much will depend on whether participants in the TiSA decide to make the outcome a PTA or, instead, inscribe the results of the negotiations into their GATS schedules of commitments and make the TiSA a so-called “critical mass agreement.” From a trading system perspective, the latter would be an important boost; making the TiSA a PTA would in contrast be a major blow.

The shift to a PTA-centered trade strategy by many major high-income countries is not just a result of the difficulties that have been experienced in getting to “yes” on the DDA, it also reflects the increasing complexity of dealing with the spillover effects of a broad set of policies affecting GVC trade, and

6 The TiSA includes Australia, Canada, Chile, Chinese Taipei, Colombia, Costa Rica, Hong Kong China, Iceland, Israel, Japan, the Republic of Korea, Mexico, New Zealand, Norway, Panama, Paraguay, Pakistan, Peru, Switzerland, Turkey and the United States.

the changing composition of trade as technology supports a rapid increase in trade in services and associated cross-border data flows.

The structure of international trade has changed in recent decades as a result of the increasing fragmentation of global production that is associated with global value chains. A GVC involves a collection of firms (plants) located in different countries jointly forming a “production line,” with different parts of the production process undertaken by firms (plants) in different countries. Depending on the location of a firm (country) in a GVC, participation may either involve forward linkages, where an activity produces an output that is used in production for export in another nation, or backward linkages, where a firm uses imported parts and components that are inputs for production that is exported. An example is country *A* producing hides from cattle that are tanned and dyed in a neighboring country *B* using chemicals imported from a third country *C*, with the leather produced in *B* used in the production of a car seat cover in country *D* that is used by a car plant located in country *E* that exports the cars to country *F*.

A GVC permits enterprises in different countries to concentrate on (specialize in) specific tasks and activities without having to source required inputs locally or to vertically integrating to produce and market the end product. GVCs increase interdependence – each link in a chain relies on the upstream producers delivering their output on time and meeting the required quality and safety standards, whereas upstream firms are dependent on the downstream segments working efficiently, as stoppages or distribution problems there will affect the demand for inputs. The growth in GVCs has been accompanied by greater cross-border movement of capital and knowledge, as well as workers.

GVCs span a huge variety of firms, ranging from SMEs that provide a variety of inputs, to logistics providers, processors, manufacturers and service suppliers. While large multinational lead firms decide where to locate plants, where to invest and who to source from and how, these lead firms source inputs and buy services from numerous local suppliers and subcontractors that provide a range of goods and services. Much of the value added that is embedded in a product reflects the payments for intermediate goods and services. Thus, a wide range of firms and sectors, including companies providing services to firms in other sectors, benefit from and are affected by GVC-based trade and investment decisions. Available data indicate that about one-third of the value of all traded manufactured goods reflect the value of embodied services, and that, overall, if account is taken of sales of services by foreign affiliates, services account for more than 50% of world trade (Francois and Hoekman, 2010).

The structure and volume of GVC trade is very sensitive to operating and transactions costs. This makes a wide range of policies relevant, both policies that impact directly on financial and operating costs and policies that affect the reliability and predictability of flows within GVC networks. Uncertainty and (risks of) delays associated with unpredictable operating environments give rise to a need to maintain higher stocks and other forms of hedging and insurance, the costs of which may preclude supply chain-related investments.⁷

An open trade regime matters for GVCs, but equally important are actions to minimize trade frictions, such as delays in border clearance and low-quality transport and logistics that lead to physical losses, and to facilitate investment in operating or distribution facilities. Connectivity – including the quality of transport and logistics services and information and communications technology (ICT) networks and related services – is often critical. The policy agenda becomes more complex, spanning many areas that may not be covered by the WTO, or only partially. For example, very specific types of government intervention may be needed to address coordination failures that negatively affect GVCs, but at the same time such measures may have negative spillover effects on other countries.

Challenges Looking Forward

The most immediate challenge confronting the WTO as an institution is to move on from the failed DDA negotiations. This may entail greater reliance on variable geometry – agreements and cooperation between clubs of countries. The revealed preference for PTAs illustrates that club-based cooperation is the revealed preference of many countries. The task for the WTO is to channel more of the energy that currently is invested in PTAs towards rule-making under the WTO umbrella. Necessary conditions for this to occur are deliberation on both old and new policy areas that generate negative externalities and call for concerted action and cooperation, and more collective learning about the experiences of PTAs in dealing with these policy areas. The 21st century agenda confronting the WTO centers on “behind-the-border” regulatory policies as well as “legacy” 20th (or, indeed, 19th) century issues such as remaining tariffs. Reducing the market-segmenting effects of differences in regulations is difficult because of concerns that it may compromise the attainment of regulatory objectives (a “race to the bottom”). Identifying areas of regulation that could be the focus of cooperation in the WTO requires discussion and deliberation,

7 See Hoekman (2104) for an extensive discussion.

with active participation of the business community, policy research institutes and international regulatory networks.

Numerous observers have argued that cooperation on regulatory “behind-the-border” policies cannot occur between 163+ countries.⁸ An implication is that the WTO Membership may need to accept greater small group cooperation *inside* the organization as opposed to leaving the field to PTAs.

Movement in this direction has already been occurring, and indeed, has always been an element of cooperation in the GATT/WTO. Recent examples of agreements between only a subset of the WTO Membership include the Information Technology Agreement (ITA), ongoing negotiations on an agreement on environmental goods, and past agreements on basic telecommunications and financial services that were incorporated into the GATS. As noted above, it is possible (and desirable) that the TiSA become another example. A key feature of these agreements is that benefits extend to all countries, not just those that sign them – they are so-called “critical mass agreements.”

Another challenge for the WTO as an organization concerns the need to establish and deepen partnerships and harness complementarities with other international organizations dealing with trade policy, and the international business community. Greater engagement with business organizations is necessary for better economic governance, not least because of GVCs, which increase the interface between private and public international law; are giving rise to transnational initiatives among firms to agree on norms and standards; are an element of corporate social responsibility initiatives; and a focal point for public and private capacity-building programs, to name just a few dimensions of the governance dimensions associated with GVCs. Public-private partnerships are now commonplace when it comes to investment projects and the operation of (segments of) GVCs. The purely state-to-state nature of WTO operations is increasingly outdated.

Many international organizations, regulatory networks and standards-setting bodies play a role in creating the governance frameworks for policy areas that impact on trade and investment. The WTO is in many respects a weak organization in comparison with the multilateral development banks, the IMF, the OECD, and so forth when it comes to its mandate and financial resources to undertake monitoring, research and analysis, engage in policy dialogue and advisory services, capacity-building, etc. There are many “linkages” between

8 Baldwin (2016), for example, suggests that world trade governance is likely to evolve into a two-pillar system, with the WTO focusing on traditional trade issues and the mega-preferentials dealing with disciplines for GVCs, capital flows, enhanced protection of IPRs, and so on.

the domain of the WTO and the areas of activity of other institutions. Examples include sectoral regulation and associated international efforts and networks through which regulatory cooperation is pursued; governance of (multinational) business and associated GVC-based production and trade (including private product and production standards, labeling and traceability requirements, etc.); mega-regional PTA-based initiatives in areas of direct relevance to the trade order (e.g. the proposal by the European Union to establish a permanent investment court); as well as the regimes governing international financial flows and exchange rate policies.

Mention should be made here of the UN system as well, in particular as it relates to the achievement of the Sustainable Development Goals (SDGs). Trade is mentioned as an instrument to achieve some of the SDGs, including by correcting distortions in world agricultural markets, improving Aid for Trade support for developing countries, regional and trans-border infrastructure investments, and increasing the integration of small-scale enterprises into GVCs. An open, rules-based, non-discriminatory multilateral trading system and doubling the LDC share of global exports – in part through the timely implementation on a lasting basis of duty-free, quota-free market access – are other instruments identified in the document presenting the SDGs (United Nations, 2015).

Hoekman (2015) suggests the adoption of a trade cost reduction goal would help to leverage trade to achieve the SDGs. Reducing trade costs benefits both exporters and importers as well as households in developing countries. A trade cost reduction target would also encourage governments to identify actions that will do the most to facilitate trade, including in areas that are not covered by the WTO. There are many reasons why costs may be high, including own trade policies of developing economies, a lack of trade facilitation and weaknesses in transport and logistics services. A trade cost reduction target leaves it to governments to work with stakeholders to identify how best to reduce prevailing excess costs – thus encouraging the type of public-private partnerships and cooperation with other organizations discussed above.

Conclusion

The inability to get to “yes” in the DDA does not imply a lack of relevance of the WTO. Multilateral negotiations have become more complex because developing countries are more active and engaged in pursuing their objectives. PTAs may well be more effective mechanisms to address matters of a regulatory nature, or that involve the liberalization of politically sensitive areas such as the

movement of people. It is noteworthy that some PTAs address matters such as labor and environmental standards and include a focus on human rights, rule of law and other dimensions of public governance. These are areas of policy that are not covered, or covered only tangentially, by the WTO. In other regulatory policy domains there is already a substantial interface between the WTO and other international regimes – one example is in the area of product standards (health and safety norms for food and animal products), another is the protection of IPRs. In these various areas, other institutions take the lead in setting substantive norms (ISO, FAO/Codex Alimentarius for product standards; WIPO for intellectual property). The same is true for development assistance, where the WTO today interacts more with international development agencies than it did in the past.

These are all areas where PTAs have little role. PTAs also generally do not address subjects that have been the source of disagreement in WTO negotiations such as agricultural support policies, which are important to developing countries. As the world economy becomes even more interconnected as a result of the “Internet of things”, e-commerce and the associated increase in cross-border service flows, policies that limit or raise the cost of digital trade and data flows will become ever more important. Mega-PTAs may result in agreements on how to address such matters, but from a global efficiency perspective what is needed are rules of the game for digital commerce and cross-border data flows that span all major economies. In short, the future of the WTO is an important topic not only for the institution itself, but also for the health and expansion of global trade in the 21st century.

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CHAPTER 2

A New Architecture for the WTO?

Miguel Rodríguez Mendoza

WTI Advisers

Introduction

The WTO is currently facing an “adaptability” crisis. The world economy has changed significantly since the WTO was created back in the mid-1990s, and new challenges are quickly piling on top of the old ones. The rise of emerging countries and the relative decline of traditional economic powers; the negotiating requests, demands and approaches from different member countries; the proliferation of regional trade pacts and the need to deal with complex new issues, such as climate change and food security, are – in different ways and intensity – shaking the foundations on which the WTO was built some 20 years ago.

Thus, a key question is whether the WTO is capable of facing these new and complex issues or whether there is instead a need to revise it in some fundamental ways. Should the WTO’s current negotiating mandate and structure be expanded? Would it be better or necessary to complete the unfinished business of the Doha negotiations before taking up new negotiating initiatives? What should be done to strengthen the multilateral trading system and to ensure the future success of the WTO? Are the results and/or limited agreements reached at the last WTO Ministerial in Nairobi make a difference to the rather negative perception developed recently about the “negotiating” function of the WTO?

To strengthen the multilateral trading system is especially important from a sustainable development perspective. Over the past six decades, the system has provided an unprecedented level of stability and predictability in the way WTO members conduct their trade operations. It has also provided – particularly

since the establishment of the WTO – a credible and solid mechanism to adjudicate trade disputes, one that is guided by law rather than power.

Developing countries, most of which steered clear of the system during the GATT years, have for the most part joined the WTO, making the multilateral trading system a truly universally accepted set of values and rules, and not the rather limited “club” that it used to be. These developing countries are now using the system to their advantage – they hold the key to forward-looking negotiating outcomes, and account for more than half of the 500-plus disputes dealt with so far by the WTO.¹

But the WTO is at a critical juncture. A renewed sense of international cooperation among WTO Members is essential for dealing, first and foremost, with the never ending Doha negotiations. Completing Doha would allow the WTO to focus on some of the most pressing challenges that in my view the system now faces: *first*, defining a new set of negotiating modalities for the future; *second*, revisiting the traditional approach to the participation of the private sector (i.e. the business community) in its activities; and *third*, dealing appropriately with the increasing number of trade agreements entered into by its Member countries, especially the so-called mega-regional agreements such as the Trans-Pacific Partnership (TPP), whose negotiations were recently concluded, and the Transatlantic Trade and Investment Partnership (TTIP), which is still under negotiation.²

Completing the Doha Negotiations

Trade negotiations are what the WTO was created for in the first place. Concluding the Doha trade talks – approaching their 15th anniversary in 2016 – is a must if the WTO wishes to move forward and tackle future challenges head on. Not delivering on Doha will damage the organization’s very core function, discredit its efficiency, and make it extremely difficult for the WTO to acquire a mandate to deal with pressing non-Doha issues (such as climate change and food security) and, as I mentioned before, the increasing number and complexity of regional trade agreements. Thus, the issue is not *whether*

1 Dispute number 504 was initiated on March 16th, 2016 when Japan requested consultations with Korea on certain antidumping duties it had imposed on pneumatic valves from Japan (see https://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm).

2 This chapter draws significantly on the reports and discussions that took place in the context of the E15 Initiative, a program of exchanges and analyses on the current status of the multilateral trading system launched in 2011 by the International Centre on Trade and Sustainable Development (ICTSD) and a number of partnering institutions, including IMD/The Evian Group, and involving an impressive number of leading international experts; see www.ictsd.ch for more detailed information on the E15 Initiative.

the WTO should complete the Doha negotiations – that’s a given. The issue instead is how to put an end to the current deadlock and keep the negotiating machinery rolling on.³

Dealing with the “Single Undertaking”

Over the years, a number of options have been suggested for moving the negotiations forward. However, these have run against the wall of the “single undertaking,” a procedural device that has been elevated to the category of guiding principle in WTO negotiations. Initially designed to facilitate an equitable global agreement during the Uruguay Round, the “single undertaking” is no longer a negotiating tool. Instead, it has become a way for those countries least willing to take on new commitments to hold the negotiations hostage.

There is a need to revisit the meaning and purpose of the “single undertaking.” Does it mean that every single word in every single agreement needs to be agreed simultaneously by all participants to have an agreement on the whole? Do the negotiating issues have all the same value to all the negotiating partners? Are they all equally important? The common answer to these questions is, obviously, a rotund “no.”

If the GATT negotiating history is to offer any lesson, it’s that every negotiating round has always left aside some pending issues, with the goal of addressing them later on in future negotiations. In the early years of the system, during the first GATT negotiations – which dealt mainly with tariff cuts – it was clear that further, additional cuts had to be dealt with in future negotiations. During the Tokyo Round – the first to deal with non-tariff issues – the concluding deals also left a number of pending subjects to be resolved at a later stage.

Even the Uruguay Round, despite being based on the “single undertaking,” was no exception to this rule, as it left aside a number of issues in agriculture and trade in services – the famous “built-in agenda” – with the goal of addressing them later in a post-Uruguay Round environment. Thus, the “single undertaking” does not mean solving all negotiating issues at the same time; it just means finding an appropriate outcome for all of them at a particular point in time, even if occasionally some of these issues are to be dealt with in the future.

3 Some analyst and “practitioners” are even questioning the need to “revive” a process that they see as already dead (see the *Financial Times* article of December 31st, 2015 by Michael Froman, the US Trade Representative; and Carlos A. Primo’s article on the IMD website at <http://www.imd.org/news/Doha.cfm>).

Moving to a Final Doha “Deal”

At present, of all the Doha issues, an agreement on non-agricultural market access (NAMA) is the one that holds the promise to move the negotiations toward a final deal. Even if tariff reduction is perhaps not the most “economically” significant of all the subjects included in the Doha negotiations, negotiating tariff cuts and consolidating them in the various country schedules is something that trade negotiators are used to doing, can be done relatively quickly and has a very high visibility. Progress in this area may thus have a demonstration effect in the other areas of the negotiations.

The situation that WTO Members face today is not unlike the one faced by GATT members in the early rounds, i.e. a need to reach an acceptable level of tariff cuts among the key trading partners – including now China and the other emerging economies – and to apply them on a most-favoured nation basis. Thus, strange as it may seem, the old issue of tariffs cuts might today help to unlock the paralysis in the other areas of the negotiations and finalise a global pact, just as they have traditionally done.

It may seem ironic that a protectionist device that most analysts had written off as insignificant and outmoded could continue to play such an important role in today’s negotiations. However, the reason may lie not in the intrinsic value of tariff protection, but rather in the visibility that it would give to a negotiating package. In politics, reality almost always takes a back seat to perception, and in developed countries the perception that some countries are “free riding” in the negotiations has taken a strong hold.

Tariffs are not a major impediment to global trade. Existing tariff protection has not prevented world trade from growing significantly in the last few decades. Applied tariffs are now at historically low levels, due, in part, to past trade negotiations, WTO accessions and unilateral tariff reductions undertaken by a number of countries, mainly developing countries. However, tariff protection in most emerging markets, which account for a growing proportion of world trade, is well above tariffs in many developed and developing countries. For example, average applied tariff levels in China and Brazil are 9.6% and 13.5%, respectively, as compared with average tariffs of 3.5% in the United States, 3.4% in Peru, or 6.7% in Switzerland (WTO, ITC and UNCTAD, 2015).

Importantly, opening emerging economy markets is not only in the interest of the industrialized countries, but also benefits developing countries, whose exports go increasingly to emerging markets and to other developing countries. According to UNCTAD, in 2013 South–South trade flows represented more than half of overall developing country trade. This share varies by region, ranging from above 40% in Latin America and transition economies to almost

70% in South Asia and East Asia. Although a proportion of South–South trade encompasses intraregional flows, the largest part involves trade with the East Asian region, and since 2008 this region has become an increasingly important trading partner for all other developing country regions (UNCTAD, 2015).

A solid agreement on the market access negotiations – one that requires all countries to make a meaningful contribution consistent with their economic realities and possibilities – will give the Doha Round a renewed sense of progress. But this alone will not be enough. A solid deal on agriculture is also required, as no final Doha deal will be possible in the absence of more disciplined farm markets. The agreements reached at the Nairobi Ministerial go in this direction, and the commitment of WTO Members to eliminate export subsidies for agricultural exports may help the Doha negotiations to move to a final stage, but the “jury is still out” on this. Negotiations on services, on antidumping rules, on intellectual property issues and on trade facilitation are all important, but none of these could individually facilitate agreement in other areas of the Doha trade talks in the way a market access deal, including agricultural reform, would.

Getting New Negotiating Modalities

As for the future, WTO negotiations should not necessarily be based on the “single undertaking,” at least not exclusively. They will require a different, complementary approach. This approach should be predicated on the need for a more cooperative understanding among Members – one where negotiations, authorised by the entire WTO Membership, could be undertaken by groups of interested countries if and when certain specific conditions are met, and, importantly, provided the multilateral nature of potential WTO agreements is preserved.

This overall approach, however, should have one important exception: negotiations involving only a limited number of countries would not be appropriate when they include existing rules and disciplines. The WTO is a legal and institutional framework that requires its Member countries to conduct their trade and trade policies in a clearly defined manner. Therefore, the rules of the game cannot be modified without the agreement of the entire Membership, and nor can new deals be incorporated into the system without the acceptance of all WTO Members.

In almost all other instances, negotiations among groups of interested countries could take place and their results incorporated within the WTO framework. In fact, we have already seen this type of approach at work in the case of the WTO’s “plurilateral” agreements. These deals – which were

made possible via the Marrakesh Agreement – are normally entered into by groups of “like-minded” countries that decide to establish among themselves a common set of rights and obligations to deal with a particular subject matter or sector. Notably, these agreements create rights and obligations only among the participating WTO Members, rather than being multilateral deals. The WTO “plurilateral” agreements were originally negotiated during the Tokyo Round of trade negotiations (and were thus “codes”) but, unlike most Tokyo Round “codes,” did not become multilateral obligations. They became part of the WTO in 1995, and have been known since as “plurilateral” agreements. There were initially four “plurilaterals” dealing with trade in civil aircraft, government procurement, dairy products and bovine meat, but the latter two were terminated in 1997.

There is a need to move beyond “plurilateral” agreements as defined by the WTO agreement; if these deals are allowed to expand much further, we could end up with a repeat of the post-Tokyo Round GATT system, with a divided and fragmented WTO. A better alternative would be to move towards a “plurilateral *plus*” environment, where the benefits of the agreements are extended to all WTO Members, and not only to the participating countries. The Information Technology Agreement (ITA) is a perfect example of this approach. This agreement was negotiated in 1996, during the first WTO Ministerial Conference, by a group of 29 countries. A year later, it entered into force with even more members, creating an agreement that would cover more than 90% of the trade in that sector. Market size was an important consideration for the agreement to come to life – today, more than 80 WTO Members are part of ITA, and they have recently agreed to expand its product coverage significantly. More importantly, right from the outset the participating countries agreed that the benefits of the deal would be extended unconditionally to all WTO Members, whether or not they belong to the ITA.

Thus, groups of WTO Members need to have the option of undertaking negotiations among themselves on matters of their interest. Not allowing them to do so will just lead these countries to take their deals elsewhere. Therefore, we need rules in order to create new rules. This process should include at least three key considerations. *First*, it must provide for an “opt in” and “opt out” approach, entitling all WTO Members to participate in the negotiations at their own choosing, with the option of withdrawing from the talks at any point. *Second*, the benefits of the agreements should be extended unconditionally to all WTO Members. And *third*, the final deals should be incorporated into the multilateral set of rules and regulations as “plurilateral *plus*” agreements, with appropriate accession clauses (i.e. be open to all WTO Members under certain conditions).

In short, an alternative approach to trade negotiations moving beyond the “single undertaking” needs to be put in place by WTO Members, setting aside the confrontational nature of the current Doha talks. We perhaps need to abandon all encompassing “rounds” of negotiations for more “a la carte” negotiations where subjects are more likely to produce more significant and quicker results.

Finding an Appropriate Place for the Private Sector in the WTO

Although the WTO is an intergovernmental organization and decisions are taken exclusively by its member governments acting collectively, the business community has an important stake in its performance. It is bound to be affected by WTO operations, as it is mainly business, not governments, that engages in international trade. In practice, business and governments interact in the WTO in many different ways, sometimes advancing the negotiating agenda and at other times ensuring that governments abide by their multilateral commitments.

However, defining a role for the business community in the WTO is not an easy task. The essence of the WTO lies in its negotiating function, and negotiating trade deals is not something that can always be facilitated by the involvement of business interests along the lines of negotiating teams. Thus, when considering the participation of business interest in the WTO, an important distinction should be made right from the outset: the presence of business in the day to day activities of the WTO (i.e. its public discussions, its research activities and the provision of information specifically geared toward their economic concerns, among others) should not be equated with its involvement in the WTO trade negotiations, as these need to be conducted in private, behind closed doors and very often in small groups before receiving the blessing of the entire Membership.

This has always been the case – trade negotiations are private affairs whose conduct are in the hand of government officials; they are not, and cannot be, conducted in the open, as publicity is the last thing negotiators need to make deals.

This does not mean, however, that the business community should be totally absent from these negotiating process. There are many ways the business community could be made part of negotiating processes, be informed of negotiating outcomes and also be allowed, even if indirectly, to influence them.

During the NAFTA negotiations, the United States, Mexico and Canada put in place the “*cuarto de al lado*” (“room next door”) where business representatives from these countries regularly met their respective government’s negotiating teams, with the dual purpose of being informed of the evolution of the negotiations and making their views known on the various negotiating items and outcomes. Over the years, this “room next door” approach was replicated in the negotiation of the trade agreements that the three NAFTA partners conducted with other countries, particularly in the Latin American region. The approach was facilitated by the rather limited number of the negotiating partners; it would be highly unrealistic to try to replicate it at the WTO level.

In a negotiating process – whether bilateral or multilateral – the way each country deals with its business community is its own responsibility. However, in an institution like the WTO, some mechanisms could be put in place to ensure the effective, even if indirect, involvement of business organizations in its activities. Although the WTO has been formally authorized to “make appropriate arrangements for consultation and cooperation with non-governmental organizations,”⁴ which presumably include business entities, currently there are no formal mechanisms and the participation of the private sector is based on a series of ad hoc practices, such as briefings and public seminars and symposia which the WTO hosts on the occasion of Ministerial Conferences in particular. However, as pointed out in an E15 report (Elsig, 2014),⁵ the business community is less involved in the WTO than in other international fora, such as APEC, where a Business Advisory Council has been established, or the OECD, which has a Business and Advisory Committee, or the G20, with its regular B20 meetings.

Much more can be done, but it is not easy to define the appropriate or ideal mechanism that can ensure the effective participation of the business community in an institution like the WTO, whose main functions – negotiating trade agreements and monitoring their effective implementation, including by recourse to dispute settlement – are by their very nature government led.

It would be difficult, not to say inappropriate, to give business representatives full participation in these two sets of activities, since – as indicated in the E15 report (Elsig, 2014) – in addition to logistical issues of significant complexity, full participation of business representatives in, say, trade negotiations may render the crafting of trade agreements much more difficult than is currently the case.

4 See Article V.2 of the Marrakesh Agreement.

5 See also Primo Braga and Kondis (2014).

At the last two WTO Ministerial Conferences, a number of private entities, business organizations and non-governmental organizations took the initiative of organizing a series of debates where their particular concerns were examined and discussed with key government representatives. These debates took place for the first time during the Bali Business Forum, whose organization and purposes are explained in detail in Box 1, and subsequently during the Nairobi Ministerial Conference in 2015.

Box 1: Bali Business Forum

At the Ninth WTO Ministerial Conference, which took place in Bali, Indonesia from December 3rd to 7th, 2013, the International Chamber of Commerce (ICC), the Evian Group@IMD and the International Centre on Trade and Sustainable Development (ICTSD) decided to jointly organize a day-long event to focus on issues of particular interest to business representatives from WTO Member countries. The Bali Business Forum (BBF) – a first event of its type – took place on December 5th, 2013.

The BBF provided an open forum where the business community could examine the most critical issues in the international trade agenda and interact with ministers and other high-level officials to contribute towards a constructive outcome in Bali. The agenda of the BBF included issues such as: 1) the quantitative benefits of a Doha deal (or costs of a non-Doha deal); 2) the impact of mega-preferential agreements (e.g. TPP and TTIP) on the WTO; 3) the complementary nature of trade in services, trade facilitation and global value chains; and 4) the role of the private sector in the WTO.

An accompanying high-level luncheon focused on the topical issues at the intersection of the WTO and digital economy, and a business/ministerial roundtable wrapped up the ambitious agenda at the end of the day in a high-level setting. Throughout the panel discussions, members of the private sector and government officials, including CEOs and key ministers, engaged in an open dialogue on the above-mentioned topics.

The ICC, the Evian Group@IMD and ICTSD acted as the core co-conveners of the Bali Business Forum, in partnership with the Inter-American Development Bank and the International Trade Centre. The BBF also had the support of relevant business organizations and associations, such as the Washington-based National Foreign Trade Council (NFTC), the Coalition of Services Industries (CSI), the European Services Forum (ESF) and the Federation of Industries of São Paulo (FIESP).

Box 1 (contd.)

The Forum helped to facilitate, through engagement and dialogue between business executives and policymakers from all over the world, a better understanding on the possibilities of enhanced multilateral cooperation and on the need for a vibrant WTO.

Another key objective of the BBF was the identification of ways for the private sector to get more effectively engaged in WTO activities – for example, by setting up the institutional mechanisms that would facilitate engagement, such as a Business Advisory Council at the WTO, and/or the holding on a more permanent basis (e.g. on the occasion of WTO Ministerial Conferences) of a forum/dialogue along the lines of the BBF, something which was also implemented at the Tenth Ministerial Conference in Nairobi in December 2015.

Dealing with Regional Trade Agreements and Negotiations

Affecting the daily work of the WTO and hindering its negotiation outcomes is the fact that the large, industrialized countries have tended in recent years to focus on the negotiation of a number of ambitious multi-country trade agreements. These include the Trans Pacific Partnership Agreement (TPP) – involving a number of countries from Australasia and the Americas, most of which are already linked by bilateral free-trade agreements – and the relatively more recent initiative to negotiate a Transatlantic Trade and Investment Partnership (TTIP) between the United States and the European Union. Although these trade initiatives could theoretically work as stepping stones to a robust multilateral agreement, this is not an inevitable outcome under the current circumstances.

During the first “wave” of regional trade agreements (RTAs), bilateral agreements were the norm – most of the 300-plus agreements notified to the WTO are bilateral agreements. Although there are some exceptions, this is no longer the case. We are now in presence of a new “wave” of RTAs characterized by the negotiation of mega-regional agreements. In some cases, these agreements are designed to foster convergence among existing RTAs and/or involve countries representing a large share of global trade, GDP and population.

The recently concluded TPP and the TTIP, which is still under negotiation, have had their deadlines systematically postponed. The TPP was supposed to be finalized by November 2011, but it was not until October 2015 that the negotiations ended; the TTIP negotiations are still ongoing. In general, the negotiations are conducted in confidentiality, not to say secrecy, as most trade negotiations are. Thus, the precise content of these agreements or the depth of the commitments to be made are only known when the negotiations are completed. Therefore, when trying to visualize the impact of these agreements on the Doha negotiations, a series of assumptions regarding their content and the likelihood of their completion need to be made.

However, two key facts are known: the economic weight of the participants and the list of subjects under negotiation. The more important (economically speaking) the partners are to these agreements, the more potentially significant their impact on Doha and the multilateral trading system would be. By the same token, the wider the subjects under negotiation – including a number of “WTO plus” issues or issues not currently within the WTO purview – the more complex the analysis will become.

Both the TPP and the TTIP involve countries representing a very large share of the world’s population, economic activity and trade. The TPP countries are both economically and demographically diverse, as they include developed and developing countries, big countries such as the United States and small ones such as Singapore. Roughly speaking, the TPP countries include 40% of the world’s population and are responsible for some 60% of global GDP, and trade among TPP partners was more than US\$2 trillion in 2012.

The TTIP, for its part, involves 29 developed countries (the United States and 28 EU member countries) that represent the world’s largest economic relationship, with reciprocal trade (goods and services) and investment flows that amounted to more than US\$1 trillion in 2012. The negotiating parties are also the source of most trade preferences in favor of developing countries.

The economic weight of countries participating in mega-regional negotiations will certainly influence the capacity of these agreements to impact both the Doha negotiations and the multilateral trading system, and the elimination of tariffs among them will have an undeniable effect on tariff preferences through preference erosion (although some studies see preference erosion as a relatively minor effect). These agreements may also have, as do most preferential trade agreements, trade diversion effects, although these are difficult to quantify.

However, it is in the area of trade regulation that mega-regionals may have a more lasting effect, and it is in this area that the impact on Doha and the multilateral trading system at large will be felt more dramatically, especially

if mega-regionals are completed relatively soon and the Doha Round has not yet drawn to a close. What distinguishes mega-regionals from other free-trade or preferential agreements is the inclusion in the negotiations of a number of regulatory issues, many of which are currently outside the scope of the WTO and subject to domestic regulations, but which are nevertheless considered essential for today's global commercial relations.

These regulatory issues include, but are not limited to, regulatory coherence – for example, on the safety of products and the methods of production – state-owned enterprises, professional services, customs, e-commerce, labor and environment issues, government procurement, investment issues, currency issues, temporary entry of business people as well as standards related to sanitary and phytosanitary measures and technical barriers to trade.

In other words, the mega-regionals have the potential – due to the sheer size of the countries involved in the negotiations and the nature of some of the issues under negotiation – to significantly expand the scope of the international trading system by setting up standards that would apply initially only among those countries, but that could eventually become global standards.

Once the mega-regionals are completed and new regulatory issues agreed upon by the participant countries, the newly agreed standards will not be easy to modify in WTO negotiations or elsewhere; they will fix TPP and/or TTIP countries' positions in future negotiations and form the basis for their negotiating positions. Therefore, there is the risk of a “fragmentation” of the multilateral trading system with different standards adopted by different sets of countries, a situation not too dissimilar to that experienced after the Tokyo Round of negotiations and the adoption of “codes” on a number of non-tariff barriers by a group of (mainly developed) GATT members.

Thus, more than the traditional market access issues such as tariff reductions, preference erosion or trade diversion, the impact of mega-regionals on Doha and the WTO should be analyzed in terms of their “regulatory” impact, that is, in terms of the implications for the multilateral trading system of such a large group of countries, involving both developed and developing countries and representing such a large share of global trade, setting up new standards in areas either not yet covered or insufficiently covered by the WTO.

Summing up, the current mega-regional negotiations present both risks and opportunities to developing countries, the Doha negotiations and the multilateral trading system. Like any free trade agreement, these negotiations may have an impact on trade preferences and may have some trade diversion effects. However, these ramifications should not be overemphasized. If the experience with past free trade agreements offers any guidance, trade diversion

and/or preference erosion are less significant than some academic analyses have suggested. More significant could be the set of new standards and regulatory frameworks that might be incorporated into the agreements which would, as a result, fix the positions of participant countries to those standards, thereby complicating the multilateral examination of the latter.

One of the reasons why countries have moved to regional negotiations is often said to be the long-lasting deadlock in the Doha negotiations. Yet, the WTO continues to play a critical role in today's global economy. It ensures the transparency of the trade practices of its members, enforces existing multilateral rules and disciplines, and adjudicates trade disputes in case of breach of WTO obligations by any of its Members. And it is precisely because of these important functions that delays in completing the Doha negotiations and the focus on preferential trade initiatives are challenges that the WTO cannot ignore or underestimate. And this should certainly be the preferred approach by developing countries, most of which are outsiders to regional and/or bilateral deals, including mega-regional negotiations.

In order to keep an eye on the current negotiations of regional deals and to provide a forum where interested parties and entities can examine and discuss issues of relevance to these agreements and their possible impact/relationship with the multilateral trading system, ICTSD, together with the Inter-American Development Bank (IADB), is implementing an E15 initiative: the RTA Exchange. The main features are summarized in Box 2.

Box 2: The RTA Exchange

For the last few years, the Inter-American Development Bank (IADB) and the International Centre on Trade and Sustainable Development (ICTSD) have been working towards the implementation of the RTA Exchange, an initiative whose basic contours were agreed during the 2013 WTO Ministerial Conference that took place in Bali, Indonesia, after being pencilled out at several meetings of the E15 Group of Experts on Regional Trade Agreements.ⁱ More recently, the Asian Development Bank (ADB) has also decided to be part of this initiative and to contribute to its implementation, and both the IADB and the ADB are in the process of defining their cooperation activities in this area.

The RTA Exchange is intended to provide a venue, virtual and otherwise, where interested stakeholders from the RTA and the WTO worlds interact with each other, discuss policy relevant issues around WTO and RTA convergence and identify options to multilateralise best practices or, as appropriate, regionalize best multilateral rules and/or institutions.

A key device of the RTA Exchange is an interactive website (www.rtaexchange.org), which is being coordinated by INTrade, an IADB mechanism that provides information on trade and integration activities in Latin America and the Caribbean.ⁱⁱ The activities of the RTA Exchange will also include the provision of information and news on RTA developments, the organization of global and regional conferences, informal roundtables, briefing sessions, expert meetings and functional dialogues on key RTA rules and institutions, in association with RTA Exchange partners.

i The E15 Group of Experts on RTAs has been jointly managed by the International Centre on Trade and Sustainable Development (ICTSD) and the IADB with the main objective of examining whether a new substantive and institutional framework for addressing RTAs by the WTO is necessary and desirable.

ii INTrade (www.intradebid.org) is a comprehensive online gateway bringing together information on integration and trade in Latin America and the Caribbean. The system includes in-depth data on trade agreements, detailed statistics on imports and exports, and indicators that measure the structure and performance of trade.

Conclusions

None of the issues discussed in this chapter is new – they have been discussed by policymakers, academics and practitioners, both inside and outside the WTO, for a long time already. The suggestions for reform put forward are also well known by most trade practitioners and, to varying degrees, could be accepted by most of them. However, no action has been taken so far to put them in place and no process is envisaged to collectively discuss them, as WTO Members and trade negotiators seem to be too busy getting out of the current stalemate to engage in discussions on the future of the WTO.

Yet, something needs to be done, and done quickly, to keep a vigorous multilateral trading system from stagnation. And if governments are too busy to engage collectively in a reform process, perhaps the WTO leadership (i.e. its Director General and its DDGs) or a group of like-minded governments could take the initiative and, with the help and support of interested institutions from civil society and the business world, engage in a collective, open and effective discussion on the kind of multilateral trading system that would be best suited to the trade and economic challenges of the 21st century.

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CHAPTER 3

Why Engage in Trade Negotiations and the Relevance of the WTO

Alejandro Jara

King & Spalding

The attempt to further trade liberalization that has been a feature of the multilateral trading system since 1948 has stalled. The inability to conclude the Doha Development Agenda (DDA) negotiations, particularly since 2008, is a crisis of major proportions of international cooperation in the field of economic relationships and beyond. The reasons are several, but one stands out. The DDA was launched to make possible liberalization of trade in agriculture, which means among other aspects the elimination or reduction of the most trade-distorting instruments.

This crisis contrasts with the increasing spiral of trade agreements negotiated around the world that shows that the appetite for trade liberalization is present and active. We shall call these “preferential trade agreements,” or PTAs. This paradox is explained by the fact that such agreements do not deal with agricultural support (there are other areas in this situation), while this is a central element of the DDA. The unwillingness of one major power to deal with domestic support, as well as the position of one major emerging economy seeking to rewrite the agriculture rules agreed upon in the Marrakesh Agreement, make a consensus impossible. As a consequence, those seeking further liberalization have sought other means, PTAs being the main vehicle.

All the same, since the 2008 crisis, many governments have applied trade restrictive measures which have piled up. Both the Global Trade Alert (GTA)¹ and the WTO Secretariat² have documented this. This might indicate that the rulebook of the WTO needs to be updated and tightened to limit protectionist measures by governments. In this regard, results of PTAs show a mixed picture.

1 <http://www.globaltradealert.org>

2 https://www.wto.org/english/tratop_c/tpr_c/trade_monitoring_c.htm.

On the one hand, PTAs have shown little, if any, progress in areas such as subsidies and trade remedies, besides agriculture. On the other hand, in response to the diversification of economies, global value chains and technological changes, some progress is being made in improving international cooperation, particularly in the regulatory field, e-commerce, state-owned enterprises, business facilitation and transparency. In this sense, PTAs may well be the “breeding” ground where new disciplines are enshrined which, if successful, could be the foundations of an updated rulebook of the WTO, should the political conditions change.

In the meantime, countries will face increasing pressure to take part in PTAs that become part of the international law landscape. They are important both from the viewpoint of the economic impacts as well as the systemic implications.

In this context, and as part of training officials, it is important to pose some of the most relevant questions that policymakers must face when setting up a trade policy strategy that involves negotiations of trade agreements with other economies, which is what this chapter attempts to do. While a seasoned trade negotiator would take for granted most of, if not all, the questions and analyses that follow, that may not be the case for those who are at the beginning of a career in trade policy. Indeed, some elements of what follows may serve as a good basis to assess trade agreements after their conclusion and for those with a more inquisitive mind. The questions are based on the assumption that the country concerned is already a Member of the WTO. It is also worthwhile to raise some issues concerning the organization of the negotiations and the corresponding allocation of resources, as these are bound to have political impacts.

1. **Why is it necessary or convenient to negotiate a trade agreement (bilateral, plurilateral or multilateral)?** What is the purpose of the negotiation? Most, if not all, trade agreements have the purpose of liberalizing and/or facilitating trade and investment, which implies that it will go beyond what it has already agreed upon in the WTO (unless, of course, the country is negotiating with a non-member of the WTO). Consequently, a trade agreement will no doubt result in a change in the country’s policies and/or in the policies of the counterpart(s). Presumably, a government will decide to negotiate when it perceives that such changes will be to the *overall* benefit of its economy, even though there may be adjustment costs to certain sectors.

2. **Unilateral liberalization.** To the extent that these changes are limited to domestic policies, they can also be pursued unilaterally. In other words, liberalization and/or facilitation can be achieved by implementing the corresponding measures without the intermediation of a negotiation with another country. Liberalization is easier and faster to achieve if made unilaterally. In addition, the result may be of better quality since no compromises are necessary with other countries. However, from the viewpoint of the quality of the outcomes, some compromises with domestic interests may be necessary, whereas in a negotiation with other countries such compromising domestic pressures may be avoided or offset. Moreover, a unilateral liberalization may be rolled back by an ulterior piece of legislation or regulation, as the case may be. A trade agreement does not prevent this from happening but it comes at a price, because it is not simple to denounce or modify international agreements, and because of the loss of benefits in the market of the counterpart. Thus a trade agreement brings greater stability to domestic changes (the “lock-in effect”) that, in turn, probably gives greater confidence to economic agents. Finally, unilateral liberalization presents some political economic limitations, since it imposes adjustment costs to the domestic producers without any direct benefits for exporters (although it may help indirectly by diminishing the indirect anti-export bias of trade protection). Consequently, the resistance that some domestic producers may put up will only be countervailed by the support that may be elicited from importers and consumers, who usually have weaker organizations.
3. **What policy changes should be pursued? In other words, what are the objectives of a negotiation?** Usually there is no one single reason, but rather a combination of motivations that respond to the various interests and stakeholders that participate directly or indirectly in the decision-making process, that leads to a trade negotiation. The greater the number of interests that are reflected in the objectives, the greater the support for the negotiation. However, to define the objectives of the negotiations requires the agreement of the other party (or parties), and some of those may generate resistance from particular interests in a given jurisdiction. Some countries elect to have the objectives to be pursued in the negotiations pre-stated in a public statement, sometimes worked out with the legislative and after consultations with stakeholders. For example, the United States achieves this by approval by Congress of the Trade Promotion Authority (TPA). This is a vehicle whereby Congress agrees to not use its prerogative to amend draft laws, provided the Executive acts

within the agreed-upon objectives to be pursued in trade negotiations.³ Likewise, the European Commission has published its trade policies objectives after extensive consultations with the European Parliament, among others (European Commission, 2015). The following are some objectives typically pursued by governments in a trade negotiation:

- i. To lock-in domestic reform. For example, in the GATT Tokyo Round (1973-1979) Chile negotiated an across-the-board binding of 35% for all products (while the applied tariff across-the-board was 10%) to ensure there would be no rollback above the bound level.
- ii. To liberalize its own trade regime. For example, throughout the 1990s and beyond, Chile deliberately pursued free trade agreements (FTAs) to further liberalize imports.
- iii. To prise open other markets for its goods, services and investments. An FTA involves reciprocal opening of the market of the other party (or parties), which makes any adjustment cost more politically palatable. However, if the negotiation is with a duty-free country such as Singapore or Hong Kong, China, such partners will “appear” to give nothing since they have virtually no tariffs. This is a mere appearance, since binding the duty-free is very valuable, as are other provisions related to services and investment that may part of the deal.
- iv. To introduce more competition and fight inflation in the domestic market. Trade policy is part of an overall economic policy, and for the policymakers there will be welfare benefits because of enhanced competition, thus limiting domestic prices from rising.
- v. To prevent discrimination against its exporters and investors in other markets. For example, towards the end of the 1990s under the leadership of its new Trade Commissioner, Pascal Lamy, and in order to give priority to the Doha Round of multilateral negotiations, the European Union self-imposed a moratorium on the initiation of negotiations for new FTAs, only continuing those already in the pipeline. However, in 2006 the moratorium was terminated as the European Union observed that the United States and Korea were starting negotiations for an FTA and invited Korea to begin talks for a bilateral FTA, for fear that otherwise its exporters would face less favorable treatment than competitors from the United States in the Korean market. This has become one of the most powerful drivers

3 See <https://www.congress.gov/bill/114th-congress/senate-bill/995/text>.

of negotiations; in other words, a struggle against discrimination in the absence of further liberalization through the WTO.

- vi. To enhance security, cooperation and bilateral relations. Examples include FTAs such as the one between the United States and Israel.
- vii. To settle problems and prevent conditionality. For example, developing country beneficiaries of benefits under mechanisms such as the Generalized System of Preferences are regularly subject to pressures to change regulations such as environmental or labor standards, under the threat of losing the preferences. An FTA will ensure duty-free treatment once and for all, without prejudice to challenges under the dispute settlement mechanism for not complying with such standards.

4. What are the advantages and disadvantages of bilateral, plurilateral, regional and multilateral formats? Trade agreements can have different geographical coverage. Normally, the lower the number of participants, the easier it will be to reach agreement and achieve a better result. However, three or more participants can assist in achieving a balance that otherwise would not be possible. This is particularly effective when one of the parties is a much bigger economy than the other participants. NAFTA would be a good example in this regard. Also to be considered are the distortions that preferences introduce in the allocation of resources. From this perspective, a multilateral agreement would be the optimal format. Except in the case of the latter, all other formats imply a choice of the parties to the negotiation. Such choice has obvious political and geopolitical considerations. Putting these aside, there are a number of other factors that could be considered in this decision.

- i. The first consideration is the model to be used in the integration project. These are well known because Article XXIV of GATT defines what is a “free trade area” and a “customs union.” An essential element in a customs union is that beyond the formal definition that requires the existence of a common external tariff, many more common or harmonized policies are in fact required to ensure a proper functioning, such as competition policy, subsidization, government procurement, standards and trade remedies, among others. Little wonder that the only customs union to function effectively in the last 60 years is the European Union, followed by the Southern African Customs Union

(SACU)⁴ (and the jury is still out on the Eurasian Economic Union).⁵ The choice of the integration model is of course a determinant of the partners.

- ii. Gains. A trade agreement needs support from government, business, politicians, unions, and so on. While the results cannot be measured until the text is divulged, it is nevertheless inevitable that the intention of initiating a negotiation is sustained on perceived gains or benefits for the economy. The assessment of gains should not be overstated to avoid the risk of overselling and losing credibility. Increases in existing exports of goods and services, new exports, cheaper imports, more and better paid jobs, and new investments are all important selling points. If none of these gains is perceived in the case of a possible partner, it becomes difficult to justify a negotiation.
- iii. By the same token, sensitivities are equally crucial in terms of their identification and assessment. If they outweigh the perceived benefits, a negotiation becomes difficult, if not impossible. An example to illustrate this is the case of New Zealand and Chile. Starting in the mid-1990s, officials met frequently and proposed, with the approval of the respective heads of government, to initiate negotiations for a bilateral FTA. They regarded it as being of systemic long-run interest to establish a trans-Pacific model that could be expanded to other APEC economies. However, bilateral trade was small and the structure of production was similar, and the initiative did not elicit much enthusiasm in Chile. On the contrary, New Zealand is a powerful exporter of dairy products and Chile is a net importer, and Chilean domestic producers – who are highly sensitive to international prices – expressed firm opposition to the idea of a bilateral FTA. They had the support of other agricultural producers and the Ministry of Agriculture, in effect killing the idea for a few years. It was only in 2003 that an expansion of the number of participants to include Singapore and Brunei made it possible to carry out the negotiation that concluded in 2005 giving birth to the P4, the precursor to the TPP.
- iv. Size and quality of the market. By negotiating a trade agreement, a country is “exchanging” access to its market for better access to other markets. For a small country, it would seem a very good proposition to

4 Botswana, Lesotho, Namibia, South Africa and Swaziland. However, South Africa chose to negotiate an FTA with the European Union independently of its SACU partners. The latter in practice treat EU imports duty-free, but their exports do not enjoy the same access as South African products to the EU market, without prejudice to the Everything but Arms initiative of the European Union.

5 Belarus, Kazakhstan, Russia, Armenia and Kyrgyzstan.

negotiate with a much larger economy. But “size” can be measured in different ways: GDP (at market or PPP exchange rates), total imports by value or volume, imports of products exported by the bigger country, etc. (or a combination thereof). A real example to illustrate this occurred in the second half of the 1990s, when Chilean exporters observed that Mexico was negotiating FTAs with several Central American countries and requested that their government do the same to avoid being discriminated against. Putting aside the maxim that “any market is a good market” and any political considerations, the decisive factor behind allocating resources to negotiate with Central America was the fact that, though small (measured in different ways), these markets imported more manufactures from Chile relative to other markets. In this case, the *quality* of the market was a compelling reason.

5. **Defining the agenda.** In parallel with the above points, another important consideration is the determination of what exactly will be the subjects of the negotiation. This involves an understanding of what are the objectives to be pursued in each item or chapter. For example, it makes a difference to say that there will be a chapter on cross-border trade in services with the objective of liberalizing *all* services, as opposed to binding the present *status quo* of access and national treatment for services supplied from the negotiating partner, which implies that existing restrictions are maintained.⁶ The political impacts of the two are very different. In many cases, using existing agreements as a template can facilitate the determination, since there will be a clearer view of the possible outcomes. The more parties that are involved, the greater the need for this understanding and the more formal it becomes, to the point that multilateral agreements need a document to launch a negotiation, such as the Doha Ministerial Declaration. In a bilateral setting, this usually takes the form of a press communiqué.
6. **The communication of “red-lines”** is important but not essential. “Red-lines” refer to limits to liberalization or other disciplines that, for whatever reason, a government will not agree to, even if it implies that an agreement will not be reached. This is a process that runs in parallel with the definition of the agenda, and involves communicating to the counterpart what is not negotiable. However this is done – in writing or through verbal exchanges – it is important to avoid unpleasant surprises down the road that may impact key expectations and upset the balance of

6 Usually the preservation of existing restrictions is accompanied by the “ratcheting effect,” which implies that any future changes cannot increase the degree of non-conformity with the treaty; changes can thus only be more liberalizing.

interests, and that may derail a negotiation and generate mistrust. A typical example would be communicating that everything will be negotiable except certain products (the United States typically excludes sugar from most of its trade agreements) or a service (most countries follow the GATS and exclude air transportation from PTAs). The red-lines should not be used to acquire bargaining chips. If during the negotiation a red-lined issue is negotiated away, then all other red-lines may be regarded as negotiable, thus losing its effect. In the absence of red-lines, there is less trust and the parties will not be willing to table their final/best offers in order to retain chips should red-line issues suddenly appear in the negotiation. For example, in the TPP negotiation, because of internal electoral politics, the United States took a long time to communicate its approach and positioning with regards to textiles and apparel, and other sensitive areas. According to some negotiators, this was the cause of unnecessary delays.

7. **The political economy of the other party (or parties).** As in most negotiations, difficulties often arise because of domestic political constraints, however beneficial a particular outcome may be. To have a good understanding of what lies behind a particular position is crucial in order to determine what is important and what the limitations are that the counterpart faces. This also allows those positions that are motivated by a negotiating tactic of acquiring bargaining chips, instead of a genuine concern or resistance, to be weeded out. To have the necessary and undistorted relevant information at hand probably implies the employment of law firms or other sources of legal, economic and political analysis of the other party. For example, negotiating services and investment implies dealing with complex regulatory frameworks that are better understood by local lawyers, particularly when the other party does not share a similar legal and administrative culture.
8. **The domestic consultative process** with most, or all, stakeholders is an imperative of modern day trade agreements. Moreover, as the agreements cover other areas besides tariffs (in particular, services and intellectual property), the number of parties with opposing interests increases. Time and resources spent on consultations before and during the negotiations are therefore a key element to neutralize the resistance, or at least force stakeholders to develop arguments with the relevant evidence. In this process, it is likely that many sectors that fear greater external competition will argue that they should be excluded from the negotiation. In other words, they will want to become part of the national red-lines. Such positions are best dealt with when the government communicates *ex ante* that exclusions (or other exceptional treatments) will only be entertained

when certain objective criteria are met. Once the negotiation is launched, this dimension becomes more difficult because a balance must be struck between the transparency that is required to engage domestic stakeholders in consultations on the one hand, and the necessary confidentiality of the negotiations, particularly the texts as they are developed, on the other. The manner in which consultations are organized is not something for this chapter to dwell upon. However, it seems valuable to point out that some of the best practices are those that force the stakeholders to organize themselves in order to bring to the table approaches that have already been negotiated, eliminating extreme and unrealistic positions. Since the stakeholders will be many, it follows that such practices will increase efficiency and help generate consensus. Without counting other ministries and governmental agencies, examples of other stakeholders include i) business; ii) politicians; iii) parliamentarians; iv) unions; v) non-governmental organizations (NGOs); vi) academia; and (vii) professional associations

9. **The consultative process: the special case of business.** While all stakeholders are important, business is special in the sense that it bears the risks, and therefore has much to win or lose depending on the quality and size of the markets. By the same token, business has special responsibilities to engage by expressing its views and, if the case warrants, by providing political support. Understandably, however, business is a mix of competing and sometimes contradictory interests. It follows that at a national level, its messages often get diluted in generalities that accommodate all sectors, which renders the content quite useless. In this regard, sectoral expressions are more valuable for a government. Having said that, business should be encouraged to state its views of the type and quality of rules it needs to make more investments and exchanges of goods and services possible. This is at the heart of the modern trade agreements, including the WTO. While business acts mostly at the national level, it should also build international coalitions and be active, particularly in Geneva. While the International Chamber of Commerce or the Coalitions of Services Industries in several countries (and also grouped in the Global Coalition of Services) offer good examples, the fact is that they are present in Geneva only two or three times a year, and consequently involvement in the details of negotiations is not possible. A much better example is the Global Express Association, which groups express delivery industries, with a permanent presence in Geneva.

By the same token, governments and international agencies should do more to engage business, particularly by opening institutional channels for their participation (and that of other stakeholders as well). This could be done at the WTO, for example, by opening to observers the proceedings of the trade policy reviews and allowing business to pose questions directly to the government under review; or by allowing business to express its specific trade concerns to the Committees of Technical Barriers to Trade and of Sanitary and Phytosanitary Measures. These are but a few examples of how engagement by business can be improved. In shaping the future agenda of trade negotiations, the view of business will be crucial regarding content, and its support indispensable to move to higher levels of international cooperation.

10. **The role of the media, including social media,** is also a central element to be considered in pursuing a negotiation. With few exceptions, the professional media is not specialized and cannot be expected to accurately communicate to a wider public issues relating to complex public policies.
11. Points 8 and 9 above have an external dimension insofar as the process of consultations can also be carried out with *stakeholders of the other party*, particularly those that could be more supportive. Likewise, the media of the other party should not be neglected as an important dimension of the political effort to advance and conclude negotiations of a trade agreement.
12. **The organization of a negotiation.** In the absence of an institution (like the WTO), and therefore of a Secretariat, the organization of a negotiation is a time-consuming and not inexpensive affair. Consequently, much effort and resources are devoted to developing the institutional backup and efficient processes. For example:
 - i. Who will play the role of secretariat?
 - ii. How will texts be controlled and circulated?
 - iii. Which are to be the negotiating groups, and who shall preside and report?
 - iv. Who will be responsible for providing background information (texts of other negotiations and jurisprudence)?
 - v. What language(s) will be used to conduct the negotiations and in the texts?
 - vi. The legal scrubbing
 - vii. Translation.

13. The legislative process of incorporating international obligations into the domestic legal framework. While this is not part of the negotiation proper, the manner in which the incorporation takes place has an important impact on the scope of trade agreements. Broadly speaking, there are two models. As an example of one approach, in the United States the Executive doesn't seek the approval of the treaty itself, but instead submits to the legislature the text of the changes to domestic law that are necessary to implement the international obligations.⁷ This implies that by and large, once this process is completed no further legislative action is required to implement a trade agreement. It also means that any future law approved by Congress can modify prior law, and thus the international obligation contained therein.

The other approach is approval of the treaty itself by the legislature, and under many legal systems future law cannot derogate or modify such treaties. However, many treaty obligations may need further legislative action. For example, if a treaty provides that there will be an authority to carry investigations when an application of a safeguard measure is requested, a separate law must designate who will be the investigating authority. This can be avoided if in the treaty itself such designation is made (typically in an Annex), and is thus of the text that the legislature approves. It is doubtful, however, whether this technique can be used in more complex matters. If ulterior legislative action is required for some treaty obligations, there is an element of uncertainty over whether or not approval will be forthcoming after ratification of the trade agreement. Other parties may require full approval not only of the treaty, but also of the implementing legislation before allowing entry into force. This may generate tensions because it may be perceived as an intrusion by a foreign government in the legislative process. A prior understanding of the procedures in this regards, along with the appropriate explanations, may facilitate the incorporation of trade agreements into domestic law and the subsequent implementation.

7 To approve trade agreements as treaties, under the US Constitution the advice and consent of two-thirds of the Senate would be required. In contrast, domestic laws can be approved by simple majority in both Houses.

The Future of WTO Trade Negotiations

Despite the failure of the DDA negotiations, it is inconceivable that the multilateral trading system will cease to be a forum – and arguably the best forum – to negotiate trade liberalization.

The failures of the past 15 years leave no doubt that the manner in which negotiations are conducted must change, at least to reflect present realities and future needs. To achieve a new understanding of the format and substance of the negotiations will take time and a long-term political approach to international cooperation in the field of trade. Many changes are necessary, and indeed some are already underway. The following flags some of the most important issues that members will have to confront.

No negotiating process can continue to be organized along traditional lines (developed, developing and least-developed countries). By the same token, flexibilities like special and differential treatment will no longer work as an instrument for inclusiveness unless they are based on the individual needs of each economy, as in the approach used in the Trade Facilitation Agreement.

The politics must change. Not much more can be achieved if the inability for the last 10 years of the United States to accept outcomes that will change its domestic laws persists, particularly to reduce the levels of trade-distorting agriculture domestic support. Likewise, some emerging economies (for example, India and South Africa) cannot persist in refusing results that will liberalize their imports and instead seek to increase safeguards and other trade-restrictive instruments.

Plurilateral negotiations have surfaced. Some of these are based on the perception that a critical mass exists and thus the outcomes are made extensively on an MFN basis, such as the Information Technology Agreement (ITA) and Environmental Goods Agreement (EGA) exercises. In contrast, other processes, such as the Trade in Services Agreement (TiSA), envisage results that only benefit the signatories (even though nothing could prevent a TiSA signatory from binding its individual concessions under the GATS). However, some form of packaging still seems necessary to ensure that the necessary trade-offs are present. For example, it is difficult to foresee a stand-alone agreement to reduce or eliminate trade-distorting domestic support in agriculture.

The real economy requires an expansion of the agenda, along at least two dimensions. Since the financial crisis, protectionism has been on the rise, even though trade disciplines have undoubtedly contained some pressures. A review is required of the existing disciplines on subsidies, anti-dumping measures, government procurement, export duties and restrictions, among other areas, to

check the worst manifestations of protectionism. Another dimension concerns rules in “new” areas such as investment, competition policy and state-owned enterprises. Special attention should be placed on implementing agreements reached in other multilateral fora , such as the elimination of fossil-fuel subsidies agreed upon at COP21.

Perhaps the first achievement of any future process should be to establish a different basis for any negotiation by binding everything at the applied level, including industrial tariffs, agricultural domestic support, services, government procurement and export duties, among others. This confidence-building approach would set the stage for effective liberalization.

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CHAPTER 4

The Future of the WTO Dispute Settlement System: Consolidating a Success Story

Giorgio Sacerdoti
Bocconi University

Results Achieved

On reaching its 20th anniversary, the Dispute Settlement System (DSS) of the WTO continues to be considered a success story, and rightly so. The mechanism has been defined by a former Director General as the “jewel in the crown” of the WTO, a statement which is even more justified in the light of the failure of the WTO Members to conclude the Doha Development Round (started in 2001), notwithstanding the limited success of the Bali (2013) and Nairobi (2015) Ministerial Conferences, and to reinforce other non-judicial mechanisms within the WTO.

It is interesting to note that the DSS, specifically the Appellate Body, is now taken as a model for “judicializing” other fields, an example being the recent EU proposal to replace investor-state arbitration (ISDS) with a two-level international tribunal in the TTIP.¹ At its beginning, however, the DSS was criticized both by some WTO Members² and by NGOs for allegedly devolving to unrepresentative international “faceless judges” – accused moreover of

1 See the full text at http://trade.ec.europa.eu/doclib/docs/2015/november/tradoc_153955.pdf. A two-level, permanent bilateral Investment Court, replacing Investor-State traditional dispute settlement arbitration, has been introduced in the final revised text of the Canada-EU Trade and Investment Agreement (CETA) at the beginning of 2016, see EU Commission, trade doc. 154329 (February 2016) and at www.international.gc.ca, Final CETA text.

2 Notably by members of the US Congress.

indulging in “judicial activism” – disputes also affecting non-trade interest and individual governments’ regulatory powers.

This positive evaluation is based on:

- The high number of cases introduced (the 500th mark was reached in November 2015) and almost always (90% of those brought to adjudication) resolved effectively by the removal of restrictive measures of an importing country found in breach of WTO obligations by independent and impartial rule-based adjudication.
- The effective functioning of its multi-stage procedure (from consultation to implementation, through a double-stage adjudication phase), which is meant to solve specific, mostly bilateral disputes, but at the same time to give guidance to all the interested members and to take into account the multilateral dimension of the trading system.
- The participation in it of both major trading powers and small developing countries (signaling the importance of the DSS also for small players and developing economies to ensure access for their products to the larger economies’ markets).
- The development of a balanced and consistent case law, sensitive to non-trade concerns such as environment protection and health, which recognizes on one hand the need to uphold market access obligations, and on the other hand the existence of evolving non-trade values and policies – domestic and international – that need to be safeguarded as part of the domestic policy space of WTO Members.

This has afforded “stability and predictability” to the system (as set forth in Article 3.2 of the Dispute Settlement Understanding, or DSU), also in the recent times of financial crisis and economic slowdown. According to official documentation, opportunistic resort to protectionist measures (anti-dumping, subsidies, safeguards) has been contained, although independent research tends to challenge this claim and has a more pessimistic view.³

3 For a relatively positive view, see the various reports submitted by the WTO to the G20 meetings pursuant to the latter’s request and the related data available at <http://tmdb.wto.org>. For a critical position, see the chapter by Simon Evenett and Johannes Fritz in this volume.

Current Problems

On the other hand, the system shows signs of stress (as a victim of its own success, mainly due to the increase in the number of disputes and their complexity), while multilateral negotiations in the Doha Round are lagging. The following major issues have emerged which threaten its effectiveness and may thus diminish the trust in, and recourse to, the system:

1. The increasing number of cases brought to panels and the increasing complexity of disputes and sophistication of arguments made is extending the length of proceedings beyond reasonableness, especially at the panel stage, and is putting strain on the limited resources of the Secretariat.
2. The willingness of losing respondents to promptly comply with the decisions appears to be decreasing, in that effective implementation, while usually performed, requires on average more time. Alternatives to compliance (such as compensation), which appear to be on the rise, may tilt the system towards the protection of the interests of major trading nations, who may be able to pay-off weaker members while maintaining their import restrictions.
3. WTO Members appear to be unable to agree on further liberalization (notably in services) and on adding new rules to the multilateral system to face new issues (such as the green economy, environmental subsidies or electronic commerce). This leads to a possibly problematic role of “gap-filling” and “law-making” for the DSS, which was not intended.
4. The parallel massive increase of regional trade agreements (RTAs), to which WTO Members are increasingly turning (including “mega-RTAs” such as the TPP and the TTIP), risks reducing the relevance of the WTO and therefore possibly of its DSS, which moreover might find competitors in the dispute settlement mechanisms of RTAs.⁴

This chapter addresses these issues and points to possible solutions, several of which have already been aired in various circles in the past. These proposals fall into two groups. The first group is meant to address the most pressing problem at present, which has been raised more than once by countries concerned at the Dispute Settlement Body (DSB), namely, delays in the process at the panel stage due to the lack of legal resources in the Secretariat to staff the many

⁴ It has been noted that RTAs have practically never been challenged in the WTO DSS. This could be due to the fact that they are considered by and large to be compliant with WTO obligations. Alternatively, it is possible that participants in RTAs refrain from challenging other RTAs in order to avoid provoking challenges to their own (the compliance of any RTA with all WTO requirements being doubtful).

panels that are being established.⁵ The second set of proposals looks at broader changes to remedy structural problems, but still through changes to the DSU that can be adopted within the current framework.

As a result, panel proceedings that should in theory take not more than six months (Article 12.9 DSU), but which in practice took around one and a half years in “normal” cases until recently, now may well take between two or three years from the formal establishment of the panel by the DSB to the circulation of their report. Panel reports are thereafter subject to appeal, where the Appellate Body faces increasing difficulties in respecting the short 90-day period prescribed for issuing its own reports, not to speak of the further possible proceedings before full implementation by the losing party.⁶ This time lag undermines the value of any favorable decision for obtaining effective redress against domestic measures in breach of WTO commitments, which is especially damaging in respect of temporary measures such as anti-dumping duties.

More broadly, this dysfunctional operation of the DSS, in disregard of one of its basic tenets and praised features, namely its speed, may undermine the whole operation of the system and recourse to it as the key instrument for ensuring respect of trade-opening commitments. As stated by Korea at the DSB meeting of August 31st, 2015:

“WTO disputes are not about abstract disagreements. Real world economic interests underlay every dispute. There were real people suffering while a dispute was pending (...) The problem would get worse if left unaddressed. Long delays created perverse incentive by lowering the cost of adopting and maintaining WTO-inconsistent measures,

5 A forceful complaint was that by Korea at the DSB of August 31st, 2015. Korea complained that in DSS 488, where Korea challenged US anti-dumping measures, the Secretariat had notified Korea that the panel established on March 25th, 2015 would not begin its work until the end of 2016 at the earliest, a date some 15 months from the time Korea had been notified of the delay, “not because the panelist were unavailable, but due to the constraints affecting the Secretariat.” Korea pointed out that this “remarkable, extraordinary, unreasonable delay” in light of both the DSU provisions and the economic reality, just for the case to get started “was almost twice as long as the period foreseen by Art. 12.9 DSU between the establishment of the panel and the circulation of the report.”

6 As an example, at a recent DSB meeting in 2015 Canada complained that four and a half years after the establishment of the panel, the COOL dispute with the United States was still far from being settled. After the panel the appeal, the fixing by an arbitrator of the reasonable period of time for the US to comply that was not respected, a compliance panel (Art. 21.5 DSU) against the United States by Canada and Mexico (the other complainant) where the panel and the Appellate Body found that the measure taken by the United States had not brought compliance (but possibly even worsened the breach), the arbitration panel (Article 22.6 DSU) was just starting its work to establish whether the countermeasures announced by Canada and Mexico were excessive in comparison with the trade loss caused to them by the COOL measure, as submitted by the United States. President Obama announced the repeal of the relevant US provisions on December 18th, 2015, just a few days after the arbitration panel had concluded its work, determining the level of retaliation that Canada and Mexico could put in place to offset the adverse effect of COOL on their exports. For a realistic view, see “Torture by Tariff – Retaliating against unfair trade practices is a calculation in cruelty”, *The Economist*, June 20th, 2015.

insisting, rightly, that they would not be subject to review by the WTO for years. Members could therefore expect more protectionist measures and more, not less disputes being brought to the WTO. These in turn, would cause further delays, prompting a vicious, never-ending cycle. It was in the interest of everyone, the parties, the wider membership and the Secretariat not to let this happen.”⁷

It is curious, however, that Korea itself, followed by other speakers, did not ask for more effective remedies – which the Director-General (DG) instead initiated thereafter – beyond increased transparency and information from the Secretariat as to the reasons for the “queue,” and as to the situation in the line and the outlook for “their” case being decided. The same attitude prevailed in the discussion that followed the DG’s lengthy and detailed statement at the DSB of October 28th, 2015 where he made the point that the problems would not be resolved just through administrative measures and a shifting of resources within the Secretariat. Several Members acknowledged this issue and decried the negative consequences of the current set on the effectiveness of the DSS, but abstained from launching any ideas for tackling the problems more seriously.⁸

7 Doc. WT/DSB/M/ 367, pp. 22-29. The concerns of Korea were shared at the meeting by a number of countries, starting with Guatemala (whose delegate stated aptly, “[t]he WTO dispute settlement system was one of the most effective and prompt international systems of adjudication. Victim of its own success, the system faces the risk of becoming slower. If no effective action were taken to address this unfortunate situation, the principle of “prompt settlement of disputes” in art. 3.3. DSU would become a mere “best effort” provision, not more than an illusory aspiration.(...) long delays in the DSS mechanism may create perverse incentives for the adopting political motivated WTO-inconsistent measures.” Others interventions came from (in order) Chile, China (“this unprecedented situation would seriously undermine the effectiveness and credibility of the WTO DSS”), Australia (“willing to consider any option that might help alleviate the current situation and improve the system over the long term. This included ensuring that the Secretariat had the resources needed to service disputes in a timely manner and also exploring ways for the Membership to reduce the burden on the system in terms of the length and complexity of disputes”), Russia, Mexico, Pakistan, Japan, Brazil, Canada, India, (“the credibility of the system was at stake”), the European Union (“manage the situation at hand” and “find solutions to the mid and long-term situation against the background of ever increasing pressures in the WTO DSS”), Argentina, Chinese Taipei and Norway. In contrast with the serious concerns voiced by most other countries, the United States was more restrained, stating briefly that “Korea has raised an important systemic issue (...) This raised some significant concerns, particularly in light of the fact that the WTO DSS had, for many years, operated with admirable concern. The US shared the view that members needed a better understanding of the causes behind delays so that they could develop and consider appropriate solutions.”

8 See the minutes of the meeting at WT/DSB/M/369 of January 20th, 2016, p. 20. DDG Brauner has been entrusted by the DG to follow up with the Members on these issues.

Proposals

This chapter subscribes to the practical measures at the administrative level that the DG has declared he is implementing at recent DSB meetings.⁹ At the same time, the current initiatives of the DG for increasing human resources – i.e. competent lawyers – in the Secretariats of the Legal Division and Rule Division that service panels does not seem sufficient to fix the problem. Other solutions may be called for that go beyond the competence of the DG.

Accordingly, the second set of proposals hereunder are more far reaching and forward looking, as they are meant to address the long-term sustainability of the DSS with regards to effectiveness and outputs. While these proposals do not require any overhaul of the current system, and nor would they affect the basic tenets of the original WTO DSS, in order to be adopted (as would any other proposal to this effect) they would require a broad consensus of the membership that is currently lacking, and not just in relation to these issues.

Those more substantial reforms to resolve this issue at the *panel level* would require considering more far-reaching options, such as:

1. Discouraging the bringing of complaints to the panel stage by making the initial phase (consultations) less of a mere formality, possibly with the engagement of the DG and resort to mediation and conciliation
2. Putting more financial resources to the service of the legal Secretariat, overcoming the zero-growth budgetary constraint that tilts in favor of first shifting resources within the WTO Secretariat without the possibility of adding new resources from the legal market place
3. Reorganizing the legal Secretariat by merging the Legal Division with the Rule Division, a distinction which reflects a division of work from GATT times and which is not just any more
4. Enlarging the available pool of panelists, resorting also to non-governmental panelists from third parties in any dispute; using more systematically available competent panelists (leading to the de facto creation of a pool of recurrent, semi-permanent panelists); and reducing procedural delays

9 His first intervention on the subject was at a DSB in September 2014, when he announced the creation of 15 new lawyer posts in the three dispute settlement divisions: Legal Affairs, Rules, and the AB. However, the organization had difficulties in filling these. In his address to the DSB on October 28th, 2015 the DG explained in detail the further steps he had taken and was taking to mitigate delays, consisting mostly of reallocating of personnel; hiring new legal staff; adjusting the grades and salaries to the competence of the lawyers, taking into account the competition by law firms; increasing internal mobility; and pooling junior lawyers of both divisions assisting panels. This should result in more efficiency and has already nearly doubled the relevant positions – from 30 to 57 – since 2013.

due to the “interim report” and translation (the availability of a greater number of more devoted and competent panelists could in turn make it possible to rely more on them also for drafting, as is the practice in both international courts and investment or commercial arbitration)

5. Making the disputing parties pay a share of the costs of the proceedings, which are currently charged to the whole membership.

Other phases and aspects of the DSS also need interventions to make them more efficient.

As to the *Appellate Body*, in view of the fact that the number of disputes brought to the panels is ever increasing so that very soon it will also the appellate stage, possible remedial solutions are:

6. Staffing the Appellate Body more adequately
7. Increasing the number of Appellate Body members from seven to nine
8. Making their position permanent, a status that would also better ensure in the future the selection of competent, diverse and truly independent judges
9. Making their reappointment for the second four-year term automatic, or replacing the two four-year terms with one non-renewable seven-year term.

As to the *implementation phase*:

10. The monitoring role of the DSB should be made more effective in order to induce more prompt compliance.¹⁰

The procedure should be tightened so that the prospective nature of WTO remedies (the obligation to comply not being retroactive from the date of the breach but to be implemented only after a “reasonable period of time” from the adoption of a panel or Appellate Body report) does not reward the dragging of feet by the losing party with regards to compliance with adverse decisions.

Maintaining the efficiency of the DSS and its effectiveness in ensuring compliance with the WTO multilateral trade rules entails broader benefits beyond ensuring the effectiveness of expected trade openings from the commitments that WTO Members have undertaken, as important as these are.

It ensures at the same time the role of the WTO as the guardian of the multilateral trading system and the position of its multilateral rules as the accepted global framework within which interested countries may engage in regional trade agreements. RTAs should be the basis for extending international

10 As advocated by Canadian Ambassador Jonathan Fried when he was chairman of the DSB in 2013.

cooperation and trade liberalization (“WTO-plus”) without endangering the WTO *acquis*. They should represent building blocks, and not stumbling blocks, by establishing supplemental frameworks to further facilitate trade through coordinated regional action which should be supportive of the multilateral rules.

It must be recognized that the possible solutions to the current problems set forth above are not a quick fix that may be implemented without WTO Members engaging in the issues, evaluating the most appropriate remedies and being open to looking for shared improvements. That said, this is not an out-of-reach ambitious program or an all-comprising shopping list.

Rather, it is a realistic and modest agenda for fixing, within the existing framework, the current problems and enabling the DSS to go on serving the WTO Membership and complying with its objectives and purpose in the years to come. We do not propose to transform the panels in a first instance tribunal, or to abolish the adoption of panel and AB reports, or other similarly radical overhauls.

Moreover, there is a specific instrument for Members to discuss and elaborate the necessary amendments to the dispute settlement rules. This is the DSU review negotiation framework agreed by a Ministerial Declaration in 1994 and extended by the Doha Ministerial Declaration in 2001, under which amendments to the DSU may be agreed without having to activate the cumbersome WTO amendment process. This exercise should have been completed first by 1997/1999, and then by 2003, but it is still going on indefinitely at an almost standing pace.

The DG’s statement to the DSB of October 28th, 2015 presented the various measures he has put in place in order to add resources to the Secretariat to address the most pressing problems, but it warned the Members that more is needed. However, the unconcerned attitude of most WTO Members as to these issues, at least until recently (they see the problems but prefer to leave any solution to the DG, though conscious of its limited capabilities to resolve them), does not bode well for any effective solution.

On the contrary, the DSS not being too efficient and allowing delays in implementation and political twisting may even accommodate some frequent users of the DSS. They may view themselves more as defendants and thus not in a hurry to implement changes through politically difficult domestic processes of compliance, rather than as successful claimants eager to obtain as promptly as possible the other party’s due market opening to the benefit of its producers and exporters.

Analysis and Suggestions

The Current Situation

Results Achieved, Disputes Resolved, Legal Security Provided

On November 10th, 2015, the WTO website featured within its news items the statement of DG Roberto Azevêdo celebrating the WTO Dispute Settlement System (DSS) having reached the 500 mark.

The receipt of the 500th trade dispute for settlement, said the DG, “shows that the WTO’s dispute settlement system enjoys tremendous confidence among the membership, who value it as fair, effective and efficient mechanism to solve trade problems.” The 500th dispute was submitted on November 10th, 2015, when Pakistan filed a request for consultations with South Africa regarding the latter’s provisional anti-dumping duty on cement from Pakistan. The parties involved and the subject matter of the dispute are also significant, because they show that developing countries use the system both as complainants and respondents in South-South relations, and that trade remedy measures feature importantly in matters brought to the WTO.

The news item included comments and data that can be the starting point of our analysis, taking stock of the achievements of the DSS as an introduction for addressing the current issues in a system that has been, and is, successful in offering an orderly rule-based solution to trade frictions, but that shows signs of stress (in part due to its own success).

The success is evidenced by the fact that resort to the DSS has become a normal feature in the operating of the multilateral trading system, displacing resort to unilateral measures. Practice has confirmed what had been set forth in Article 3.10 DSU, namely that “requests for conciliation and the use of the dispute settlement procedures should not be intended or considered as contentious acts.” This setting distinguishes the WTO from other international fora, where respondents often raise lack of jurisdiction as a preliminary objection to escape the process. It makes it more business like, as is the case in the national context.

Of the 500 disputes notified to the WTO, only 282 have been brought to litigation. Resolution through bilateral negotiations, including formal withdrawal of the request, has been notified to the WTO in 110 of the cases, while the parties have not informed the WTO of the status of the other 108 (which must be considered dormant or de facto settled).¹¹ As of the end of

11 This lack of information signals the need to strengthen the obligation of Members to notify the WTO in a timely manner of the status and outcome of all disputes that have been formally filed.

2014, 201 panel reports had been issued, of which 136 had been appealed (68% of the total, on average). In 2014 there were 13 panel requests appealed, while the AB issued eight reports concerning five matters.¹²

In 2015, by the end of November four panel reports had been issued covering five disputes and 11 had been adopted by the DSB, while the AB had issued appellate reports in four disputes on different subject matters.¹³

A measure of success is also the broad participation of WTO Members in the process. As of the same date, about two-thirds of the Members (102) have participated in dispute settlement proceedings, either as parties (claimants and/or respondents) or as third parties (35 Members as third parties only). Looking at the consultation requests, developing and developed countries are equally represented as complainants, while complaints are mostly directed towards developed countries.

As can be expected, the largest economies are both the most frequent initiators of cases (with the United States leading with 108, followed by the European Union, Canada, Brazil, Mexico, India, Japan and Argentina all above the 20 mark) and the most frequent defenders (with the United States again leading with 124, followed by the European Union, China, India, Argentina). Finally, the compliance mark is said to be about 90%. Countermeasures in the form of withdrawal of benefits, i.e. imposition of selective additional duties, have been imposed only in a handful of cases, while no Member has ever denied responsibility to comply with an unfavorable final decision.

Of course the number of disputes is not by itself a sign of a healthy system; the ability to process them timely and according to the rules is.¹⁴ Notwithstanding some delays in full compliance, there is no sentiment that WTO Members have become less inclined to respect the rules. On the other hand, a certain surge of national anti-dumping measures, as monitored by the AD Committee, could be a sign of increased pressure on export markets at a time of economic

12 The data provided are drawn from those provided, mostly in the form of tables, by the DG in his statement to the DSB of October 22nd, 2015, those annexed to the AB Report for 2014 and those included in the news item of November 12th, 2015 on the 500 mark. Some data are not easy to compare, especially since there is a difference with regards to the relevant year between panel and AB reports *issued* and *adopted* by the DSB. Moreover, some proceedings concern several disputes brought by different claimants against the same measure of the respondent State, that are examined together by a single panel. On the other hand some appeals are formally separate (and counted individually) because the claimants are different but are dealt with in a single report.

13 The exact numbers do not always match because of the different practice of the panels and the AB in calculating as single or separate disputes those in which different claimants challenge the same measures of the respondent state, the same panel being appointed to hear all the challenges.

14 According to the AB Report for 2014, “[i]n its first 16 years the DSB has handled disputes spanning over USD 1 trillion in trade flows” (WTO, 2015, p. 3).

slowdown, to the point of being a sign of resort to unfair competition.¹⁵ This is possibly a cyclical phenomenon, rather than a structural disregard for the rules.

In fact, Article 3.7 of the DSU would discourage Members from bringing disputes which might be resolved amicably without even resorting to the system, stating that “[b]efore bringing a case a Member shall exercise its judgment as to whether action under these procedures would be fruitful” and that “[a] solution mutually acceptable to the parties to the dispute and consistent with the covered agreement is clearly to be preferred.” In the same spirit of not considering the starting of a case to be an unfriendly act and encouraging at the same time parties to exercise some kind of self-restraint when considering bringing a case, Article 3.10 states in its final sentence that “[i]t is also understood that complaints and counter-complaints in regard to distinct matters should not be linked.”

This notwithstanding, on several recent occasions the initiation of a case by a country against another country has been immediately followed by the initiation of a separate case by the respondent in the previous case against the first country (notably between the United States and China and between Argentina and the United States and the European Union). Although there is no evidence that the second case was a kind of tit-for-tat response to the first one, this belief has been informally expressed as a sign of an abuse or political strategic use of the DSS contrary to its purpose.¹⁶

Finally, the smooth functioning of the DSS and the accumulation of consistent interpretations of key provisions of the WTO agreements, while not discouraging the bringing of new disputes, has made reliance on those provisions more firm. Outcomes are more foreseeable, thanks to the role of the AB in providing consistent case law on which panels in turn can rely. The overall role of the DSS has been expanded by the lack of action by Members in other capacities. Authoritative interpretations by the General Council acting under Article IX of the WTO Agreement have never been issued and other quasi-legislative action by Members, such as within WTO specialized

15 This could be the situation in the steel market, where sources indicate overproduction in the face of a decrease in demand (see <https://www.steelorbis.com/steel-news/latest-news/oecd-steel-committee-calls-for-immediate-action-to-address-excess-capacity-909449.htm>).

16 See Feinberg and Reynolds (2006); European Commission, Press Release (IP/13/772), European Union requests WTO Panel on Chinese Anti-Dumping duties on Steel Tubes, August 16th, 2013, available at <http://europa.eu/rapid/press-release-IP-13-772-en.htm>

committees, has been scant. Thus the DSS has remained the only source of authoritative guidance for the multilateral system at large.

The Increased Number and Complexity of Disputes

In its statement at the DSB on October 28th, 2015, following that of September 26th, 2014 on the same issues and informing the Membership of initial measures undertaken by him to face the problem,¹⁷ the DG gave a variety of information and figures evidencing the increased use of the DSS and the increased complexity of cases that are putting a strain on the resources and generate delays. The DG has pointed to the number of active panels that are operating at the same time, which reached 30 as of September 2015 (compared with 29 in 2014,¹⁸ and an average of 20 between 2000 and 2013). The number of new panels established by the DSB has also increased from six in 2010, to nine in 2011, to 11 in 2012, to 13 in 2014 and finally to 15 by September 2015.¹⁹

Disputes have also become more complex in that more domestic measures of the respondent country are being challenged – currently each dispute involves an average of 28 measures and 180 claims. The evidentiary burden before panels is also more demanding – one ongoing dispute (and not one of the two massive Boeing-Airbus aircraft disputes, which are still before the panels under Article 21.5 at the compliance stage) has reached more than 1,700 exhibits just at the initial stage. “On average, there are three times as many exhibits per panel now than in early WTO days,” noted the DG.

Another complexity relates to the requests by parties for preliminary procedural rulings (for example, to declare some claims inadmissible because they were not included in the initial request for consultations), which has become almost a standard feature in panel proceedings, adding submissions or exhibits, and therefore requiring more time of the Secretariat and the panelists.²⁰ This is a typical lawyers’ trick that shows how much the system has tilted – as have

17 An important initiative of the Legal Affairs Division has been the launch of the WTO Digital Dispute Settlement Registry, which will allow electronic filing of submissions and secure access to briefs and documents by the parties, besides serving as an electronic repository of all panel and AB records and providing easy online access to non-confidential information on cases to the public.

18 Nineteen panels in operation (12 in trade remedies and seven in other areas), 11 in composition, besides three appeals and two arbitrations on the reasonable period of time pending.

19 The issue of delays at the panel level caused by resource constraints in the Secretariat had been already raised at the DSB in 2014, and the DG explained the shifts and increase in legal resources he had undertaken in a statement at the DSB meeting of September 26th, 2014. This statement and the data provided are to be found in the AB report for 2014 (WTO, 2015, p. 93).

20 The high number of third parties in many proceedings (up to 36 in a recent case) adds also complexity in the handling of cases by panels.

other arbitral *fora* – towards judicialization, when a more conciliatory approach originally prevailed and was assumed.

Suggestions for Tackling the Problems

Panel proceedings: Possible Remedies to the Growing Delays

As I have explained above, the first effect of the increase in the number of disputes brought to panels is the delay in the effective initiation of the work by panels after the DSB has established them formally at the second meeting in which a Member has requested so, pursuant to Article 6.1 DSU. The DSU envisages in Article 8.7 that a panel be composed – that is, the panelists be appointed – 20 days thereafter, if the parties agree on the names suggested by the Secretariat (Article 8.6), or within an additional 10-day period if the DG appoints them due to lack of agreement. Recently, however, the practice has been for several months to elapse between establishment and composition, or between composition and initiation of the panel process. This is not due to procedurally difficulties but is a deliberate, inevitable choice by the Secretariat because of a lack of resources to staff the panels. The difficulty of finding suitable panelists due to the high demand, caused by the number of panels operating at the same time, adds an increased layer of difficulty and possibility for delay.²¹ It must be said that the situation of an adjudicating body to which a dispute has been submitted not even starting to examine the matter for several months is not unprecedented at the international level, where various courts and their member states strive to find solutions to the increasing recourse to adjudication.²² This is however not a justification for the WTO not sticking to its short deadlines which are one of the most distinctive and positive features of its dispute settlement system.

The DG itself underlined in its statement that the measures he was undertaking – reinforcing the human/ legal resources available to panels and reorganizing the cooperation between the Legal and Rules Divisions – would not resolve

21 Besides the 15-month delay complained about by Korea at the DSB of August 31st, 2015 referred to above, the most recent document on the issue is telling. On October 6th, 2015 the chairman of the panel in a case between the European Union and Brazil (joined to one on the same issue initiated by Brazil against Japan, DS 472 and 497) informed that the panel established on December 17th, 2014 and composed more than three months later on March 17th, 2015 expected to issue its report by the end of 2016, more than two years after the European Union had obtained the institution of the panel in order to obtain the withdrawal of the measures by Brazil that it had challenged.

22 Therefore in the European Union it was decided in 2015 to double from the numbers of the judges of the first level tribunal (the General Court) from 28 to 56. At the European Court of Human Rights, various procedural devices have been introduced through the years (such as increasing the possibility of summarily dismissing petitions for manifest inadmissibility) to cope with the explosion of recourses (which, however, are predominantly from private parties in both *fora*).

the structural problems or prevent the increase of the backlog.²³ The DG invoked the cooperation of the Members, specifically of the disputing parties, to “alleviate the pressure on the system” and to avoid a collective failure. In this respect, he alluded to “Member-driven, demand-side solutions,” without indicating specific initiatives, which might be beyond his powers. He launched, procedurally, a cautious consultation process with Members within the WTO to devise solutions that could be implemented by best practices without implying DSU amendments (such as limiting the number of pages of briefs or the number of exhibits).

It is unlikely, however, that the tendency to have recourse to the DSS will slow down, in view of the increased favor for litigation at the international level, the increase of instances where trade obligations collide with the exercise of domestic regulatory powers, and the increase in WTO Members that are actively engaged in international trade matters. Innovative remedies must be devised by looking at and tackling the roots of the problems.

The inability of the current system to cope with the increase in litigation is due in great part to its structure, which at the panel and Secretariat levels is still basically patterned after the GATT model of panels. As is well known, these panels were made almost exclusively of governmental experts, picked *ad hoc* to resolve occasional specific disputes among trade diplomats in Geneva familiar with the system, reflecting the non-legal character of trade disputes in those days.²⁴ Even today, panelists are not professional judges or arbitrators – about half of them are trade diplomats based in Geneva who do not have a legal degree and normally work for their government. The rest is made of governmental experts, rarely are academics resorted to.

As a consequence, these panelists have to rely heavily on the lawyers of the Secretariat assigned to each panel (one senior and one junior, as a rule) to perform their job, from research, to organizing hearings, to drafting. In the abstract, this approach appears contradictory in view of the professionalization required and legalization inserted in the system, but WTO Members are attached to the tradition of being judged by their peers and also value the assistance of the Secretariat as a guarantee of consistency.

Now that the flow of cases is constant and sustained, similar to or perhaps even more so than in a regular court, the system will be increasingly unable

23 The merging of the two divisions could also be envisaged, fully pooling the resources devoted to the DSS while maintaining the distinct expertise of the Rule Division in trade remedy disputes.

24 Small but important efficiency innovations could also concern the composition of panels, where parties often disregard the provision of Article 8.6 that “[t]he parties to the dispute shall not oppose nominations suggested by the Secretariat under the same provision except for *compelling reasons*,” thus causing additional delays; and the suppression of the Interim Review Stage (Article 15), which has become redundant with the introduction of appeal.

to perform its functions effectively unless (a) the Secretariat is expanded in consequence, including its budget; and/or (b) panelists are more devoted to the task and professional, that is, available on short notice to actively and exclusively perform their tasks and able to do so more autonomously.²⁵

This suggested configuration is found both in permanent international courts and within international commercial and investment arbitration under different models. At international courts, judges are mostly full time and are assisted by a centralized secretariat and/or by one or two full-time individual clerks. The secretarial support is much less in international arbitration, even compared to the WTO – arbitrators are selected among recognized experts in the field who are able to research and draft by themselves, possibly with the support of personal assistants from universities or their own law offices.²⁶ The support of the secretariat of the institution is limited to procedural matters and formal external review of the decision as autonomously prepared by the arbitrators themselves.

At the WTO such a development, that is, engaging more panelists while maintaining the unique role of the Secretariat, would in turn be facilitated by broadening the pool of potentially available panelists. The first easy change is to allow nationals of third parties to a dispute to be selected as panelists, provided they are non-governmental. Currently, nationals both of the litigating parties and of third parties can be appointed only with the consent of the parties (Article 8.3). Besides depriving the system of competent experts who could act as panelists²⁷ and thus relieving the shortage, this restriction leads to the panelists being chosen mostly from a small group of (small, mainly developing) countries that are rarely involved in disputes. This means the representative character of the adjudicators is not in line with the geography of the litigants and the issues raised.²⁸

Also, the procedure for selecting panelists, which is currently rather cumbersome and entails a delicate interaction between the Secretariat, the parties and the prospective panelists, should be streamlined so as to discourage parties from dragging their feet (Malacrida, 2015).

25 In December 2015 the General Council adopted a new fee pattern whereby non-governmental panellists now receive CHF900 per day and government panellists CHF300.

26 The differences between the WTO DSS at the panel level and ISDS, especially as concerns origin, qualification and the role of the adjudicators, has been addressed recently in Pauwelyn (2015).

27 This means that in practice, potential US, European, Japanese, Canadian, and Chinese panelists are hardly ever appointed, since the respective countries almost always participate as third parties to proceedings when they are not the main parties.

28 Joost Pauwelyn has noted that by contrast, for investment disputes at ICSID, where most challenges involve developing countries, most arbitrators chosen are nationals of developed countries (Pauwelyn, 2015).

Transferred to the WTO, either model would require:

- *More financial resources* to the legal Secretariat (Legal Affairs and Rule Divisions), also for compensating panelists;²⁹ adequate additional funding cannot be made available by just shifting funds within the budget, and a real increase of the budget and therefore of the members' contribution would be required
- Having recourse to a (probably not so) *small group of recurrent panelists*, as is already de facto the case,³⁰ who should be able to ensure availability and capability of operating autonomously; they should therefore not be engaged currently in governmental work and be remunerated adequately.

Panels could thus operate somewhat like the AB, their members meeting for longer periods in Geneva during proceedings and immediately thereafter for the deliberation of their report. It would be for the Secretariat to go on giving support to the panelists in the form of research, previous case law and precedent, while active drafting could be more in the hands of the panelists or, in any case, of the chairman. The current role of the Secretariat would remain necessary in order to ensure that these ad hoc panels, composed of diverse members, do not endanger with their individual decision making the consistency of case law (which is, in any case, subject to appellate review).

Such an evolution would not even require changes in the DSU provision. It would probably entail a change in the mix of panelists' backgrounds. There would be fewer active trade diplomats and more retired experts and persons with different backgrounds, such as academics and former officials from international organizations. Since high-quality reports are a must that is advocated by everybody concerned it is difficult to see how this quality can be maintained without changes to the current system. The challenge is that the more and more complex disputes and sophisticated arguments (moreover increasingly exposed by expert lawyers from specialized resourceful law firms) require increasing:

- The legal competence of the adjudicators
- The availability of legal support to them
- The time they must be able to devote to each case
- Their remuneration.

29 Governmental panelists currently work for free since they are supposed to act for the WTO during their working hours (the WTO pays a small sum to the Members that lend them); the others receive a small *per diem*, which does not reflect the engagement that should be required of them, even after a recent small increase. The issue has been recognized and an increase was decided in December 2015, see note 24.

30 Pauwelyn (2015) assessed that there are 15 panelist that have been appointed more than six times in recent years, and a high number of "single shooters."

What this change requires is for sure *additional financial resources*, whereas Members appear/like to believe that quick, high-quality and efficient justice may be obtained at no cost – an obvious impossibility. The mantra that Members are not ready to accept increases in the yearly budget (“zero-growth”) of course renders a solution quite difficult.

Hardly anybody has looked at *the cost of the DSS*, how it is financed and how it is apportioned among those who directly benefit from it. There is no accurate breakdown of the general costs of the WTO Secretariat and those pertaining to dispute settlement, because it appears that a consistent share of the latter (above the official figure of only 13% of the total) is charged to general administrative costs. Looking at the official data on the WTO website, however, it appears that the services of the organization cost little in absolute terms to the Members, and even less so the Dispute Settlement System.

The United States’ contribution to the total WTO budget in 2015 is US\$22 million, China pays \$16.8 million, Japan \$8.7 million, Brazil \$2.4 million, and the EU members together (although they contribute individually) about \$75 million. Without commenting on the incredible imbalances that these figures reveal, especially considering the frequency of recourse to DSS by individual Members (such as Austria contributing almost as much as Australia, and Singapore almost twice that of Brazil), one is on the safe side submitting that just the costs of the lawyers engaged by either parties (including the lawyers of the industry concerned standing behind them) in the cases involving the United States are higher than the contribution of the United States to the whole WTO budget (and this is the same for any other country involved in disputes).³¹

If the overall budget devoted to the DSS cannot be increased (some Members may even consider that this constraint is a way to put pressure on the DSS and its components by micro-managing any additional resource and their destination), one should reflect on an alternative solution – *making the users pay* for using the system (either through a fee system or having a separate budget for the DSS), as is the case in most courts and for the international secretariats administering institutional arbitration, such as ICSID or the ICC.

A final item concerns the *demand side*. Is it possible to limit the number of cases brought to adjudication?

In this respect, it would be worth studying how to make the pre-adjudication phase (the *consultations*) more effective, possibly providing for the input of the Secretariat as legal-economic support (What is involved economically? What

31 By comparison, it has been stated that the legal costs of an average ICSID case are \$4 million.

legal alternatives could be acceptable? What issues are in fact not in dispute?). Also, recourse to “good offices, conciliation and mediation” as envisaged in Article 5 as voluntary steps at any time during the dispute, for which the DG is available under Article 5.6, could be reinforced. They might be made compulsory as a preliminary stage for certain types of disputes.

Also related to the demand side is the frequency of compliance proceedings under Article 21.5 DSU. These are panel proceedings started by the original complainant who challenges the WTO consistency of the measures that the respondent has taken to comply with an unfavorable outcome. This entails the obligation to withdraw or amend appropriately the measure found inconsistent with the provisions invoked by the claimant (as per Articles 3.7 and 21). These disputes are heard by the original panel reconvened for this purpose, whose report may in turn be appealed. Article 21.5 claims are upheld in the DSS most of the time, signaling a lack of proper follow-up by respondents. At the same time, these proceedings consistently absorb resources of the system, especially considering that some of the most complex disputes have gone through this stage and thus appear almost never-ending (e.g. EC-Hormones; the two aircraft cases, Boeing / Airbus, US-COOL, just concluded after more than four years; US-Tuna II).³² Some kind of simplified or accelerated proceedings should be devised for these cases, which are often the most complex. In these cases, the parties involved could be asked to assume the costs, which are currently charged to the whole membership.

The Appellate Stage: Improving the Organization of the Appellate Body and the Selection and Reappointment Process in Order to Guarantee its Independence from WTO Member Interference and its Authority

The problems faced by the panel stage and the Secretariat due to the increase in the number and complexity of disputes are now reaching the Appellate Body – lengthier panel reports,³³ more appeals pending at the same time, more complex cases with more issues appealed and more challenges raised.³⁴ Cross appeals have also become more frequent. This makes the issuance of shorter reports, as is also often advocated for panels, quite difficult.

This “wave” may put additional pressure on the ability of the AB to perform its task in a timely manner while maintaining the high quality of its reports,

32 If the reports of the compliance panels in the two aircraft cases (DSB 316 and DSB 353) are issued as announced in mid-June 2016, this will be around four years after the two panels were composed in 2012. The *Australia Tobacco* dispute will also have lasted about four years at the panel stage if the report is issued as announced in mid-2016.

33 The number of pages of “average” panel reports has increased from 49 in 1996-2000 to 183 in 2010-2014, as reported in the DG Statement of September 26th, 2014 in the AB report for 2014 (WTO, 2015, p. 88).

34 This evolution has been highlighted by the AB in a Communication of May 30th, 2013 (“The Workload of the Appellate Body”).

for which it is generally praised and which represents a basis of the trust that the DSS inspires in Members and beneficiaries.

The organization of the AB under the relevant rules of the DSU (Article 17) leaves it little flexibility to cope with a regular higher number of cases; it is made of only seven members, who decide in randomly composed divisions of three, and it must issue its reports within 90 days.

As to procedure, the AB has adopted in recent years several practical measures within its competence to establish its “working procedures” (Article 17.9), including reducing the time framework in the initial phase of the process in order to have more time to examine the case and decide (in 2010), and asking the parties to supply summaries of their arguments, to be annexed to the AB report without need for the AB and its legal staff to perform this task directly (in 2014). In parallel with the increase of staff at the panel level, the legal staff of the AB – until recently a relatively small group of just ten lawyers – has also been marginally increased. The AB has lately suggested a limit to the volume of parties’ submissions in a communication circulated in October 2015, in which the AB gave evidence of its workload and the size and complexity of the cases, with a view to stimulating the debate with interested WTO Members and in the hope of a positive response.

Dealing with the case load and the complexity of appeals is directly related to the issue of *respect of the 90-day deadline*. The AB has tried its utmost to respect in all cases this deadline, to which Members attribute great importance, although a delay of a few days is irrelevant compared to the delays normally accumulated in the other phases of the proceedings, sometimes by decision of the parties themselves.

Going beyond this deadline is sometimes caused by the complexity of the case (such as in the aircraft cases), but recently it is more often caused by the overlapping of appeals that makes it impossible for the members of the AB to attend to multiple disputes according to the standard time schedule. The issue has been that a few parties, especially the United States, insist that this should be made only with the consent of the parties to the dispute. The AB has recognized that involving the parties is appropriate and has done so, but does not want its hands tied and to subordinate the establishment of its agenda, as necessary in these formerly labeled “exceptional cases,” to the will of the litigants in any given case. The debate has been ongoing for some time, fueled by criticism from some countries in the DSB when a deadline has been missed (although when this does occur it is usually just by a few days). The complaints have not been against extending the proceedings in case of objective impossibility of respecting the deadline, but focus on the lack of

previous agreement with the parties (the United States) or the lack of full information on the reasons thereof from the AB (Japan).³⁵ Other countries (the European Union, India and Brazil) pushed back against Japan's request, saying that micro-managing the AB schedule would not help resolve the issue of delays. An alternative is to have a custom-made schedule, agreed with the parties, for any case where the 90-day deadline does not appear not.

If the workload remains at the current level, relaxing the 90-day deadline by a few days on a case-by-case basis, or even replacing the 90 days with 120 days, will not resolve the issue. *The number of the AB members should be increased*, taking into account that when it was initially created with seven members, the Membership of the WTO was more limited and important current players in the DSB, such as China and Russia, were not even members. *Nine* has been suggested as a reasonable number of members; new human resources would be added, reflecting geographically the expanded membership without diminishing the collegiality on which the consistency of the AB case law and its independence rests.

The AB would benefit from (modest) reforms limiting the *risk of a reduction of the authority of the AB* as a pivot of the stability and the predictability of the WTO system. First, since the AB members are de facto engaged full time, it would be reasonable for the terms of their employment to reflect this situation. In case of full-time employment, a fixed monthly compensation might even be less onerous for the WTO budget than the current *per diem* arrangement.³⁶

Second, and more importantly, the issue of the *modalities of the renewal* of their tenure after the first four-year term should be streamlined. Until recently renewal was de facto automatic, and appropriately so, with the DSB extending any mandate as a matter of course if the AB member concerned had expressed his willingness to renew. More recently, under the impulse of the United States, the DSB has asked that the AB members coming up for renewal meet the WTO Members and be available for questioning. The issue has become sensitive – one could foresee a situation in which countries would subtly interfere with pending cases and try to influence the judges, making the renewal of AB members dependent upon their answers.³⁷

35 Most recently at the DSB meeting of October 28th, 2015.

36 Making the position full time would also make potential candidates more aware of what the position entails and would thus encourage more competent candidates to come forward.

37 This process is reminiscent of the hearings by the US Congress of candidates to the US Supreme Court proposed by the president, but the setting, the position of the US Supreme Court and the individual role of its judges is quite different. On the other hand, one should not forget that the AB, however modest its name and institutional setting, is the only international court with compulsory jurisdiction (moreover in respect of broad sensitive matters) over states such as the United States, China and Russia, which usually accept to participate in international adjudication, if at all, only on an ad hoc, mostly ex post facto basis. Hence the keen interest of large economies in the selection of their future judges.

The solution was finally found by holding an informal DSB meeting on November 12th, 2015, with this encounter taking place on the understanding that questions by delegations would be of a general and systemic nature only. In the subsequent, formal DSB meeting of November 25th, Singh Bathia from India and Thomas Graham from the United States were reappointed by consensus.

In view of this development, a one-time term, for instance of seven years, would avoid any inappropriate impression of pressure and interference in the reappointment process by individual WTO Members.³⁸ The current active engagement of key WTO Members in the appointment process appears excessive; it gives the impression that some key WTO Members try to form an AB composed of members who are responsive to their wishes with regards to their approach to interpretation and similar issues. The process has recently even entailed interviews in Washington and Brussels (a kind of roadshow to which candidates have had to submit lately) and the close scrutiny of their academic CVs and publications.³⁹ This resulted in a notable instance in 2014 when a qualified candidate who had accepted by all the membership was then vetoed by one country, leading to the repetition of the selection process.

The increased tendency for AB members to come from trade diplomacy and national administration, at the expense of academics and national judges (who are endowed with practical international experience as negotiators, arbitrators or administrators), risks diminishing the ability of the AB to reason and decide with full independence, impartiality and objectivity. This is irrespective of the personal integrity of all AB members, who have never been criticized from this point of view.⁴⁰ An appropriate mix of competences within the AB is key for it to operate at the highest qualitative level, irrespective of the ability of its dedicated legal staff. It is important that the AB be able to issue well-reasoned reports, based on a full knowledge of international law, that receive not only the approval of WTO Members but also praise from the community of academics and other experts in the field.⁴¹

38 There is a widely shared belief among those familiar with these developments that the unavailability for reappointment of the US AB members Merit Janow (in 2007) and Jennifer Hillman (in 2011) was prompted by the negative position towards their reappointment privately aired by the USTR at the time. The reasoning behind a country not supporting a member of its nationality in a body, such as the AB, that operates by consensus and where dissents are rare, anonymous and not capable of shifting the course of the case law, is unclear. This attitude may even undermine the trust of his or her colleagues in the independence of such member. In the case of a smaller country not supporting an outgoing AB member of its nationality, it is almost inevitable that the successor would be of a different nationality. This is what happened upon the resignation from the AB of Oshima from Japan shortly before the expiration of his term in 2012. His successor was the current AB member from Korea, Seung Wha Chang, and as a consequence, Japan "lost its seat," which it had held since the beginning of the AB.

39 Elsing and Pollack (2014) examined this issue through extensive interviews with former candidates.

40 On these issues see Shaffer et al. (2016)

41 See the piece by former AB member David Unterhalter of South Africa (Unterhalter, 2015).

The independence of the AB is fortunately assured by two factors. First, the collegial attitude of its members makes it impossible to single out an individual member's position on any specific issue from the outside. Second, the different, even opposing positions of WTO Members on these issues, as on many others, while paralyzing even modest reforms, has the advantage of making it unlikely that initiatives to reduce the authority of the AB will succeed.

As to the Implementation Phase

The DSS ultimately pursues a practical objective: maintaining the balance of rights and obligations, market access and liberalization commitments agreed upon by the Members in the various WTO agreements, discouraging breaches and redressing them as promptly as possible.

The *monitoring role of the DSB on implementation* is one of the features that makes the WTO DSS stand out in comparison to other international dispute settlement mechanisms, where implementation is ultimately left to the good will of the party concerned, under threat of diplomatic pressure or unilateral countermeasures.

Surveillance by the DSB should be made more effective, as advocated by the Canadian Ambassador Jonathan Fried when he was chairman of the DSB in 2013. It should not be just a formal exercise of registering statements or automatically authorizing countermeasures in the form of suspension of concessions when an adjudicative body has confirmed non-compliance.

Ways and means should be devised, based on 20 years of experience, to exercise collective pressure on a recalcitrant Member in order to *induce and facilitate prompter compliance*. One avenue might be to suggest ways to effect implementation, which is currently left completely to the party found in breach. This option is currently in the hands of panels and of the AB under Article 19.1 DSU, but they have generally refrained from using it. The reason is that these suggestions risk not being followed (they are not binding), thus indirectly diminishing the authority of the underlying holdings contained in the panels and Appellate Body report. A commitment to the DSB by a party obliged to comply might stimulate more active domestic engagement by the competent national authorities to effect timely and complete implementation.

The implementation procedure should also be tightened to induce compliance by avoiding that the prospective nature of (future) WTO remedies, which already favors non-compliant respondents, rewards even more dragging of feet by the losing party in implementing adverse decisions.

One possible way to reinforce the compliance process might involve rethinking the relationship between the imposition of countermeasures and arbitration *ex Article 22.6* when there is a dispute on the proportionality of the level of concessions that the winning party intends to put in place. Currently, the principle stated therein is that “[c]oncessions or other obligations shall not be suspended during the course of the arbitration.” As currently framed, this provision favors the party in breach, in that the application of trade sanctions against it is postponed. At the same time, it protects that party from being subject to unilaterally determined excessive sanctions by prohibiting their application altogether. A more efficient compliance-inducing mechanism should be devised (for example, providing for authorization to apply trade sanctions at the initiation of the Article 22.6 arbitration, subject to restitution with interest and possibly a penalty of sanctions applied in excess of the determination of the arbitrators).

Concluding Remarks

Some concluding remarks should address the interplay between the broader evolution of international trade relations and the functioning of the DSS.

On the one hand, it has been submitted that the existence of an efficient DSS makes concluding the Doha Round less pressing, since its smooth functioning alleviates the need to address difficult negotiating issues. The most contentious issues, so runs the argument, may be left to be resolved by the panels and the AB. This argument does not stand in my view, because adjudicating disputes concerning existing agreements cannot be a replacement for the making of new agreements, whether within the Doha mandate or “post-Doha,” especially if negotiations are meant to cover “new,” hitherto unregulated areas. Nor can dispute settlement “compensate” for the lack of further liberalization of trade, be it in the form of negotiated reductions of tariffs on goods or new concessions on services.

I do not believe that there is any evidence of the inverse either, namely that the efficiency of the DSS makes WTO Members wary of concluding new agreements; it would be always possible to carve-out some agreements from the DSS jurisdiction should this be the problem.⁴² The greatest challenge to the WTO comes rather from regional trade agreements, since difficult issues that are intractable at the global level may be agreed more easily between like-minded countries or countries with similar or complementary economies.

42 Thus in the TPP certain “SPS-plus” obligations have been excluded from the dispute settlement mechanism.

A multilateral response might be to resort to plurilateral agreements in which the WTO and its DSS maintain a role (Hoekman and Mavroidis, 2015).

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CHAPTER 5

“Behind-the-Border” Policies: Regulatory Cooperation and Trade Agreements

Bernard Hoekman¹

European University Institute and CEPR

Introduction

With the establishment of the World Trade Organization (WTO) in 1995, much of the vision of the drafters of the 1948 International Trade Organization (ITO) Charter was realized, albeit some 50 years later.² However, since its creation, WTO Members have found it very difficult to negotiate new rules of the game. Disagreements among countries regarding the benefits of committing to additional policy disciplines, most notably between the United States and other OECD nations on one side and emerging economies such as Brazil and India on the other, have impeded progress on the WTO’s traditional market access agenda (mostly tariffs and agricultural support). This in turn has precluded moving on to new issues.

The average level of tariffs for OECD member countries has fallen to the 3% range; for major emerging economies like China and India the average applied tariff is less than 10%. Policy-induced market access frictions and trade costs today are increasingly regulatory in nature. The rapidly changing composition of trade as a result of technical changes – reflected in global value chains that span many countries, and products embodying value added services

¹ This chapter draws in part on Hoekman (2015a, b) as well as research with Petros Mavroidis and Charles Sabel.

² The ITO was supposed to complement the World Bank and the International Monetary Fund in the area of trade-related policy, but never entered into force as a result of a decision by the US government not to submit the treaty for approval by the Congress.

that are connected to each other (the “Internet of things”) and the increase in cross-border data flows this generates, with associated concerns about data security and privacy – is moving national regulation to center stage. The associated agenda is not about deregulation – what is driving concerns in the business community are the trade-impeding (cost-raising) effects of *differences* in applicable domestic health, safety and security standards, prudential and licensing requirements, certification and compliance assessment procedures for both products and production processes used by suppliers of goods and services.

Continued deadlock in the WTO starting in 2008 led to the focus of attention in addressing such international regulatory spillovers shifting to other fora – notably preferential trade agreements (PTAs). The ongoing negotiations on a Transatlantic Trade and Investment Partnership (TTIP) between the EU and the US and the recently concluded Comprehensive Economic and Trade Agreement (CETA) between Canada and the EU are important examples of PTAs that include a significant focus on regulatory matters.³ This is a second-best solution, given that the organization of production and trade into international value chains/networks means that end products are impacted by many regulatory jurisdictions. PTAs almost by definition will not span all the countries involved in many (most) global value chains, thus limiting the positive impact that they can have in addressing regulatory differences and uncertainty for firms and consumers, while at the same time giving rise to the possibility that PTA-based regulatory initiatives may generate trade and investment diversion.

Trade agreements are not the only game in town to address regulatory spillovers. Governments may and have pursued different types of regulatory cooperation efforts, ranging from sector-specific initiatives such as mutual recognition agreements (MRAs) to cross-sectoral, “horizontal” efforts that center on “practice” and learning from international experience and more formal mechanisms such as the Canada-US Regulatory Cooperation Council (Canada, 2014) that operate independently of a prevailing trade agreement (i.e. NAFTA).

What follows discusses the general challenges confronting international regulatory cooperation from the perspective of reducing trade frictions. The

3 Only two chapters of CETA deal with reductions in import tariffs and the removal of discrimination in government procurement — that is, classic market access issues where there are direct restrictions on the ability of foreign companies to supply products. The majority of the substantive chapters of CETA deal with product regulation, customs procedures, trade facilitation, policies affecting specific services sectors, mutual recognition of professional qualifications, domestic regulation more generally, procedures for regulatory cooperation and dialogue, and sector-specific protocols (e.g. on the mutual acceptance of the results of the conformity assessment of good manufacturing practices for pharmaceutical products).

first section defines the task confronting policymakers and develops a typology of the types of initiatives that can be used to reduce negative trade spillovers created by regulatory differences. The next section discusses the question what role a trade agreement might play in addressing regulatory spillovers, something that arguably has not been considered seriously enough by the trade community. The third section briefly reviews some of the extant disciplines and provisions in the WTO that have a bearing on domestic regulatory policies. The fourth section does the same for recent PTAs. The fifth section suggests some limited initiatives that could be pursued under WTO auspices or in a plurilateral trade setting. The final section concludes.

Dimensions of Regulatory Cooperation

Competition between regulatory regimes is the default situation in international relations, with different jurisdictions independently applying their own set of regulations to products and producers. While competition implies differences in applicable standards across countries, over time, as learning occurs, there may be incentives to emulate more successful approaches and norms, generating convergence over time. Competition is a powerful discovery mechanism and a force that will help to identify more efficient forms of regulation to achieve a given objective. But competition may also have adverse outcomes. The commonly expressed fear of a "race to the bottom" is one possibility, albeit one for which there is generally little evidence. A much more frequent consequence of competition is excess costs associated with different regulatory regimes that have similar objectives. In such cases there are potential gains from cooperation.

International regulatory cooperation is difficult. There have been long-standing transatlantic efforts to cooperate on regulatory matters, with only limited success (Vogel, 2012). The most progress has been achieved in the European Union in the context of creating a single European market for goods and services, as this required overcoming the trade-impeding effects of differences in product market regulation. This was pursued through a variety of approaches, ranging from harmonization of new regulations to mutual

recognition (Pelkmans, 2012).⁴ The EU is of course *sui generis*. The more general challenge confronting the trade community is to identify approaches to reducing trade costs through regulatory cooperation in the *absence* of a political commitment to fully integrate markets and *without* supranational institutions that are tasked with reducing the market segmenting effects of national policies.

In principle, addressing this challenge should be facilitated if regulatory objectives are equivalent across countries and economies have similar income levels. Approaches may differ towards reducing risk and avoiding catastrophic events, but if goals are very similar, regulatory cooperation may reduce compliance costs without undercutting the attainment of national regulatory objectives. The agenda here is not just about reducing compliance costs for firms and thus prices for consumers. More important – and, indeed, a necessary condition for reducing costs (increasing efficiency) – is that cooperation enhances the effectiveness as well as the efficiency of regulation. Cooperation must be a mechanism that improves regulatory outcomes over time in all participating jurisdictions (Hoekman, 2015b). A basic question for policymakers is how best to design international regulatory cooperation so that it does so. This requires knowledge about the potential benefits and the political feasibility of cooperation.

Table 1 distinguishes between the magnitude of net economic gains from regulatory cooperation and the political and technical difficulty (cost) of implementing the necessary cooperation. In principle, cooperation should center on areas that fall into the bottom-right cell *D* and on efforts to move items from *C* to *D*. As important is to avoid investing resources in regulatory areas that fall into box *A*. Mapping policy areas into these different categories cannot simply be based on technical analysis but requires active engagement by regulators, business and consumers. Regulators should be interested in those activities and initiatives that increase their ability to achieve their mandate more effectively and efficiently. Business presumably would like to see compliance costs fall, while citizens and consumers may worry that cooperation will erode regulatory standards, resulting in a “race to the bottom.” This is a major factor underlying the strong resistance by some civil society groups in the EU, Korea and other nations to new PTAs that involve “deep integration” (see, for example, Cardoso et al., 2013 on fears that TTIP may do so). The result

4 Mutual recognition involves agreement that products legally introduced into the commerce of one jurisdiction may be sold and consumed without additional controls in another jurisdiction. To take the example of food safety standards, mutual recognition between *A* and *B* implies that *A* recognizes that the norms prevailing in *B* satisfy its own safety norms and vice versa. If the underlying norms in the two jurisdictions differ enough, such an approach is not feasible. Even if *A* and *B* harmonize their norms, trade still might be affected by redundant costs if both continue to inspect products before they are allowed to be sold. Only if *A* and *B* mutually recognize (accept) that their respective enforcement systems are effective will harmonization eliminate regulatory trade costs.

of these different entry points implies that not all issues will lend themselves equally to cooperation. Insofar as the areas of concern fall into boxes *C* or *D*, a precondition for cooperation is to address the worries of either regulators and/or consumers that make an issue area politically sensitive. But efforts to do so through joint learning and interaction should prioritize areas that offer the highest potential economic benefits. In some instances this may not be possible; in others it may require a substantial amount of time to establish the needed understanding and trust to allow cooperation to occur. There is therefore a dynamic time dimension to this two-by-two matrix.

Table 1: Net economic payoffs and feasibility of cooperation

		Political/technical costs	
		High	Low
Net economic benefits	Low	A	B
	High	C	D

Various approaches have been pursued to attenuate international regulatory spillovers (OECD, 2013). These include seeking to converge over time on the substance of new regulatory norms (harmonization and international standardization), accepting differences in regulation and focusing on putting in place processes to address negative spillover effects of such differences through mutual recognition agreements or determinations of regulatory equivalence, and efforts to increase “coherence” across regulatory regimes. The latter generally center on identifying good practices and basic principles such as transparency, consultations with stakeholders, use of impact assessments, and so on.⁵

Cooperation can be characterized along a spectrum of “soft” to “hard” depending on how binding (enforceable) the commitments are, with agreements ranging from “shallow” to “deep” depending on whether they entail commitments not to do something or go beyond that to require positive action. Efforts to increase coherence across regulatory regimes are an example of “soft” cooperation. They have been a central element of international initiatives on regulation pursued in the OECD and APEC, which focus on principles and processes as opposed to the substance of regulation.

“Shallow” types of cooperation may be limited to commitments to enhance the transparency and visibility of extant regulation and new regulatory initiatives,

5 There is of course an extensive literature on the various options and experiences; see for example, Vogel (2012) and OECD (2014). Much of the focus will (have to) be sector specific; see, for example, Arnold (2005), Bismuth (2010) and Verdier (2011) for analyses of services regulation.

or they may go further and involve creation of processes through which parties inform and/or consult each other or commit to providing opportunities for comment before adopting new regulations. Some instances of “shallow” regulatory cooperation may be relatively straightforward to apply to a large number of countries, as they are in the nature of focal points and guidance for national policy. Whether or not a country implements the principles or good practices will not have a direct effect on the realization of regulatory goals in another nation.

Deeper forms of regulatory cooperation have implications for the realization of regulatory objectives – they create interdependence between jurisdictions: the attainment of a regulatory goal in country *A* becomes a function of actions by country *B*. Deeper forms of cooperation span a range of possibilities, from harmonization at one extreme – i.e. adopting the same norms – to (mutual) recognition agreements or acceptance of the equivalence of regulatory regimes.

Table 2 illustrates different types of regulatory cooperation and lists a number international institutions and fora that have been created to support their implementation. There are many examples of both “shallow” and “deep” regulatory cooperation – the ones mentioned in Table 2 are just illustrative.⁶ Many (most) of these do not involve trade agreements, but some do. The alternative approaches can all be embedded into trade agreements. There are several mentions of the WTO in Table 2, reflecting the fact that its multilateral agreements – GATT, GATS and TRIPS – make references to harmonization (international standardization) and/or mutual recognition agreements, even if there is no legal obligation imposed on all WTO Members to harmonize their norms or to recognize those of trading partners (the WTO status quo is discussed below).

Coherence involves efforts among jurisdictions to ensure that the regulatory process conforms to what are generally accepted to be good practices (e.g. ensuring that regulation is transparent; that there is the opportunity for stakeholders, including foreign firms and governments, to comment on proposed new regulations; or that the process of regulatory development should be informed by an economic impact assessment or a cost/benefit analysis). The aim here is not to question or discuss the objectives or the substance of regulation. Instead the focus is on the process through which regulation is developed and implemented. Coherence is an important element of WTO

6 Major international regulatory/standards-setting bodies include the Codex Alimentarius Commission, the International Electrotechnical Commission, the UN Economic Commission for Europe (UNECE), the International Organization for Standardization (ISO), the International Air Transport Association (IATA), the International Accounting Standards Board (IASB), the International Telecommunications Union (ITU), the Basle Committee on Banking Supervision, the Financial Stability Board (FSB), the International Organization of Securities Commissions (IOSCO) and the International Association of Insurance Supervisors (IAIS).

disciplines on sanitary and phytosanitary (SPS) measures and technical barriers to trade (TBT) and has been the focus of work programs in organizations such as the OECD, various UN bodies and APEC for many years.

Consultation goes beyond joint efforts to define and implement good practices (coherence) and begins to engage with the substance of regulation and its spillover effects. Examples include the scope that has been created in the WTO to raise specific trade concerns (STCs) regarding (proposed) TBT and SPS measures (Wijkström, 2015) and the framework that has been established for consultations on regulatory matters through the Canada-US Regulatory Cooperation Council (RCC).

Table 2: A typology of regulatory cooperation and illustrative examples

	Global	Plurilateral	Bilateral
"Shallow" cooperation			
Coherence	BCBS, UNCITRAL, ISO; ICN; WTO	OECD, APEC, GPA; GATS (Telecom Reference Paper)	BITs
Consultation	OIE, IOSCO, WHO, WTO: TBT/SPS	EU; G20	RCC (Canada-US)
"Deeper" forms of cooperation			
Recognition (MRAs)	CIPM; ILAC; IAF	EU-US (various); ASEAN (various); ...	US-Australia (securities); Trans-Tasman MRA
Equivalence	SPS (WTO)	EU	EU-US air safety; ANZCERTA
International Standardization	UNECE, Codex Alimentarius; IMF; GlobalGap; VSS	FSB, ESMA, EU, ICH	RCC (new regulations)

Notes: *ANCERTA*: Australia-New Zealand Closer Economic Relations Trade Agreement; *BCBS*: Basle Committee for Banking Supervision; *BIT*: bilateral investment treaty; *CIPM*: International Committee for Weights and Measures; *FSB*: Financial Stability Board; *GPA*: WTO Government Procurement Agreement; *IAF*: International Accreditation Forum; *ICH*: International Conference on Harmonization of Technical Requirements for Registration of Pharmaceuticals for Human Use; *ICN*: International Competition Network; *ILAC*: International Laboratory Accreditation Cooperation; *OIE*: World Organization for Animal Health; *RCC*: Regulatory Cooperation Council; *VSS*: voluntary sustainability standards.

Deeper forms of cooperation go further in seeking to reduce the market-segmenting effects of differences in regulation across countries. Examples are agreements to (mutually) recognize a foreign regulatory process, efforts between regulators to determine instances where regulatory regimes are equivalent, and efforts to adopt common regulatory standards or conformity assessment processes – i.e. harmonization of norms. Such deeper forms of regulatory cooperation are difficult to achieve for a number of reasons. There may be (i) mandate gaps, in that domestic regulators are not permitted to pursue cooperation or have not been given the resources to do so; (ii) coordination gaps in instances where international cooperation requires several regulatory agencies within a country to work together; or (iii) informational gaps within and across countries, such as a lack of data on how a regulatory regime “works” (Hoekman, 2015a). Addressing these gaps requires institutions and processes that foster regular communication and repeated interaction. This is needed both across agencies within countries – frequently multiple regulators and government bodies are engaged in setting and enforcing product and process regulations – and across countries. This is non-trivial, especially in federal states where regulation is applied at the state level (for example, in 13 provinces and territories in Canada, 29 states in India and 50 states in the US). In the case of the EU, the 28 member states continue to have significant autonomy in the implementation of regulation in many areas.

Regulators frequently have their own mechanisms through which they interact with each other internationally. Governments at different levels (central, sub-central, municipal), regulators and international businesses are all engaged in mechanisms that entail cooperation with counterparts across borders (jurisdictions). Lead firms set standards for quality, health and safety for both products and processes that occur in their supply chains. They may cooperate in private standards-setting activities that have as a goal achievement of interoperability and minimum standards across supply chains. They may work in cooperation with non-governmental organizations (NGOs) and governments to do so (an example being the Global Food Safety Initiative). NGOs do the same – there is a plethora of different private standards-setting bodies that develop norms and offer certification services to companies that engage in international trade. The characterization of levels of “regulatory” cooperation in Table 2 also applies to the world of private standards, as is illustrated by the inclusion of several such initiatives.

What Role for Trade Agreements?

A key question for policymakers and stakeholders is whether, given a presumption that there are good reasons for pursuing regulatory cooperation, this should be embedded in trade agreements. Given a rationale for regulatory cooperation, what is the value added of tying this to a trade agreement as opposed to simply giving regulators a mandate to interact and work together to improve regulatory requirements and processes? Assuming a positive answer to the question on embedding regulatory cooperation in trade agreements, an ancillary question is whether this is best pursued through the multilateral forum (the WTO), through PTAs or both.

Trade agreements are designed to reduce explicit discrimination against foreign suppliers of goods and services. An implication is that traditional sector-specific regulation that entails barriers to entry lends itself to the reciprocal bargaining and market access commitments that are the core feature of trade agreements. As such regulation can be "captured" by incumbent firms who use their political influence to ensure that they have favorable treatment (Stigler, 1975), a very similar dynamic as that underpinning trade negotiations can be used to reform such types of regulation. However, while entry-restricting regulation continues to exist for some sectors – especially in some services – in the 1980s and 1990s regulation changed in nature. Regulation is no longer dominated by efforts to control the behavior of firms in sectors in which entry is restricted.⁷ Instead, the focus is on ensuring that markets are contestable and on the use of market conduct and liability rules that are (supposed to be) applied equally to domestic and foreign goods and services to do so, complemented by mechanisms to elicit revelation of information by firms on their costs (Laffont, 1994; Posner, 2013).

The source of regulatory trade costs lies in *differences* in regulations across jurisdictions and the need to comply with the requirements of multiple regulatory bodies in different countries. As already noted, reducing the market-segmenting effects of differences in regulations is difficult because of concerns that it may compromise countries' regulatory objectives and hinder the execution of regulatory agencies' legal mandates and obligations. This implies that reciprocal commitments to change national policies – the bread and butter of trade agreements – often simply will not be feasible. The nature of regulation is technical and dynamic, involving many actors with different degrees of autonomy and decentralization; moreover, regulators will respond

7 A caveat to this is that state-owned or state-controlled enterprises continue to be prevalent in many countries. Insofar as this is associated with barriers to entry, trade agreements are appropriate instruments through which to seek to impose market disciplines on such entities.

to differences in local circumstances and changes in knowledge over time. This makes it difficult – indeed, undesirable – to “negotiate” substantive changes in regulation or to impose regulatory harmonization or convergence by fiat. Instead, regulatory cooperation must be premised on mutual assessments of performance of regulatory regimes to enable regulators to assure principals (stakeholders, legislatures) that the other party has effective systems in place. In practice, convergence, if it occurs at all, will most likely be gradual, with partner countries over time moving closer to systems that are constructed and implemented the same way.

The increasing complexity and interdependence of modern economies that is reflected in the growth in collaborative international production networks (“global value chains,” or GVCs) has led to forms of what has been called meta-regulation (Coglianese and Mendelson, 2010). Meta-regulation involves the establishment of monitoring and learning regimes. Instead of presuming that regulators should define uniform rules based on scientific evidence, the aim of meta-regulation is to create incentives for companies to invest resources in regular collection and analysis of data to identify and mitigate specific risks they either confront or may generate. Such approaches are salient in the context of GVCs. For example, ingredients contaminated with pathogens are periodically introduced into global food supply chains and widely propagated as the adulterated foodstuffs are incorporated into diverse batches of processed products. The inadvertent co-production of hazards by firms that are part of international networks – often identifiable years after products have entered commerce – calls for regulatory approaches that recognize such possibilities and that are designed to generate and disseminate relevant data to all parties concerned on a timely basis.

As a result of the type of uncertainty that accompanies GVC-based production and extensive cross-border flows and interdependence, the regulatory problem becomes one of organizing and supervising joint investigation by firms of emergent risks and responding to them before they cause harm. This is a problem that calls for approaches that involve data collection, data analysis and data sharing. An example is the use of hazard analysis of critical control points (HACCPs) for pathogens, implemented on both sides of the Atlantic, involving a mix of administrative action, legislation and private standards (Sabel and Simon, 2011; Humphrey, 2012).

Can trade agreements support this type of regulatory cooperation? This is perhaps less obvious than often seems to be assumed. Trade agreements can be characterized as purposeful efforts to align the behaviors of key players (governments in particular, and through them, regulatory agencies) in a top-down manner. However, insofar as regulation increasingly revolves around

a decentralized effort at problem solving – i.e. bottom-up mechanisms – a potential role for trade agreements to support regulatory cooperation is by acting as a device to more credibly commit to pursuing the needed bottom-up approach by creating an institutional framework that promotes and supports this. Whether trade agreements can be designed to do so is an open question. While it is often argued that a major rationale and objective of recent mega-regionals such as TTIP and TPP is to address the costs arising from differences in or duplication of regulatory regimes, arguably there has not been enough engagement with the public at large to explain why it makes sense to address regulatory matters in these PTA negotiations and to ensure that all parties have a common understanding of what this will (and will not) entail.

Perhaps the most straightforward case for using trade agreements is that this will help ensure that the trade effects of regulation are considered explicitly. Regulators often do not consider the international implications of what they do. To a large extent this is simply because they are not called to do so by their authorizing environment. They may be limited in their appreciation of the economic effect and costs associated with implementation of their regime on firms and consumers in other jurisdictions. A necessary condition for regulators to consider the (cross-border) economic implications of their work is that they have incentives to do so, which raises issues related not just to their legal mandates but also the design of institutional mechanisms that facilitate learning and a better understanding of the overall impact of regulatory norms on trade and investment incentives. In terms of the typology of Table 1, a trade agreement may help in identifying which areas of regulation fall into boxes *C* and *D*.

Trade agreements may also be used as an instrument to generate the political oversight needed for implementation of cooperation. An important feature of trade agreements is that there are a large number of interests represented. This can not only ensure that areas that are priorities from a trade perspective are identified and put on the table, but also help overcome political economy constraints that preclude movement in a direction that governments perceive will enhance aggregate welfare. Regulators may have a vested interest in the status quo, or have been captured by a domestic industry. Focusing on such problems in a trade agreement context may help mobilize the political support needed to push through reforms. Referring back to Table 1, dealing with regulatory matters in a trade agreement may help move forward over time on issues that are in boxes *C* and *D*.

Addressing regulatory issues in a trade agreement also may benefit regulators if it helps to mobilize additional resources to support cooperation. This can both support greater attention being given to cooperation – as that will entail

a resource cost for the agencies involved – and, indirectly but potentially importantly, allow for a reallocation of scarce resources to other areas. That is, if cooperation is successful – for example, it results in acceptance that two regimes are equivalent – regulators can allocate less to surveillance of that particular issue area and focus more on other concerns. The benefits of regulatory cooperation accrue not just to companies and consumers in the form of lower compliance costs; if it results in reductions in operating costs for a regulatory agency, this will release resources for other purposes.

In practice, capacity constraints may impede even the shallowest forms of cooperation. Basic principles such as transparency, notification and allowing for comment from stakeholders on proposed new regulation may not be implemented because of resource constraints. There is a significant technical assistance and capacity-building agenda associated with improving regulatory systems and governance in developing nations. Including regulatory cooperation in a trade agreement can provide a focal point to mobilize aid for trade. The 2013 WTO Trade Facilitation Agreement (TFA) illustrates one approach through which additional resources can be mobilized to improve national regulation through international cooperation.⁸

The WTO Status Quo

The WTO is supposed to be the global apex institution dealing with the cross-border spillovers created by national trade-related policies. The primary focus is on trade policies, but it also includes disciplines on domestic regulation, motivated by a concern that these not be used to discriminate against foreign products. The national treatment rule is a general obligation for goods, whereas it is a specific one in the case of services – applying only to scheduled services/modes of supply. The WTO does not engage on the substance of regulatory measures – all it requires is that foreign products are treated the same as domestic ones. The WTO does embody some disciplines that require minimum levels of regulation – for example, the TRIPS agreement requires Members to implement minimum standards of protection for intellectual property – but the substance of the rights and requirements/criteria involved are left to other international bodies to determine.

Concerns that product-specific regulatory norms may be used for protectionist purposes motivated the negotiation of specific disciplines going beyond the

8 This was done by linking implementation of the TFA to technical and financial assistance from high-income countries, under the umbrella of the 'aid for trade' initiative; see Hoekman (2016).

national treatment rule: the Agreement on Technical Barriers to Trade (TBT) and the Agreement on Sanitary and Phytosanitary (SPS) Measures. The TBT agreement addresses technical requirements (mandatory regulatory norms) imposed by governments for goods; the SPS agreement deals with mandatory health and safety-related norms for agricultural products (foodstuffs, plant and animal health). The TBT agreement goes further than national treatment by requiring that Members base their product regulation on available international standards (whenever appropriate) and adopt the least trade-restrictive measure that is necessary to achieve their regulatory objective.⁹ The SPS agreement makes explicit reference to an indicative list of international bodies that promulgate SPS norms, such as the Codex Alimentarius Commission. If a national product-specific regulatory measure is based on an international standard, it is presumed to satisfy the least trade-restrictive test in that the norms are considered to be necessary and non-discriminatory in effect and in intent.¹⁰ Whether this is in fact the case is another matter, as in practice the process of international standardization may not devote much attention to trade effects. The presumption is that because many countries will be involved in the process of defining international standards, whatever is agreed is regarded as being non-discriminatory in intent, no matter the actual effect on trade. As argued below, this is one weakness of the current approach in the WTO towards international standardization.

Many of the standards that confront firms operating internationally address management processes and production methods. Systems such as ISO 9000, ISO 14000 and ISO 26000 are used by companies as a signal of quality, a demonstration of a commitment to social responsibility or as requirements that must be met by suppliers in a trade relationship with buyers or by companies that are part of international value chains and production networks. Standards of this type are not covered by the WTO as they are not mandatory.

Conformity assessment procedures for technical product regulations are also subject to WTO disciplines, including the non-discrimination rule. Relevant guides or recommendations issued by international standardizing bodies are to be used if they exist, except if inappropriate for national security reasons or deemed inadequate to safeguard health and safety. In principle, WTO Members are free to join and use international systems for conformity

9 What follows focuses on the TBT agreement. Similar considerations apply to the SPS agreement.

10 One reason why there are two product standards agreements is that the health and safety concerns that arise in the production, trade and consumption of food, plant life and animals are considered to be particularly important. In effect, many SPS norms can be characterized as measures that are aimed at catastrophe avoidance – the spread of diseases, the probability of serious illness, and so on. Such considerations also arise with technical barriers to trade as these may have similar motivations – e.g. a ban on the use of lead paint, radioactive residues, etc. – but they often address other types of issues as well (e.g. radio frequency interference, interoperability, and so forth).

assessment. The results of conformity assessment procedures undertaken in exporting countries must be accepted if consultations determine these are equivalent to domestic ones. WTO members are encouraged to negotiate MRAs for conformity assessment procedures, and not to discriminate between foreign certification bodies in their access to such agreements.

The SPS and TBT Committees have been characterized as technical expert-driven catalysts for multilateral dialogue, providing a forum for the development of guidance (soft law) and peer review of trade measures (Wijkström, 2015). An important dimension of what the WTO does in the area of product regulation is compiling information on new measures. WTO Members are required to notify the WTO of new measures that are not based on international standards. Over 45,000 measures have been notified since 1995. The TBT and SPS committees have developed procedures that can be used by governments to raise concerns they have regarding proposed or applicable product standards of another WTO Member. This has come to be known as the “specific trade concerns” (STC) procedure (Horn et al., 2013). Between 1995 and 2015, over 800 STCs pertaining to SPS or TBT measures were raised in the relevant committee, implying that fewer than 2% of notified measures raised concerns. This process is widely regarded as being a useful mechanism to address concerns raised – about 40% of STCs in the area of SPS have reportedly been resolved (WTO, 2015). Over time the STC mechanism has evolved – for example, in 2014 WTO Members agreed to a procedure through which they can seek the services of the Chair of the SPS Committee or another facilitator to help find a solution to their concerns.¹¹

Much prevailing regulation deals with services. The WTO has fewer disciplines for regulations affecting services than for goods (product regulation). Article VI.4 of GATS calls on the Council for Trade in Services to develop any necessary disciplines to ensure that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services,¹² and Members may not apply regulatory requirements so as to nullify or impair specific commitments made for sectors/modes (Article VI.5(a)). The GATS therefore embodies a weak “least trade-restrictive” norm, but there is no obligation to use international standards – WTO Members may use whatever standards they wish.

11 See https://www.wto.org/english/news_c/news14_c/sps_10sep14_c.htm.

12 A Working Party on Domestic Regulation was mandated to develop disciplines called for by Article VI.4 to ensure that licensing and qualification requirements and related standards are not unnecessary barriers to trade in services. A precursor to this working party, the Working Party on Professional Services, agreed in 1998 on a set of principles to ensure transparency of regulations pertaining to licensing of accountants and accountancy services.

GATS Article VII (Recognition) promotes the establishment of procedures for (mutual) recognition of licenses, educational diplomas and experience granted by a particular Member. It permits a Member to recognize the standards of one or more Members, but does not require, or even encourage, Members to recognize equivalent foreign regulations. Article VII:2 requires a Member who enters into a mutual recognition agreement (MRA) to afford adequate opportunity to other interested Members to negotiate their accession to such an agreement or to negotiate comparable ones. Article VII:3 stipulates that a Member must not grant recognition in a manner which would constitute a means of discrimination between countries. Members must inform the Council for Trade in Services about existing MRAs and of the opening of negotiations on any future ones. Most such notifications pertain to the recognition of educational degrees and professional qualifications obtained abroad.

The WTO does little at present to support regulatory cooperation on a multilateral basis; the focus has been on national policies. This has included deliberations (in the context of the TBT Committee) on what constitutes good regulatory practice and options that governments can use to streamline the way regulations are prepared, adopted and applied through the "regulatory lifecycle." An example is the deliberation that commenced in 2012 over voluntary guidelines that would reduce the possibility of product regulation having the effect of unnecessarily restricting trade. However, to date no agreement on a set of good practice guidelines has proved possible because of concerns that the Appellate Body might invoke such norms in a dispute, notwithstanding the fact that it would be explicit that they would be non-binding.¹³

There is much more to be said about the state of play in the WTO on regulatory matters. The foregoing brief snapshot makes clear that the WTO is more involved than might be expected, but that many areas of regulation are not subject to multilateral rules of the game – especially service sector regulation. The role of the WTO as a transparency mechanism is much better developed for product regulation than it is for other types of regulation that have an impact on trade. The various committees and working parties dealing with different dimensions of economic regulation have acted as foci for deliberation and information exchange. More can certainly be done if governments are willing to do so, but the experience over the last decade or so with attempts to refine and expand disciplines on domestic regulation of services and to agree to voluntary principles of good practice for regulation illustrates that

13 The Appellate Body has held that a 2000 decision by the TBT Committee on a set of (voluntary) principles for the development of international standards, guides and recommendations was a "subsequent agreement" under the Vienna Convention on the Law of Treaties; see Wijkström and McDaniels (2013).

achieving a consensus in these areas may not be possible. As far as regulatory cooperation is concerned, one shortfall in the approach taken in the WTO has been the absence of a concerted effort by WTO Members to encourage international standardizing bodies to consider the trade effects of the norms that they develop (Hoekman and Mavroidis, 2016a).

Regulatory Cooperation in (Mega-)PTAs

How do PTAs compare to the WTO? There is of course huge heterogeneity, but most PTAs do not do more than the WTO, while the one outlier, the EU, goes far beyond the WTO in the area of regulatory cooperation. The only other PTA that includes substantial regulatory cooperation in specific areas is the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) (Steger, 2012). Recently concluded mega-PTAs such as TPP do not go very far beyond the WTO – the value added primarily involves language aiming at greater coherence of regulatory regimes of the signatories (Bollyky, 2012), along with provisions calling for consultations (i.e. the shallow forms of cooperation discussed in the first section).

The EU has used a mix of approaches to remove the market-segmenting effects of national product regulation, including harmonization and mutual recognition. The latter became a key driver following decisions of the European Court of Justice, which ruled that, in the absence of overriding concerns that permit an exception, EU members must accept products into their markets that have been legally introduced into the commerce of another member state. However, the EU experience illustrates that mutual recognition requires some minimum level of harmonization of norms (common “essential requirements”).¹⁴

Recent PTAs involving the EU complement mutual recognition with efforts to move towards mutual “equivalence.” This involves agreement that the regulatory objectives of the parties involved are equivalent *and* acceptance that implementation and enforcement mechanisms in the parties’ jurisdictions are effective. Under a “standard” mutual recognition approach, *A* satisfies itself that *B* achieves its norms through the similar kind of testing, inspections, sampling and so on that *A* undertakes. Under regulatory equivalence, *A* simply accepts *B*’s processes and systems: each government agrees that the regulatory regime of the other party is equivalent to its own in terms of both objectives and the effectiveness of the institutional apparatus through which these objectives are

¹⁴ See Pelkmans (2012) for an in-depth discussion.

pursued.¹⁵ A necessary condition for an equivalence approach is trust: there must be a prior process of "mutual assessment" (Messerlin, 2014) or evaluation of the regulatory goals and implementation regime in the relevant jurisdictions that results in a judgment that these are "equivalent."

CETA — at the time of writing the most recent of the new type of trade integration agreements and likely to be a model for what the EU and the United States might agree to in TTIP — includes some language on equivalence (Hoekman, 2015a). CETA calls for the establishment of a regulatory cooperation forum to facilitate and promote the realization of the objectives laid out in the regulatory cooperation chapter. It also provides that the parties *may* consult with stakeholders, including the research community, NGOs and business and consumer organizations "on matters relating to the implementation of" the regulatory cooperation chapter (DFATD, 2014, Chapter 26, "Regulatory Cooperation," Article X.8). Article 2 of the CETA chapter on regulatory cooperation commits both parties to developing their regulatory cooperation to prevent and eliminate unnecessary barriers to trade and investment; enhancing the climate for competitiveness and innovation, including through pursuing regulatory compatibility, recognition of equivalence and convergence; and adopting transparent, efficient and effective regulatory processes that better support public policy objectives and fulfil the mandates of regulatory bodies. Article 3 mentions such objectives of regulatory cooperation as building trust; deepening mutual understanding of regulatory governance and obtaining from each other the benefit of expertise and perspective to improve regulatory proposals; promoting the transparency, predictability and efficacy of regulations; identifying alternative instruments; recognizing the associated effects of regulations; and improving regulatory implementation and compliance.

Another objective of CETA is to facilitate bilateral trade and investment by reducing unnecessary differences in regulation and identifying new ways of cooperating in specific sectors. In a similar vein, the agreement mentions the complementary goal of enhancing the competitiveness of industry by looking for ways to reduce administrative costs and duplicative regulatory requirements, and "pursuing compatible regulatory approaches including, if possible and appropriate, through: a) the application of regulatory approaches which are technology-neutral, and b) the *recognition of equivalence* or the promotion of

15 A key difference, therefore, is that regulatory equivalence requires a willingness to step back from a focus on technical product considerations and to assess systems as a whole. Thus, whereas mutual recognition means assessing country *B*'s meat inspection system on the basis of a sampling regime and the results of testing in country *A* of a sample of products originating in *B*, an approach based on regulatory equivalence would justify trust in a partner country's products on the basis of systemic arguments.

convergence” (DFATD, 2014, Chapter 26, “Regulatory Cooperation,” Article X.3(d)(iii); emphasis added).

Language on – and examples of – regulatory equivalence embodied in CETA include the chapter on SPS measures, which requires each signatory to accept the measures of the exporting party as equivalent to its own if the exporting party “objectively demonstrates that its measure achieves the importing Party’s appropriate level of protection” (DFATD, 2014, Chapter 7, “Sanitary and Phytosanitary Measures,” Article 7.1). Principles and guidelines for the determination of equivalence are set out in Annex IV to the SPS chapter, while Annex V lists areas where the parties have agreed there is equivalence. One function of the CETA Joint Management Committee for SPS Measures is to prepare and maintain a document detailing the state of discussions between the parties on their work on recognizing the equivalence of specific SPS measures. A Protocol on the Mutual Recognition of the Compliance and Enforcement Programme regarding Good Manufacturing Practices for Pharmaceutical Products provides for the determination of the equivalence of regulatory authorities that certify compliance with these practices. Annex II (on Medicinal Products or Drugs) of the protocol lists products for which the parties have agreed that their requirements and compliance programs are equivalent.¹⁶⁸

The CETA chapter on regulatory cooperation creates an entry point with respect to greater use of regulatory equivalence among like-minded countries, but puts little emphasis on the use of equivalence as a way to reduce regulatory differences and costs. Indeed, the chapter, while laying out a rather long illustrative list of possible cooperation activities, does not mention “equivalence” in Articles X.4, X.5 or X.7. Article X.4.18 does call for identifying approaches to reduce the adverse effects of existing regulatory differences on trade, including “when appropriate, through greater convergence, mutual recognition, minimising the use of trade distorting regulatory instruments, and use of international standards,” but the activities listed in these articles focus on transparency and data and information sharing.

Even though CETA goes further than the TPP on regulatory cooperation, it arguably does little to reflect the changes in the way international trade is now organized. More rapid progress in attenuating the trade-cost effects of different regulatory policies might be realized by creating processes and institutional

16 See <http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/ceta-accg/text-texte/28.aspx?lang=eng>. Some mention of regulatory equivalence also occurs in the chapter on financial services, a sector where the approach has been pursued internationally for some time; see, for example, Verdier (2011). The chapter permits Canadian institutions to provide portfolio management services to EU professional clients on a cross-border basis (that is, without having to establish in the EU) once the European Commission has adopted the equivalence decision related to portfolio management (EU prudential requirements will still apply).

mechanisms that take a broader value chain perspective (Hoekman, 2015 a). Concrete initiatives to reduce the costs of redundant regulatory requirements and processes must be policy specific — that is, they must involve the type of cooperation called for in CETA and that is already being pursued in the Canada-US Regulatory Cooperation Council. But missing from current approaches are cross-cutting, supply chain-informed deliberative mechanisms that focus on a broad range of policies that affect trade costs and that provide a framework for regulatory cooperation to improve the competitiveness and efficiency of industry – two goals that Canada and the European Union set for themselves in CETA (DFATD, 2014, Chapter 26, Article X.3d) (Hoekman, 2015a).

Reducing the Negative Trade Effects of Behind-the-Border Regulation

Regulatory measures generally fulfil a specific social or economic purpose, even if the effect is to restrict trade. Addressing possible trade-reducing (distorting) effects of regulation requires first an understanding of the effects of prevailing (proposed) policies. Many desirable reforms will not require actions by other governments (trading partners), but regulatory cooperation may help in identifying what such reforms should seek to do and increase the effectiveness and efficiency of regulation. Trade agreements may help by mobilizing and sustaining political attention and thereby overcome resistance by vested interests and incentivize regulatory bodies to give more of a priority to actions that reduce the negative trade impacts of regulation.

As already discussed, trade agreements are geared towards the negotiation of enforceable policy commitments. Binding disciplines reduce uncertainty for traders who know that the dispute settlement mechanism can be used to ensure that governments live up to what they sign on to. A precondition for agreement on binding international rules is a shared recognition that the negative spillovers associated with a policy (or set of policies) are significant and that a proposed set of (enforceable) disciplines will result in greater efficiency (lower costs). Such an understanding exists when it comes to tariffs and related border barriers, but much less so when it comes to domestic regulatory policies.

It is important to recognize that trade agreements may not have a “comparative advantage” in supporting effective cooperation between regulators, even if trade negotiators have the best of intentions. The public backlash against TTIP in the European Union has largely been driven by concerns that greater integration of the transatlantic marketplace may result in an erosion

of regulatory regimes in areas that are of great importance to significant segments of the EU population – such as the use of genetically modified organisms (GMOs) and specific food standards. Regulatory cooperation is likely to be more easily pursued if it involves a bottom-up process that is driven by regulatory agencies, as opposed to being imposed top down as an element of a trade agreement. A useful prescription in this regard is to apply the principle “first, do no harm” and to concentrate on incorporating measures in trade agreements that can be defended as improving the ability of regulators to do their job better. That is, the aim should be empowerment of regulatory bodies rather than imposing restrictions on them (or being seen to be doing so even if that is not the intention).

From a trade perspective, international cooperation on regulation arguably should center on improving the transparency of applied policies; supporting analysis of the trade (and investment) effects of specific types of regulation; giving regulators a mandate that encourages (permits) them to design regulations that do not unnecessarily restrict trade; and doing more to ensure that the process of international standards-setting and norms-setting occurs with greater attention given to the potential trade impacts. Measures taken by the trade community to achieve these objectives should not affect the ability of regulators to do their job.

Transparency. This is a core feature and function of the WTO. The regular work of the TBT and SPS Committees, including notifications and the opportunity to raise specific concerns, can be emulated in other areas of regulation. Here an obvious area to prioritize are services and regulations that impact on the ability of firms to supply and consumers to buy products that are connected to/use “the cloud” (data localization requirements, etc.) The relevant GATS bodies have not ignored issues of domestic regulation (see above), but much more could be done to map out the policies that WTO Members are pursuing. The recent joint venture with the World Bank to maintain and update a database on services trade policies – the Services Trade Restrictiveness Indicators (STRI) – is a good first step, but this is mostly limited to policies that are discriminatory and do not cover domestic regulation. It is unlikely that this can rely only on notifications – it will require a pro-active effort by the WTO Secretariat, working with other international organizations.

Much greater transparency is also needed as regards PTAs. Insofar as PTAs give rise to innovative approaches to attenuate the market-segmenting effects of differences in regulatory policies, they can help all countries identify approaches that can usefully be emulated. All WTO Members have a strong interest in understanding what PTAs end up doing and achieving. Documenting and analyzing the approaches that are implemented by PTAs to reduce regulatory

barriers would not only improve transparency per se, but can also inform a process of learning about what works and what does not and perhaps identify specific features of cooperation in PTAs that might be multilateralized. There have been some moves in this direction on an ad hoc basis; for example, the GATS Working Party on Domestic Regulation conducted a dedicated discussion on domestic regulation in regional trade agreements in 2014.

Learning: analysis and deliberation. As noted previously, there is often relatively little, if any, effort by national regulators and international standards-setting bodies to consider the trade impacts of regulatory requirements and alternative approaches that might have less negative effects while not impacting on the probability that regulatory objectives will be realized. There is also arguably more that can be done to understand how the universe of regulatory measures maps into the categories defined in Table 1 and the potential efficacy of the different types of international regulatory cooperation summarized in Table 2. There would appear to be significant scope to use the WTO bodies that already have a mandate to discuss regulatory policies (TBT, SPS, services) to commission analysis of trade effects and to engage more regularly with the business community in discussions aimed at identifying where greater effort to pursue regulatory cooperation – which need not occur through the WTO – could have a significant impact on trade costs. Currently there is too little scope for engagement with the business community within WTO bodies. There is more attention for this in recent (mega-)PTAs, but even there the extent to which business is part of regulatory deliberation is too limited (Hoekman, 2015b).

Give regulators a mandate to consider trade effects. A simple yet powerful change that WTO and PTA members could seek to achieve is to agree that the regulatory process should include an assessment of trade effects – perhaps as part of broader regulatory impact assessments that are generally considered to be an element of good practice. This is already “on the table” in the deliberations on a voluntary code of good practice in the TBT Committee. If no consensus can be achieved there – and given that in other areas of regulation, this agenda is not “on the table” – one way proponents could consider moving forward on this is through a plurilateral agreement (see below). In order to increase the prospects that such assessments are made, regulatory agencies should be provided with the necessary (financial) resources so that such an effort would not crowd out (or be seen to crowd out) other activities. Incorporation of “trade effects assessment” language in trade agreements is in itself an instrument through which regulatory agencies can lay claim on additional resources from the government that are needed to fulfil the commitment.

Engaging with international standards-setting bodies. More generally, there is a clear case for more regular interaction with international regulatory bodies. Again this is something that already occurs on an ad hoc basis. For example, representatives of the Basel Committee on Banking Supervision, the Financial Stability Board, the International Association of Insurance Supervisors and the International Organizations of Securities Commissions have been invited periodically by the GATS Committee on Trade and Financial Services to present recent developments in the area of international regulatory norms and initiatives in the financial sector and discuss possible implications for trade in financial services. However, this is largely limited to one-way information transmission. What would arguably make a difference is a greater effort by WTO Members – who are all represented in international standards-setting bodies – to include a focus on the trade effects of new international norms and standards.

Club Formation Under WTO Auspices?

Going beyond greater transparency, analysis and interacting with international standards-setting bodies, at the level of the WTO consideration should be given to facilitating small-group cooperation on regulatory policies under the umbrella of the WTO. There are two alternative mechanisms for Members to form clubs on an issue-specific agenda of common interest: conclusion of a Plurilateral Agreement (PA) under Article II.3 WTO, and so-called critical mass agreements (CMAs). CMAs are agreements in which negotiated disciplines apply to only a subset of countries, but benefits are extended on a most-favored nation (MFN) basis. Examples include initiatives such as the Information Technology Agreement (ITA) and other so-called “zero-for-zero” agreements in which a group of countries agree to eliminate tariffs for a specific set of products. There are also CMAs for services, for example, on basic telecommunications and on financial services under the General Agreement on Trade in Services. PAs differ from CMAs in that they may be applied on a discriminatory basis – that is, benefits need not be extended to non-signatories. There are currently two PAs incorporated into the WTO: the Agreement on Civil Aircraft and the Agreement on Government Procurement.

PAs and CMAs differ from PTAs in important respects. WTO rules require that PTAs cover substantially all trade in goods and/or have substantial sectoral coverage of services. In contrast, CMAs and PAs can be issue specific. PTAs tend to be closed clubs – most PTAs do not include an accession clause. Those PTAs that do allow for accession often restrict it to countries in a specific geographic region. This helps explain the proliferation of PTAs – a new agreement often tends to be negotiated between members of any given

PTA and a non-member, because it is not possible for a non-member to join an existing regional trade agreement. CMAs and PAs, in contrast, are open in the sense that in principle any WTO Member can join if it wants to and is able to satisfy whatever disciplines are embodied in the agreement.

There are good reasons for attempting to do more via CMAs and PAs (Lawrence, 2006). As discussed by Hoekman and Mavroidis (2015), CMAs and PAs cannot reduce the welfare of any country, including those that decide not to join, because CMAs apply on an MFN basis and PAs must be approved by the WTO Membership as a whole. PTAs are reviewed by the WTO, but there is no sanctioning of their content; the process is limited to the supply of information. CMAs and PAs are more transparent as they involve formal scheduling of commitments by signatories and, in the case of PAs, regular reporting on activities to the WTO Membership as a whole. They imply less dispersion in rules and approaches – and thus transactions costs and trade diversion – than PTAs. Indeed, they offer a way to multilateralize elements of what may be covered in PTAs. Multiple PTAs dealing with the same subject matter often do so in ways that imply that the rules of the game for firms differ depending on the PTA that applies for a given trade flow.

There is no formal constraint on the ability of a club of WTO Members to pursue CMAs that involve deepening of disciplines on policies that are already subject to WTO rules, as long as they are willing to apply these on an MFN basis (Hoekman and Mavroidis, 2016b). There is, however, a major constraint that impedes the feasibility of pursuing new PAs under WTO auspices: incorporation of a PA into the WTO requires unanimity “exclusively by consensus.”¹⁷ This is a major disincentive for countries to pursue this type of cooperation. Hoekman and Mavroidis (2015; 2016b) suggest that WTO Members set up a task force on a code of conduct for new plurilateral agreements that apply to and benefit only signatories and consider replicating a GATS provision permitting WTO Members to make additional commitments in the GATT, so as to facilitate the negotiation of new CMAs that deal with regulatory policies that affect trade in goods. Such codes would establish the basic principles that new club-based agreements should satisfy to be consistent with the principles of the multilateral trading system, as well as substantive criteria for the rejection of proposals to pursue such cooperation under WTO auspices.

17 See Article X.9 of the Agreement Establishing the WTO.

Concluding Remarks

The gradual reduction of tariffs as part of a more general process to open economies to international trade and investment flows, in conjunction with technological changes that are permitting the digitization of products and increasing the share of services in global production, have greatly increased the impacts of differences in domestic regulation of products and production processes. The future international trade agenda is likely to become largely a regulatory agenda, the challenge being to devise mechanisms to reduce the costs of differences in regulatory regimes while at the same time ensuring that this does not erode the likelihood of attaining the regulatory objectives that have been established by the polities of countries that engage in trade.

In principle, regulatory cooperation may bolster the ability of regulators to attain regulatory objectives if it is designed with that objective in mind. Indeed, in practice this is likely to be a necessary condition for cooperation to be feasible. A key question for governments is whether trade agreements are a useful instrument to guide regulatory cooperation and if so, how regulatory matters should be addressed in trade agreements. In some areas, such as technical regulation of products, there are now well-established and reasonably effective mechanisms in the WTO through which the potential negative externalities of differences in standards can be identified, discussed and attenuated. In many other areas of regulation – such as prudential regulation of services, “private standards” systems that apply to international production processes, or standards of protection of worker rights and the environment – WTO members have yet to put in place such mechanisms. The same is largely true of PTAs – while there is much discussion of new vintage PTAs as instruments for regulatory convergence, to date steps to address such matters have been limited.

Neither PTAs such as the TPP nor the WTO engage on the substance of regulatory norms – the focus is on the trade-impeding effects of differences in regulatory standards. Cooperation on substantive norms – international standardization – is left to specialized bodies in which regulators interact. These bodies tend to be technical and focused on defining the means to achieve specific regulatory objectives (health, safety, etc.). They generally do not consider the potential impacts on trade. One role that the WTO could play looking forward is doing more to ensure that international regulatory efforts consider trade effects when developing new international norms. More generally, the WTO (and trade agreements more generally) could be used as a focal point for encouraging regulators to interact with each other and to consider cooperation that enhances their joint ability to attain regulatory objectives at lower cost. The suggestions made above regarding the form

this could take illustrate the potential positive role that trade agreements can play. Whether they will be pursued depends importantly on the stance taken by international business. A necessary condition is strong advocacy by international business for greater engagement by governments in the WTO to address negative regulatory spillovers.

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CHAPTER 6

The WTO's Next Work Program – as if the Crisis Really Mattered

Simon J. Evenett and Johannes Fritz¹

University of St. Gallen

Introduction

Typing the words “WTO stress test protectionism” into Google reveals that many in the official community claim that the WTO succeeded in preventing the widespread resort to protectionism since the onset of the global economic crisis. If, indeed, the multilateral trading system has done so well, then put the champagne on ice and the future work program of the WTO can address other matters.

Of course, there are many reasons why certain officials may find it convenient to downplay the significance of crisis-era distortions to global commerce. Some may have been persuaded by the findings of the limited WTO monitoring exercise on protectionism. This is not the place to detail the flaws in such official monitoring (see the relevant chapters in the 16th and 18th reports of the Global Trade Alert). Others may suspect that beggar-thy-neighbor activity is far greater than officially admitted but fear that public recognition of this fact could trigger a wave of retaliation. What such fears say about the robustness of the current WTO system is worth pondering.

Some business associations – such as the International Chamber of Commerce and the B20 – have not been afraid to speak about against crisis-

¹ The authors of this chapter are associated with the Global Trade Alert (GTA) initiative, the independent trade policy monitoring initiative that is run under the auspices of the Centre for Economic Policy Research (CEPR), of which Evenett is the Co-Director of its International Trade and Regional Economics Programme. The reports of the GTA, which provide far more data than are presented here, can be accessed at <http://www.globaltradealert.org/analysis>. Comments received at a session of the Evian Group in December 2015 were much appreciated.

era protectionism and, if their reports are anything to go by, are less sanguine than official assessments. In recent years particular attention has been given to far-reaching export restrictions (recall the Chinese Rare Earth case), to state-owned and state-controlled firms, and to the spread of “localization” measures, the latter not just relating to trade in goods but also to cross-border data flows. That many business associations have supported the negotiation of disciplines in mega-trade deals that go beyond those found in WTO rules probably implies some dissatisfaction with the latter.

For the most part, when it comes to crisis-era protectionism, academics have been sorely behind the curve. In an age when data are downloaded rather than collected, most academic studies have confined themselves to datasets that were available before the crisis. In effect, this has meant that many studies examine only the impact of tariff increases and trade defense and safeguard measures. Other distortions to 21st century commerce tend not to be considered. Given that trade defense measures are the minnows of international trade policy, it is not terribly surprising that these measures have been shown to have cut trade by little during the crisis era.² Much theoretical analysis of the WTO makes little reference to actual policy choice – indeed, it is almost as if the crisis never happened. If academic writing is anything to go by, there is little to learn from the crisis era for the next work program of the WTO.

If, indeed, policymakers conclude that the crisis era has few implications for the future development of the multilateral trading system, then this will represent a departure from the pattern observed after previous global economic contractions. The formation of the GATT was said to have been influenced by the beggar-thy-neighbor activity witnessed during the Great Depression. Similarly, the pervasive use of voluntary export restraints during the sharp global downturn of the early 1980s led to their banning as part of the Uruguay Round agreements. In both instances there were enough analysts and policymakers that recognized the deficiencies in existing multilateral trading arrangements. Will this time be different?

In this chapter we summarize the evidence on the resort to discrimination against foreign commercial interests that has been collected by the Global Trade Alert initiative, with which we are associated. Furthermore, in preparing this chapter we have computed the share of the G20’s exports that face different types of discriminatory policies. We discuss the evolution of these trade coverage ratios since 2009 and then reveal which policies affect relatively more of global commerce.

2 In this chapter we will confirm that the trade covered by trade defence and safeguard measures is a tiny percentage of world trade. No disagreement on this matter.

All in all, the data presented here point to a world trading system that is not holding the line against protectionism, especially against the distortions to global commerce that are not well disciplined by WTO rules. The best that can be said about existing WTO rules is that they have channeled protectionist pressure into policy instruments subject to weaker or no multilateral disciplines.

It is said that, in two speeches in 1959 and 1960, President Kennedy noted that in Chinese the word “crisis” is represented by two symbols, one for danger and another for opportunity. Having spelt out the former, we conclude our chapter with the latter – describing how a future WTO work program could be influenced by what has been learnt about government policy choice since the onset of the global economic crisis in 2008.

We should be clear about what this chapter is not about. This chapter does not provide an explanation to account for the timing and form of crisis-era discrimination against foreign commercial interests. Readers interested in this matter are referred to Evenett (2015). Nor does this chapter estimate the impact of crisis-era protectionism. For an analysis of the impact of such protectionism on the exports of the Least Developed Countries, see Evenett and Fritz (2015a). For more information on national resort to protectionism and liberalisation during the crisis era, readers are referred to the reports of the Global Trade Alert (GTA).

Monitoring Discrimination

Several considerations need to be borne in mind when monitoring the resort to discrimination against foreign commercial interests by governments during a systemic economic crisis. First, governments have many policy instruments available to them, including those not subject to WTO rules. Second, the rationale for crisis-era policy initiatives may on paper have nothing to do with seeking commercial advantage yet, inadvertently or by design, these initiatives may discriminate against foreign commercial interests.

Third, governments can obscure, hide or delay the publication of the details of discriminatory measures, not least to avoid being labelled “protectionist.” Fourth, in the 21st century, there are many more forms of cross-border commerce than traditional trade in goods, widening the range of policies of relevance to any monitoring exercise. Fifth, the financial origins of the most recent global economic crisis raise the possibility that the allocation of finance becomes another tool for state discrimination against foreign commercial interests.

For of all of these reasons, when monitoring discrimination by governments it makes sense to focus on changes in the relative treatment of domestic versus foreign rivals, rather than confine information collection to a pre-specified set of policy instruments. History shows that the most prominent form of discrimination changes with each global economic crisis (tariff increases and competitive devaluations in the 1930s, and voluntary export restraints in the 1980s). So best to keep an open mind as to what form discrimination may take.

Another implication of the foregoing considerations is that information about the incidence and extent of discrimination against foreign commercial interests is available with a lag. Consequently, although the Global Trade Alert team looks for current instances of discrimination (and for that matter, liberalization), when information about government initiatives from earlier years becomes available then this is added to our database. At this writing, a total of 7,952 government measures that have been announced or implemented since November 2008 have been documented by the GTA team.³ In the past two years approximately 2,000 measures have been documented per year, substantially expanding the database. The GTA's coverage is global.⁴

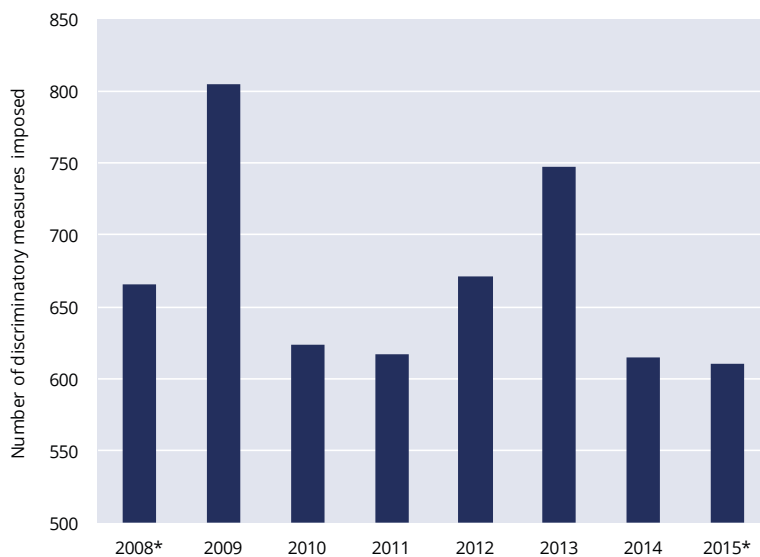
Figures 1 and 2 highlight the perils of ignoring publication lags. Figure 1 is based on the data available as of the end of November 2015. Consequently, the GTA team has had six years to document discrimination undertaken in 2009 and only 11 months to document policies undertaken during 2015. Without knowing this, one might erroneously conclude that resort to beggar-thy-neighbor activity has fallen after its 2013 surge. In fact, if our experience is anything to go by, the first published totals for a particular year are revised upward significantly over time.

In addition to tracking the annual totals, it is also helpful to report the total number of measures documented for each year at the same point in the reporting cycle. Figure 2 reports the total number of liberalizing and discriminatory measures implemented in a given year that were reported by 31 October of that year. This particular date was chosen as it refers to the information available before the end-of-year G20 summits.

3 In comparison the WTO's Trade Monitoring Database, which has at present 3,203 entries. That database can be accessed at <http://tmdb.wto.org/>.

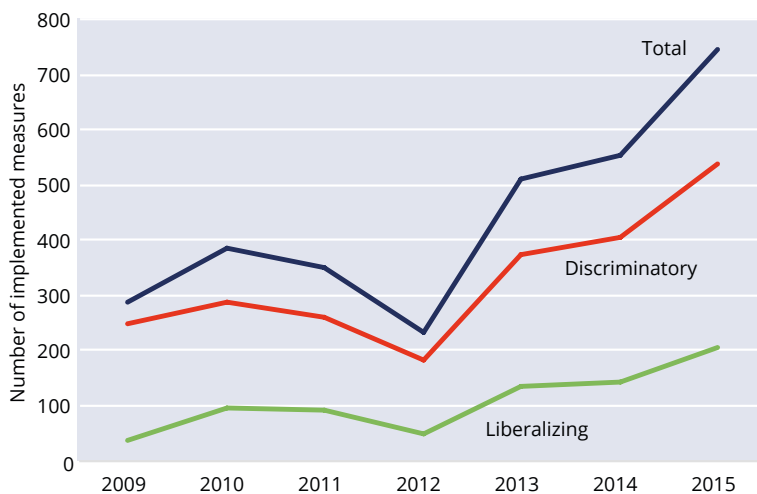
4 Further details on the approach used by the GTA team to identify, investigate and document crisis-era policy change can be found in Evenett and Fritz (2015a: 17-19).

Figure 1: Annual resort to discriminatory measures varies a lot



Note: *implies annualized total.

Figure 2: Correcting for publication lags matters – since 2012 there has been a surge in discriminatory and liberalizing measures implemented

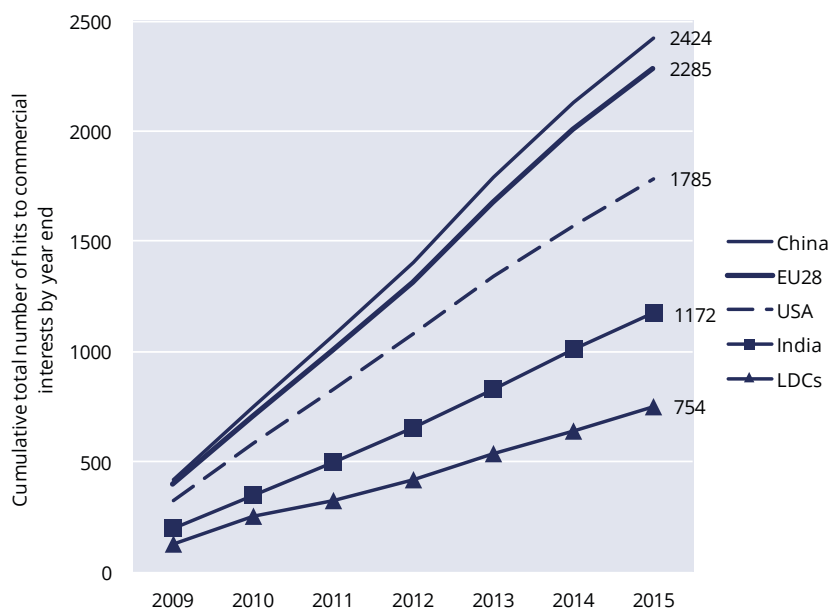


Source: Evenett and Fritz (2015b), Table 5.1.

The worrying finding in Figure 2 is that there has been a surge in the number of discriminatory measures implemented and documented from 2012 on. Some observers have wondered if that surge is the result of better monitoring on the part of the GTA team. Flattering as that may be, it is unlikely that the team has improved its productivity by over 150% since 2012. The implication being that the uptick in resort to discrimination since 2012 is real. While the number of liberalizing measures has grown too in recent years, the gap between the totals for discriminatory measures and liberalizing measures has grown. Any notion that beggar-thy-neighbor action has been tamed or was confined to earlier in the crisis should be set aside. Best not put that champagne on ice.

Using a conservative methodology, for each measure the GTA team identifies the trading partners affected, should the measure in question be implemented. It is then possible to track over time how frequently a jurisdiction's commercial interests have been harmed by the discriminatory measures implemented by its trading partners. These totals have been plotted in Figure 3 for China, the 28 members of the European Union, the United States, India, and the Least Developed Countries (LDCs). In each case the cumulative number of hits to their commercial interests keeps rising. Ministers may want to bear this in mind should they receive advice from officials and international organizations to discount crisis-era protectionism. These hits to commercial interests harm firms, employees, shareholders, owners of intellectual property and (where relevant) nationals working abroad.

Figure 3: No sign that harm to commercial interests is abating



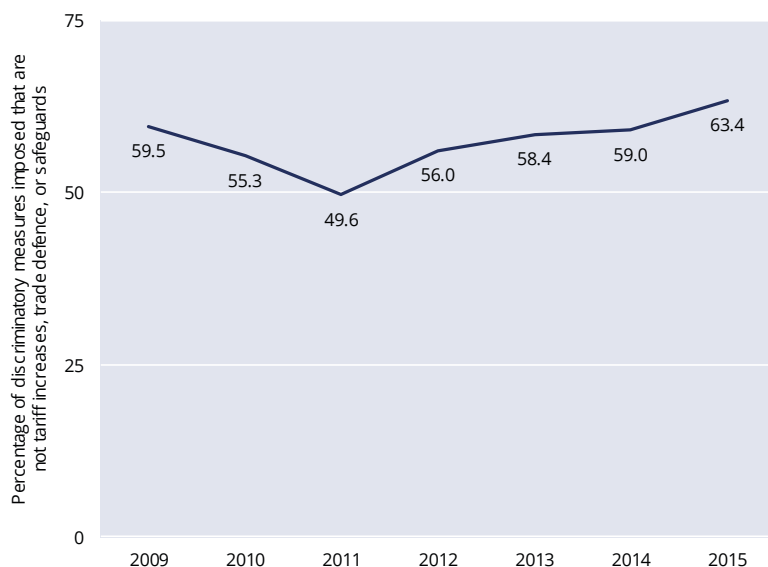
Having described the frequency of harm to commercial interests and, contrary to some official wisdom, having shown that discrimination against foreign commercial interests wasn't a contained spasm at the beginning of the crisis, we now turn to most popular forms of crisis-era protectionism.

The Most Prevalent Forms of Protectionism Used Since the Crisis Began

Before the recent global economic crisis, the stylized fact was that trade defense and safeguard measures were the principal form of discrimination used by governments (mainly in industrialized countries) to manage pressure for relief from global competition. Many developing countries still had plenty of leeway to raise tariffs without breaching WTO bindings.

As a result of the frequent use of these particular policy instruments, datasets on their use were collected and discussed. In the light of this, perhaps unsurprisingly, the initial instinct of many analysts when the crisis hit was to check if resort to these relatively transparent and more traditional policy instruments increased.

Figure 4: The crisis-era is dominated by murky protectionism – more so in recent years



It turns out, however, that much of the discrimination against foreign commercial interests undertaken by governments during the crisis era did not involve resort to trade defence or tariffs (see Table 1 for the top 10 most used discriminatory policy instruments and Figure 4 for the resort to other – murkier – forms of protectionism).

For sure, trade defence and safeguard measures are the most popular measure, but only just. Bailouts and other subsidies (unrelated to exporting) come a close second. Together, trade defence, safeguards and tariff increases represent less than half of the discriminatory measures employed in every year except 2011 (the crisis-era year with the least protectionism). Furthermore, the proportion of discrimination that is murky has grown since 2011 from one half to just under two-thirds, suggesting that governments are finding it more appealing to resort to discriminatory policies that tend to receive less attention from many analysts and international organizations.

Table 1: Top 10 most popular policy instruments employed against foreign commercial interests, listed in descending order

Discriminatory policy instrument	Number of discriminatory measures implemented since November 2008	Number of discriminatory measures still in force	Number implemented by...			Percentage of global total implemented by...		
			G7	BRICS	G20	G7	BRICS	G20
Trade defence & safeguards	1236	1033	329	377	1037	26.6	30.5	83.9
Bailouts and non-export subsidies	1196	892	346	340	756	28.9	28.4	63.2
Import tariff	782	633	25	310	544	3.2	39.6	69.6
Export taxes or restrictions	356	189	5	111	207	1.4	31.2	58.1
Localisation requirement	334	309	48	199	286	14.4	59.6	85.6
Trade finance	307	268	110	130	261	35.8	42.3	85.0
Investment limits	259	240	30	50	133	11.6	19.3	51.4
Export incentive or subsidy	242	169	18	129	173	7.4	53.3	71.5
Non-tariff barrier (n.e.s.)	207	152	17	43	132	8.2	20.8	63.8
Public procurement	187	174	68	63	158	36.4	33.7	84.5

The degree to which existing WTO obligations restrict government choices of the 10 policy instruments listed in Table 1 varies considerably. Many countries have applied tariffs close to their permitted bindings, while plenty of countries do not. Not every WTO Member is a member of the Agreement on Government Procurement and, even if they are, a national or subnational government may still retain considerable latitude to discriminate. Most limits on the use of export taxes and restrictions apply to recently acceded members. Provisions on investment policies and resort to localization measures can be found in the GATS and TRIMS agreements, respectively, but this does not seem to have stopped their widespread discriminatory use during the crisis era.

It would seem there is plenty of room for tightening up multilateral trade rules.

The Extent of G20 Exports Facing Crisis-era Protectionism

One reaction to the evidence in the previous two sections has been to dismiss it as merely referring to counts of measures. What about the scale of commerce potentially affected? As noted earlier, it is well known that the amounts of trade subject to trade defense investigations are typically small (although the 2012-2013 dispute between the European Union and China over solar panels was a notable, €20 billion exception). In the absence of any Smoot-Hawley tariff increases by any of the major trading powers, so the argument goes, surely the amount of trade affected is trivial?

In preparation of this chapter we have calculated the share of G20 exports that either face a discriminatory policy instrument in a foreign market, compete with a subsidized foreign rival in its home market, or compete with a foreign rival that has received state incentives to export to a third market. We only consider measures that have been implemented since November 2008.

In 2014 the G20 nations exported just under US\$11 trillion of goods, covering a substantial share of world trade. It is important to bear in mind that a 2% trade coverage ratio implies that \$218 billion of trade was potentially affected in 2014. Of course, the G20 is not the world, and trade in goods is only one form of cross-border commerce. Both limitations imply that the estimated scale of trade affected presented here will be underestimates.

We used product-level (technically, 4-digit HS codes) data on trade flows in preparing these calculations. For every discriminatory measure, we took account of the products implicated by that measure, the government responsible for that measure and the known trading partners for the product in question.

As trade flows tend to react to discriminatory measures, we used pre-crisis trade data (for 2005-2007) to weight each trade flow once the crisis began. We even took account of when measures were enacted in a year. For example, if a measure lasted for only two months during a year, we discounted the annual trade flow affected by 10/12ths to reflect the fact that for 10 months the measure was not in force.

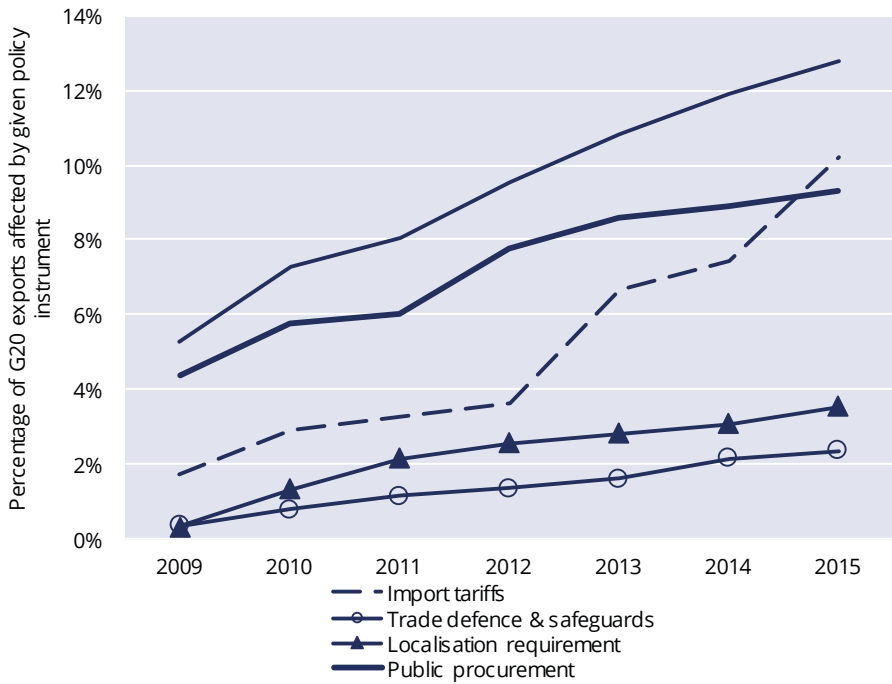
Figure 5 reports the percentage of G20 exports that faced import tariff increases, trade defense and safeguard actions, localization requirements and discriminatory public procurement measures during the years 2009 to 2015. In addition, the figure shows the percentage of G20 exports that had to compete in the home market of a foreign firm that had been bailed out.

The 2009 surge in protectionism resulted in over 5% of G20 exports competing against a bailed-out firm in its home market and over 4% of G20 exports involved shipments of products to foreign destinations where “buy national” public procurement provisions were in effect. Smaller percentages of G20 exports faced higher tariffs in 2009. These totals were to rise, however. By 2015 over 10% of G20 exports, an amount that exceeds \$1 trillion dollars in trade, compete with firms that have been bailed out during the crisis or have faced tariff increases.

In line with the WTO monitoring reports,⁵ we find the amount of trade covered by trade defense and safeguard measures to be small, relatively speaking. We estimate that localization requirements affected \$339 billion of trade in 2014, a sizeable amount for a measure that in the eyes of many analysts had been banned by the TRIMS agreement.

5 The “headline” trade coverage ratios that are found in the WTO’s monitoring reports cover only a narrow range of *import* restrictions. The WTO computes these ratios for the G20 countries, as we have. The contrast between our totals and the official numbers indicate how misleading the latter are.

Figure 5: The shares of G20 exports facing tariff increases and having to compete with bailed out firms in their home markets has risen markedly



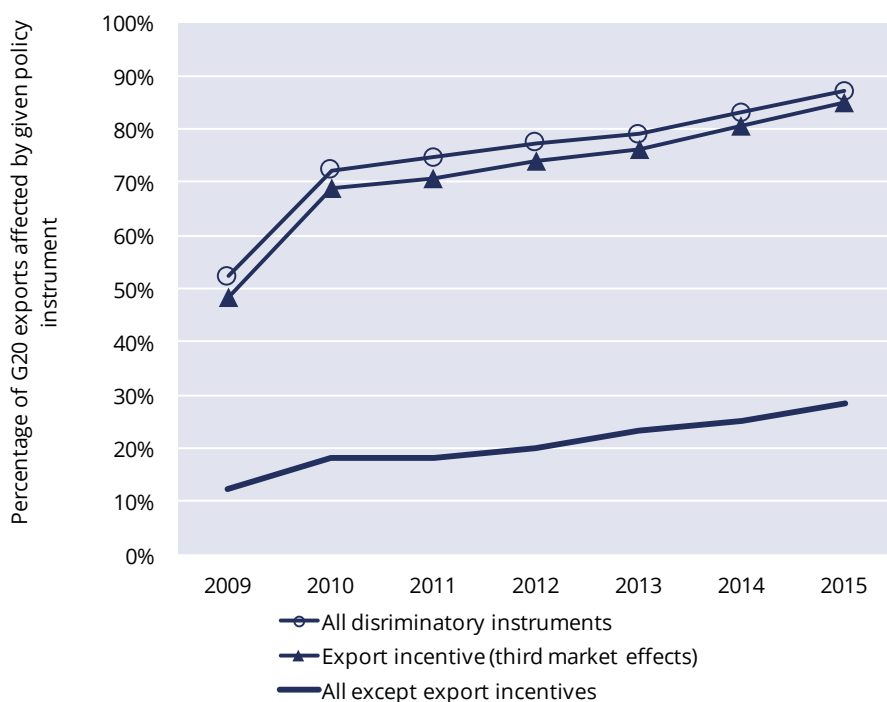
The amount of trade covered by the trade restrictions identified in Figure 5 and that competes in the home markets of bailed-out firms, however, pales in significance to that covered by state-provided export incentives. As Table 1 shows, the BRICS nations made frequent use of export incentives. Most of these incentives operate through national tax systems (some of the most far-reaching are related to value added taxes, but some are not). Such incentives can force rivals to lower prices, shrinking profit margins and diminishing the incentive to export in the first place. Moreover, uncertainty over the size of such export incentives can deter foreign rivals.

The full extent of G20 exports facing subsidized competitors is revealed in Figure 6. As nations have progressively expanded the range of products eligible for export incentives, the percentage of G20 exports competing against subsidized rivals in third markets has expanded to 84% in 2015, rising 36 percentage points in just six years.

In sum, in terms of scale, crisis-era discrimination against foreign commercial interests is more about export expansion than import contraction. Having said

that, even if export incentives are excluded, 28% of G20 exports currently face some type of trade distortion introduced since the crisis began. The long-held principle of non-discrimination has taken a battering during the crisis era and the latest data available suggest that there is no end in sight (Evenett and Fritz, 2015b).

Figure 6: The percentage of G20 exports that face competition from subsidised rivals in third markets has risen 30 points in just six years



As 2015 has progressed, more evidence has come to light of the importance of state competition in the provision of export incentives. The prolonged haggling in the US Congress concerning the reauthorization of the US Export-Import Bank is well known. It should not be forgotten too that France and the United Kingdom took advantage of this situation to lure production and jobs by US multinational General Electric. The CEO of General Electric, Mr. Jeff Immelt, went on record with the following statement:⁶

6 See <http://www.reuters.com/article/2015/09/24/ct-ge-idUSnBw245620a+100+BSW20150924>. See also <https://www.gov.uk/government/news/prime-minister-welcomes-export-framework-with-general-electric>.

“In today’s competitive environment, countries that have a functional Export Credit Agency (ECA) will attract investment...Export finance is a critical tool we use to support our customers. Without it, we can’t compete against foreign competitors who enjoy ECA financing from their governments. We are fortunate to have the support of UK Export Finance (UKEF), one of the most flexible ECAs in the world. The UK is pro-export and pro-manufacturing.”

The expansion in recent years in various forms of support for exporters has been documented by the *Financial Times*.⁷ Given the range of support documented in that article, the assumption that export finance necessarily corrects for market failures ought to be revisited.

In the interest of balance, it should be noted that certain developing countries have not just been expanding their export incentives but also improving the implementation of existing schemes so as to pay exporters more. A leading example comes from China. At a press conference at the State Council on July 17th, 2015, Mr. Wang Shouwen, Vice-Minister of Commerce for China, stated:

“During January to June, China’s volume of export tax rebates has increased 12.4 percent over the same period last year, which is far higher than the growth of export volumes and has greatly boosted the growth of foreign trade exports.”⁸

Practitioners and analysts of the world trading system who are committed to the principle of non-discrimination ought to be critical of every deviation from this norm. It is unfortunate that the term “protectionism” has long been associated with reducing imports. This may well have created a blind spot towards measures that artificially favor domestic firms when they export products to third markets.

Ironically, this evidence comes to the fore as WTO Members at their Ministerial Conference in December 2015 agreed to eliminate, once and for all, agricultural export subsidies. If one can accept the argument that subsidy wars in agriculture are wasteful, then what makes other export incentives any different? Having written this, it would be wrong to infer that revising the WTO’s subsidy code is the only lesson from the global economic crisis.

7 See <http://www.ft.com/intl/cms/s/0/fe1a26be-1be1-11e5-8201-cbdb03d71480.html>.

8 See http://english.gov.cn/news/policy_briefings/2015/07/17/content_281475148824853.htm.

Implications for the Future Work Program of the WTO

Coming on top of the decade-and-a-half long struggle over the Doha Round, the global economic crisis has exposed further deficiencies in the operation of the WTO. Since this is a member-driven organization, it would not be appropriate that the WTO Secretariat shoulder all of blame. The latter is not immune, however, from criticism – its weak monitoring of protectionism has provided cover for those diplomats and officials that are not committed to the principles of non-discrimination. From the point of view of global governance, if the WTO Secretariat feels it is unable to effectively monitor its Member governments, then consideration should be given to assigning this role to another official institution.

Moreover, the mismatch between the extensive resort to discrimination against foreign commercial interests and the limited number of disputes brought to the WTO for settlement, begs further questions. If the discrimination is legal, then do existing WTO rules provide for such little constraint on government behavior? If the discrimination is illegal, why are so few cases brought? Could a “glass houses syndrome” exist whereby “people who live in glass houses don’t throw stones”? Is the counterpart to the mutual indiscipline over protectionism mutual restraint in bringing dispute settlement cases? If so, a key weakness of the WTO Dispute Settlement Understanding – namely, that only WTO Members can bring cases – needs to be addressed.⁹ Otherwise, even with the best possible rule book, WTO obligations could be effectively suspended when a systemic crisis motivates major trading powers to simultaneously introduce discrimination against foreign commercial interests.¹⁰

The finding that another global economic crisis has brought to the fore prominent forms of protectionism not seen much in previous crises reflects the incentives created by an incomplete WTO rule book. Tighter rules on subsidies, localization requirements, and trade finance are needed. An ambitious WTO work program would also include negotiating new rules on export taxes and expanding the reach of the Agreement on Government Procurement. The considerable leeway many governments have to raise tariffs without breaking their WTO obligations is another matter that could be addressed as part of a package of reforms.

9 In the European Union, for example, the European Commission – acting in its role as “guardian of the treaties” – can bring legal cases against member states before the European Court of Justice.

10 This may be the most significant lesson from the global economic crisis for the governance of world trade. There are strong complementarities between fixing the WTO rule book and strengthening its dispute settlement function. Put differently, the benefits from improving one are conditional in part on improving the other.

Of course, it is always possible to put together a wish list of items for the WTO Membership to work on. However, the purpose of this exercise was to demonstrate that the recent global economic crisis has revealed significant deficiencies in the edifice of WTO rules. Making an effort to remedy their weaknesses – and bearing in mind the different types of cross-border commerce witnessed in the first quarter of the 21st century – ought to be a priority for the WTO Membership. There is plenty to be getting on with.¹¹

In sum, once one accepts that there has been considerable resort to discrimination against foreign commercial interests during the crisis era, then a series of awkward questions arises concerning the effectiveness of the multilateral trading system. These questions relate to the full range of the WTO's functions – going well beyond a minor tidying up exercise. Many national and international institutions have been thoroughly overhauled after their deficiencies were exposed during the global economic crisis – the World Trade Organization should be no exception.

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11 Of course, it must be conceded that incremental improvements in the WTO rule set that still result in an incomplete set of rules will still offer opportunities for circumvention whenever the next global economic crisis hits. Practically speaking, the process of filling in the WTO rule set will take decades, if it ever comes to pass. These observations may qualify expectations about what a rules-based trading system could ever accomplish in taming the resort to protectionism during global economic crises.

CHAPTER 7

Regional Trade Agreements and the WTO

Clemens Boonekamp¹

IDEAS Centre, Geneva

Introduction

Regional trade agreements (RTAs) are negotiated modalities for trade between two or more customs territories,² to the exclusion of others.³ By their nature, members of RTAs seek to grant trade preferences to each other, usually in the form of access to their markets, thus discriminating against non-members. Members of RTAs need not be geographically contiguous, or even close to each other; all that is needed is that they agree on arrangements for trade between themselves. RTAs have always dealt with reciprocal tariff reductions, but they are now increasingly complex, often with provisions for, *inter alia*, customs administration, standards, safeguards, services regulations, intellectual property and dispute settlement; some extend to competition, investment, labor and environment policies.

RTAs are a sub-set of preferential trade agreements (PTAs). These also include arrangements under which countries or customs territories *unilaterally* grant non-reciprocal trade preferences to other trading partners. Chief amongst these is the Generalized System of Preferences (GSP), under which (mainly developed) countries grant preferential tariff access for imports from developing

1 I thank staff of the RTA Section at the WTO, including Rohini Acharya, Jo-Ann Crawford and Maria Doner Abreu; their advice was invaluable but the mistakes are mine.

2 Normally these are countries, but I have used the phrase “customs territories” to include entities such as Hong Kong, China, and Macao, China – which are separate customs areas from China, each with their own trade policies – and to include a set of nations that collectively have a single trading identity, such as the European Union.

3 The term “regional trade agreement” is a bit of a misnomer, in that they are often not regional; traditionally, the WTO uses the term for such arrangements.

countries, with each GSP “donor” maintaining its own list of preferences and conditions under which the “recipients” are eligible for the more favorable treatment of their exports to the territory of the GSP provider. Other non-reciprocal preference-granting initiatives include i) the European Union’s Everything but Arms initiative, under which all imports – except armaments – from all Least Developed Countries (LDCs) to the European Union are tariff-free and quota-free; and ii) the African Growth and Opportunity Act (AGOA), under which imports of certain goods – mainly textiles and clothing – to the United States from eligible African countries are duty-free and quota-free.

This chapter deals essentially with RTAs and their status in the WTO, referring only in passing to the WTO coverage of unilateral, non-reciprocal initiatives.

RTAs have proliferated since the early 1990s, with well over 330 now in force compared to fewer than 30 in 1990. They also have their own terminology, with terms such as “free trade area” (FTA), “customs union” (CU), the more prosaic “spaghetti bowl” and, more recently, “mega-RTAs.” The next section will deal with the present landscape and definitional framework of RTAs, including their coverage. Following this the chapter will turn, in the third section, to the possible reasons for negotiating RTAs and the rapid growth in their number. The fourth section in a sense gets to the heart of the matter, examining the provisions under which members of RTAs are authorized under WTO rules to provide preferential treatment in their trade relations with each other, thus departing from the cornerstone principle of the WTO of *non-discrimination*. The intent, or economic rationale, of these provisions is to ensure that an RTA strengthens – or at least does not weaken – the multilateral trading system, but it is not always an easy matter to know whether this is indeed the case. The section therefore also looks at the relatively recent RTA Transparency Mechanism, which is a peer review exercise to improve the understanding of individual RTAs and, it is hoped, their abidance of WTO disciplines. The chapter then goes on to question, in the fifth section, whether RTAs, through their departure from non-discrimination, undermine the role of the WTO as the guardian of the multilateral trading system, particularly in light of the move towards very large RTAs such as the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP). The final section briefly concludes.

The RTA Landscape

RTAs come in many shapes and forms, but generically they are either free trade agreements (FTAs) or customs unions (CUs). The two or more members of an FTA reduce the barriers to trade between themselves but retain independent trade policies; thus, for example, tariffs on imports from FTA partners will be lowered (normally to zero), but each member of the FTA will maintain its own tariffs vis-à-vis imports from non-members. Such an FTA may cover both goods and services, though technically a services FTA is known as an “economic integration agreement.” An FTA may also cover less than substantially all of the trade in goods between partners, and is then called a “partial scope” agreement.

As members of an FTA retain their own tariffs for trade with non-members, *rules of origin* are needed to identify products from members that are eligible for the lower duties and restrictions that apply to trade between members. In the absence of such rules of origin, non-members could divert their product to the member of the FTA with the lowest duty on that product and then tranship it to the final destination in the FTA. For example, if FTA members *A* and *B*, with zero duties on trade between themselves, imposed duties on imports of motor vehicles from non-members of 10% and 5%, respectively, then a non-member exporting motor vehicles to *B* could initially ship them to *A* and then tranship duty-free to *B*, thus saving 5%; rules of origin prevent such diversion.

One of the largest FTAs is the North American Free Trade Agreement (NAFTA). With Canada, Mexico and the United States as members, NAFTA accounts for some 13% of world exports. It provides duty-free treatment for virtually all goods originating in the members, has an extensive services component, deals also with non-tariff barriers, standards, competition, investment, intellectual property and trade disputes between members and has supplemental agreements to handle labor and environmental issues. In trade parlance, it is known as a *deep* agreement, as opposed to a *shallow* agreement that would cover border measures but little else. Other large FTAs include the agreement between the Association of Southeast Asian Nations (ASEAN)⁴ and Japan, which applies only to goods and is thus a “true” FTA as compared to one – like NAFTA – that also has a services component, with this component then being known as an “economic integration agreement” (see above); the ASEAN Free Trade Agreement (AFTA), which applies to goods and is relatively

4 The members of ASEAN are Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam; Papua New Guinea is an observer.

unusual in that its members are all developing countries, a self-designation in the WTO; agreements between ASEAN and, respectively, China, India and the Republic of Korea, all of which are goods and services agreements; and the European Free Trade Association (EFTA),⁵ which is also a goods and services agreement. These FTAs may soon be joined by a mega-FTA, the Trans-Pacific Partnership (TPP), which was recently agreed but has not yet come into force; its membership accounts for around 40% of the global economy.⁶ Eventually, the Transatlantic Trade and Investment Partnership (TTIP), which is currently being negotiated between the European Union and the United States, may also join the ranks of FTAs.

Examples of smaller FTAs include agreements between Georgia and Armenia (goods); Guatemala and Chinese Taipei (goods and services); Hong Kong, China and Chile (goods and services); and India and Nepal (goods), which has rather limited coverage and is thus also known as a “partial scope agreement.”

To date, somewhat over 230 “pure” FTAs have been notified to the WTO.⁷ In addition, the WTO Secretariat is aware of some 70 such agreements that have not (yet) been notified.⁸ Over 130 FTAs with a services (“economic integration agreement”) component have been notified to the WTO, although a limited number of these are part of customs unions (see below); there are probably fewer than five such agreements that remain un-notified. Finally, there are in the order of 15 partial scope agreements.

The second generic category of RTAs is customs unions. The defining feature of a CU is that its members have a common external tariff. There is therefore no need for rules of origin between the members; once products are in the territory of the CU, they are technically free to move to any part of the CU, albeit subject to the regulatory, non-tariff provisions of each member of the CU.

The largest CU is the European Union, with a share of some 16.5% of the world’s exports of goods and services (not including intra-EU trade). Intra-EU trade, underpinned by the free flow of goods and services within the European Union, is very significant and accounts for some 50% of the exports of almost each of the members. As an indication, in 2014 total EU exports of manufactures (agricultural products) accounted for 38.5% (38%) of world exports, whereas extra-EU exports accounted for just 14.6% (10.1%)⁹. This

5 EFTA members are Iceland, Liechtenstein, Norway and Switzerland.

6 The 12 members of TPP are Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam.

7 Source: <http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx>.

8 Source: WTO document WT/REG/W/95, 17 September 2015

9 Source: https://www.wto.org/english/res_e/statis_e/merch_trade_stat_e.htm.

rather remarkable degree of integration reflects¹⁰ the comprehensiveness of the agreement, which has provisions on not just tariffs but virtually all aspects of trade in goods and services between the members, including competition, domestic regulation, environment, government procurement, intellectual property, labor, mutual recognition (services), standards and subsidies. Indeed, the European Union has a single trade policy and, unlike all other RTAs, speaks with one voice at the WTO.

The EU is also an example of an *open* RTA. If a country is able to accept and implement the “*acquis communautaire*” (EU law) and the existing members agree, it can apply and/or be invited to accede to the EU. Since the Treaty of Rome of March 1957, the original six members (Belgium, France, Italy, Luxembourg, the Netherlands and West Germany) have increased to 28.¹¹

Other examples of CUs include the Central American Common Market (CACM),¹² which is for goods only; the East African Community (EAC),¹³ which is for both goods and services; EU–Turkey, which is for goods only (and is emblematic of the fact that the EU has RTAs with each of its neighbors among its total of 37 RTAs, making it the WTO member with the largest number of RTAs);¹⁴ the Southern African Customs Union (SACU),¹⁵ which is for goods and is arguably the oldest CU, having been founded in 1910; and the Southern Common Market (MERCUSOR),¹⁶ for both goods and services.

In all, 18 CUs have been notified to the WTO.¹⁷ The question arises as to why there are so few CUs compared to FTAs. The answer is reasonably straightforward: there is a larger cession of sovereignty in adopting a common external tariff (as in a CU) than in retaining national tariffs vis-à-vis third countries (as in FTAs).

The lexicon of RTAs contains some cute terms, which nevertheless point to real phenomena. Most prominent among these is the phrase “spaghetti bowl.”¹⁸ This refers to a complex network of RTAs (Annex 1) and the complications that may then arise. For example, through various arrangements, a country may be party to more than one RTA with another trading partner, as is the

10 I use the word “reflects” advisably because causation is not clear.

11 The members are Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovak Republic, Slovenia, Spain, Sweden and United Kingdom.

12 The members are Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua.

13 The EAC’s members are Burundi, Kenya, Rwanda, Tanzania and Uganda.

14 Alone among RTAs, the European Union is a WTO Member in its own right, as are each of the Union’s 28 members.

15 SACU’s membership consists of Botswana, Lesotho, Namibia, South Africa and Swaziland.

16 Its original members were Argentina, Brazil, Paraguay and Uruguay.

17 Source: <http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx>.

18 The term was first used by Jagdish Bhagwati in his 1995 paper “U.S. Trade Policy: The Infatuation with Free Trade Agreements” (Bhagwati, 1995).

case for Singapore, which at present has three separate RTA links with New Zealand,¹⁹ and a fourth when TPP comes into force. The same Singapore product may thus be subject to three different rules of origin to qualify for preferential tariff access to New Zealand; similarly, as RTAs are normally phased in such that the preferential tariff may not be zero, the same product may face three different tariffs into New Zealand. This could certainly increase “search costs,” although in the case of Singapore the authorities have put in place a superb website to keep its exporters fully informed and to facilitate decisions. Moreover, if the producer seeks preferential access for the product elsewhere under another FTA, the rules of origin may again be different. This might require a number of distinct production processes for the same product, potentially reducing the benefits of economies of scale. When referred specifically to trade among Asian countries, the spaghetti bowl becomes the “noodle bowl.” Note that these spaghetti/noodle bowl effects could apply not just to tariffs and/or rules of origin, but also to all other arrangements between the members of an RTA (the regulatory environment, intellectual property rights protection, etc.).

An associated word is “lasagnas,” which refers to a consolidation among RTAs such that the spaghetti/noodle bowl becomes less complex. An example of this is the Mexico–Central America agreement, which replaced bilateral agreements between Mexico and Central American countries.

Figure 1, compiled by the WTO Secretariat, shows the evolution and stock of RTAs notified to the WTO up to late 2015. In all, there were 265 RTAs in force; in addition, as noted above, the Secretariat knew of at least 70 RTAs that had not been notified.

The cumulative total of notifications of RTAs in the period from 1948 to late 2015 is over 600, of which over 400 were notifications of RTAs still in force. The reason why the number of notifications exceeds the physical number of RTAs in force is that, under WTO procedures, the goods and the services components of RTAs are notified separately, as are accessions to existing RTAs.

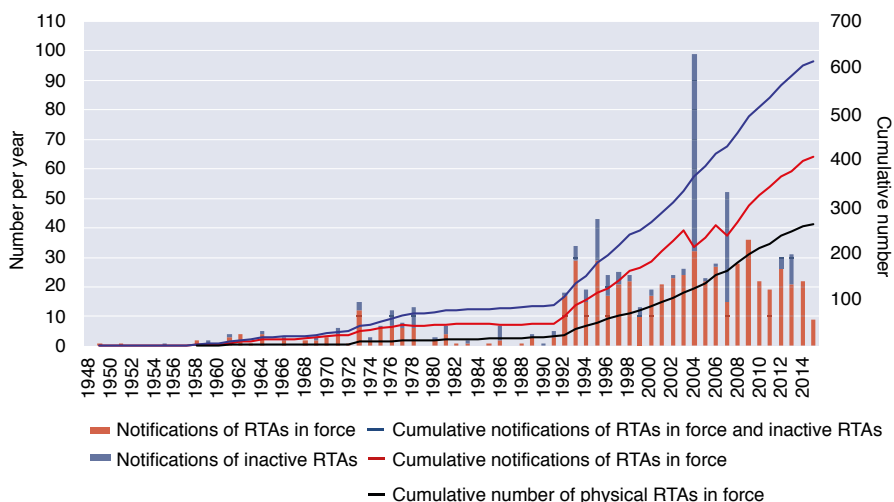
Total notifications include both notifications of RTAs currently in force and past notifications of RTAs that are now no longer active or in place, mainly reflecting both the evolution of agreements as they are superseded by “deeper integration” agreements among the same members²⁰ and the “lasagna”

19 These are the ASAEN—Australia/New Zealand FTA, the Agreement between New Zealand and Singapore on a Closer Economic Partnership (ANZSCEP) and the Trans-Pacific Strategic Economic Partnership (TPPFTA) between Brunei Darussalam, Chile, New Zealand and Singapore.

20 For example, bilateral agreements between the European Economic Communities (EEC) –the forerunner of the European Union – and a number of Mediterranean countries were later replaced by “deeper” agreements among the same parties to include, for instance, competition, investment and intellectual property.

effect, sometimes as a result of EU enlargement. Thus there is a spike in the deactivation of RTAs in 2004 when 12 new members acceded to the European Union. Prior to accession, each new member had an RTA with at least one other new member and also with the European Union, all of which were then replaced by membership of the European Union.

Figure 1: Evolution of regional trade agreements in the world, 1948–2015



Note: Notifications of RTAs: goods, services & accessions to an RTA are counted separately. Physical RTAs: goods, services & accessions to an RTA are counted together.

Source: WTO Secretariat.

In summary, in force in late 2015 were 137 RTAs in goods, 127 RTAs in goods and services and one RTA in services only (the latter being the European Economic Area, or EEA, with the 28 EU and four EFTA countries as its members). Three other points are worth noting: i) the prevalence of RTAs is such that all WTO Members are now party to at least one RTA, with Mongolia, for a long time the only Member without RTA links, having recently signed an agreement with Japan; (ii) the vast majority of the RTAs are bilateral, essentially because they are easier to negotiate; and iii) the “deeper” agreements are invariably between the more developed economies. Indeed, there are as yet few RTAs between developed countries and LDCs, an aspect that is dealt with in more detail below

Figure 1 also shows the growth in the number of RTAs. Following some 40 years of relative calm after 1948, the number of RTAs has grown almost exponentially since the early 1990s. This has made the trading system more complicated, probably reducing transparency and predictability, and has

introduced considerable discrimination among trading partners. These factors could contribute to making it more difficult for individual traders to arrive at decisions, thus possibly increasing contract-costs and prices. The obvious question, and the subject of the next section, is “Why so many RTAs?”

The “Whys?” and “Why Nots?” of RTAs

Governments are not confused about the gains from trade; by and large, they agree on the possibility of such gains. National administrations understand that a more liberal trade regime is likely to result in less bias in the transmission of international price signals, thus fostering more efficient resource allocation and improving a country’s production and consumption potential. The composition of output is likely to shift towards internationally competitive sectors, increasing the exports, employment and wages in those sectors, and away from import-competing activities, which will shed employment. Thus, while the price of, say, a t-shirt may decline – due to t-shirts now being sourced from competitive external producers – there could be noisy protests from the unemployed in the shrinking sectors. Although (and this is well established in economic theory) the “winners” could compensate for the “losers,” resulting in a net overall gain, this could require changes in social and fiscal policy that may be politically difficult to achieve. In short, if economies are to reap the benefits of a more liberal trading regime, there needs to be adjustment, and this can be painful.

Governments seeking to liberalize their external trade regimes would often prefer to do so in the context of comprehensive multilateral negotiations, such as the WTO’s Doha Development Agenda (DDA). This would strengthen – or at least not weaken – the non-discrimination, transparency and predictability characteristics of the WTO-led multilateral trading system, which is widely regarded economically as the first-best option for achieving the gains from trade. Also, and very importantly, it would offer significant trade-offs that, from a political point of view, would allow the export sectors in a country to “buy off” the import-competing producers (“yes we may be opening our markets to import competition, but our export opportunities will increase substantially, making us better off”). Note that this is a purely mercantilist argument (“exports are good, imports are bad”), whereas in fact it can be shown, as above, that liberalization can be its own reward.²¹ Unfortunately, or otherwise, the politics

21 As a corollary, and from the consumer perspective (and we are all consumers), imports are good because they improve consumer choice, and exports are bad because they reduce domestic consumption possibilities, with their role then being to pay for imports.

of liberalization work in this manner – trade agreements are treaties and they need to be ratified!

The ideal is difficult to achieve. The Uruguay Round was launched in 1986 and was concluded successfully in 1994. Since then success has been much more difficult to find. The DDA was initiated in 2001, but to date progress has been extremely sluggish at best, with few results except for the notable exceptions of the Trade Facilitation Agreement (which is not yet ratified), the RTA Transparency Mechanism (which is being provisionally applied) and decisions related to food security and export competition. The reasons are clear – the WTO has 162 Members (as of end-November 2015), each with its own agenda and red-lines which can and do change over time. It is therefore extremely difficult to find consensus, which is the way the WTO makes decisions,²² especially since an agreement establishes obligations that are legally binding. Given this reality, and the fact that governments will continue to seek the benefits that trade can bring, they are likely to look elsewhere for partners. This also brings the advantage that they can extend their potential agreements into areas not covered by the multilateral trade negotiations, such as competition and investment.²³ These factors were certainly influential in the decision to negotiate TPP, as they are in the ongoing negotiations of TTIP. And indeed Figure 1 shows that there has been a bit of an acceleration in the number of RTAs notified and brought into force since 2008, when it became evident that the already slow progress on the DDA, which arguably had already contributed to the growth in the number of RTAs, was going to falter even more, perhaps leading to the agreement's demise.

There are many other reasons, both economic and/or political, for entering into a particular RTA. Important among these is better *access* to a large market than that provided under that country's membership of the WTO. This was certainly a consideration for New Zealand when it entered into China's first country-to-country, bilateral RTA in October 2008.²⁴ The agreement was *procedurally* important for China also, because New Zealand denoted China as a "market economy," which is a status that provides somewhat more favorable treatment in the application of the WTO's trade remedy provisions.

22 There is provision for voting, but it has not been used.

23 At the outset of the DDA, the negotiating mandate included competition, investment, government procurement and trade facilitation, known as the "Singapore issues" because they were first brought onto the WTO agenda at the 1st WTO Ministerial Conference in December 1996. All but trade facilitation were subsequently dropped, not least because many developing countries were not comfortable with their inclusion and it was thought that this might be slowing progress on the DDA.

24 At that point China was already part of the Asia Pacific Trade Agreement (APTA), a partial scope RTA to which it acceded in 2002, and had goods and services FTAs with ASEAN (2005) and with Hong Kong, China and Macao, China (both 2003).

Countries have sensitive sectors – ones they would like to protect – such as agriculture in many countries (both developed and developing), textiles and clothing, and steel (mainly in developed countries). This could facilitate negotiations with *like-minded partners* for RTAs, or at least those that are less likely to pressure them on the sensitive sectors. Thus, for example, EU bilateral RTAs are generally very light on agriculture (indeed, the European Union’s customs union with Turkey excludes agriculture), those of Japan and Korea tend to avoid rice, and those of the United States are careful to retain special provisions for clothing, usually through the retention of high tariffs and rules of origin that may in fact be “fiber forward” (the raw material needing to be grown in the exporting country). “Like-minded” can also apply, of course, to those who seek partners to agreements that go beyond the normal WTO disciplines, such as the US–Australia RTA (2005), which includes provisions on competition, environment and labor and is WTO-plus on matters such as trade-related intellectual property rights.

RTAs are also used to *lock in* reforms. A telling example of this is Chile, which since its first RTA (with Mexico in 1991) has used an RTA strategy to systematically lower its applied tariffs, with a view, *inter alia*, to improving domestic resource allocation. It also serves as an example of using RTAs for *learning by doing*. When first setting out to enter into the trading system, a country’s traders need to learn how to do so, and this is perhaps best done by encouraging contracts with those with a similar culture, language, and so on. Such RTAs can be instrumental in informing how to negotiate and can subsequently lead to deeper RTAs, as was the case for both Chile and Mexico. A more recent example of this is the Japan–Mongolia Economic Partnership Agreement, signed in February 2015. This agreement also serves as an example of the “defensive” or, closely related, “bandwagon” and “domino” reasons behind RTAs. If *A* negotiates an RTA with *B*, a close trading partner *C* is likely to be close behind in seeking RTAs with both *A* and *B*; thus the Chile–Korea Agreement was relatively closely followed by the Chile–Japan Agreement. More generally, when the United States joined the European Union in adopting “regionalism,” side by side with “multilateralism”, as a trade policy track (with US–Israel, US–Canada and then NAFTA), it became clearer, indeed indisputable, that RTAs were a permanent feature of the trade landscape. Others quickly sought to follow the trend – not least Japan and Korea, which had hitherto been adherents of “multilateralism” only – and many were prompted to consider/request RTAs either with major traders or with each other as a defensive action.

Politics also plays an important role. In fact, trade policy is integral to the foreign policy of many countries, with RTAs a possible element for strengthening

diplomatic ties. The Treaty of Rome, establishing the EEC, was not without a certain political motive, with the idea in the background that “those who trade with each other do not go to war with each other.” Equally, the recent enlargements of the European Union to include Central and Eastern European countries was motivated at least in part by the notion that integration into a democratic, market-oriented system would provide those countries with a stable platform for their reforms. Also, it is difficult to credit that the United States’ agreements with Israel and Jordan were motivated only by economic factors, nor indeed its agreement with Panama. There are many more such examples, probably including TPP. In fact a look at Figure 1 shows that the surge in RTAs coincided roughly with the dissolution of the USSR. Many of the newly emerged countries, and those previously in the sphere of influence of the former USSR, sought RTAs as a step or “building block” towards their fuller integration into the multilateral trading system. Indeed, as with any country entering into an RTA, they may have acquired valuable technical and negotiating skills, as well as important allies, for their role in the WTO system. Also, on a slightly cynical note, trade ministers are politicians and need to demonstrate achievements to retain their portfolios; the signing of an RTA is a marvelous photo opportunity!

But RTAs have downsides. These include, as already noted, the beclouding of the trading environment with discrimination and complexity – the “spaghetti bowl” is real. Also important among the negative aspects of RTAs is that they tend to *divert* trade – imports are sourced from preferential partners rather than from the world’s low-cost suppliers, resulting in losses in efficiency and to consumers. Moreover, RTAs have *holes* that reduce their benefits. It is, for example, very difficult (if not impossible) to agree bilaterally, or even in a larger grouping, on effective measures to limit trade-distorting domestic support for agriculture; this can probably only be done in a multilateral setting. However, RTAs also can and do *create* trade – this is in fact their purpose – although this benefit can be reduced, *inter alia*, by exclusions from the coverage of an RTA. The trade-off between trade creation and diversion is central to WTO provisions on RTAs, and its discussion leads in the next section.

An RTA entails costs for traders. The additional search costs have already been noted. Compliance with the rules of origin, and the paper work involved, can also be expensive, sometimes to the point of eliminating an RTA’s margin of preference for the product. This can be exacerbated by the fact that the production process might need to be changed to meet the rules of origin. Anecdotal evidence suggests that a margin of preference of up to six percentage points may at times not be enough to compensate for the additional costs;

traders may then choose to access the market using the “most favored nation” (MFN) tariff, applicable to imports from non-preferential sources.

RTAs can attract attention and resources of even the largest national administrations away from the multilateral trading system. They then become a *stumbling block* to improvements in the acknowledged “first best” for the conduct of trade. And this can happen in other ways. A country with preferential access to an important market for its main exports may block a multilateral tariff deal to prevent its preference margin being reduced; in effect, it would seek to limit competition.

As a final point in this section, RTAs can marginalize smaller trading nations, including LDCs. The fostering of freer trade through RTAs may help accustom countries to competitive pressures and to sophisticated regulatory regimes, and thus may promote wider agreement on – i.e. be a building block towards – a stronger, more liberal multilateral trading system. But the smaller traders, and African LDCs in particular, are rarely partners to an RTA with major, competitive traders, which may place them at a disadvantage in the constantly changing trading environment. These countries invariably do have access to the preference schemes of their partners, but these are unilateral and can be changed or withdrawn – there is more than one example of foreign direct investment leaving a country as the latter’s preferences into a particular market (or markets) are altered.

RTAs now pervade the trading environment and, as noted, there are arguments both for and against their continued presence and growth. The question is urgent, therefore, as to how they are accommodated in the WTO, as the anchor and guardian and of the multilateral trading system.

RTAs in the WTO

The WTO is an economic organization encased in law. The rights and obligations of Members are designed to help them reap the gains from trade, but they are written in legally binding form, with a legal contract then underpinning economic intent. So too with RTAs: the economic concept of *net trade creation* provides a possible rationale for the WTO to allow the discrimination of RTAs as an exception to its cornerstone tenet of non-discrimination.

Table 1 may help to explain the concept. Consider three separate cases:

1. Home produces a good at 35, Partner at 25, and the Rest of the World (RoW) at 20. Home maintains a zero tariff on imports. Home will then import the product from RoW for the maximum gain for consumers – it is the optimal outcome.
2. Home has a tariff of 100%, raising the prices of Partner's and RoW's products to 50 and 40, respectively. It buys the Home product; there is no trade. Then it enters into an RTA with Partner, such that there is a zero tariff on Partner's product. It imports from Partner at 25, which is better than the Home price of 35; this is *trade creation*.

Table 1: Trade creation/diversion

	Home	Partner	Rest of world
Price	35	25	20
Tariff of 100%	35	50	40
Tariff of 50%	35	37.5	30

3. Home has a tariff of 50%, raising the price of the good from Partner and RoW to 37.5 and 30, respectively. Home imports from RoW at 30 and it collects 10 in tariff revenue – the net cost to Home is actually 20. It then enters into an RTA with Partner. It switches (“diverts”) its source of imports from RoW to its RTA – imports now cost 25 rather than 30, but the tariff revenue of 10 is no longer collected, for a net cost of 5. Thus, *trade diversion* is costly.

The economic position that follows from this is that if an RTA is *net trade creating*, the system as a whole will benefit. But this is what economists call a “comparative-static” result as nothing else has changed; the dynamics of a situation, such as changing tastes, could alter the outcome. Which is to say that it is very difficult to know whether an RTA is or will be net trade creating, or otherwise.

The WTO's disciplines on RTAs reflect this difficulty. Article XXIV of the WTO's General Agreement on Tariffs and Trade (GATT), complemented by its Understanding as agreed in the Uruguay Round, stipulates the legal framework for RTAs in trade in goods. Article V of the WTO's General Agreement on Trade in Services (GATS) does the same for RTAs in trade in services. The 1979 Enabling Clause provides for the mutual, preferential

reduction of tariffs and non-tariff measures among developing countries.²⁵ These provisions represent the “permission” for WTO Members to enter into RTAs. But there are conditions.

GATT Article XXIV requires, *inter alia*, that in forming an RTA, the duties and other *restrictive* regulations of commerce, except those permitted under WTO rules, be eliminated with respect to *substantially all the trade* between the parties. GATS Article V requires *substantial sectoral coverage* and the absence or elimination of *substantially* all discrimination. The Enabling Clause does not have such requirements. Article XXIV also stipulates that the duties and other regulations of commerce (note the absence of the word “restrictive” in comparison to the earlier language) applied by the parties to an RTA shall not be higher or more restrictive with respect to third parties than those prior to the formation of the RTA – the so-called “general incidence” clause, in the case of customs unions.²⁶ In the case of the Enabling Clause, members to an RTA are admonished not to raise barriers to, or to create *undue* difficulties for, the trade of other WTO Members. That is, RTAs are expected to be at least neutral with respect to their trade with third parties. Nor is there agreement in the WTO on important lacunae, such as preferential rules of origin, which could bring uniformity to how such measures are to be evaluated.

The intention of the above phrases is clear: an RTA should be to the benefit of the system – it should be net trade creating. The problem is also clear: how is any of this to be measured? These are normative matters that defy obvious quantification. And what is the difference between “other restrictive regulations” and “other regulations”? Some have suggested that 95% would be a “good” measure for “substantially all the trade,” but even at 100% there could be net diversion, for example, as a result of preferential investment rules or WTO-plus trade in intellectual property requirements. The point is that conditions evolve – a non-restrictive regulation may be changed to become restrictive for non-preferential partners, as could be the case for the recognition of professional standards. In short, it is very difficult for Members to assess whether an RTA complies with WTO rules. It is not surprising then that only one RTA has ever been found to be compliant, namely the customs union between the Czech Republic and the Slovak Republic, which was established when Czechoslovakia became the two republics and which “disappeared” when both states acceded to the European Union in 2004. Nor does WTO

25 Its full name is the 1979 Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries. The Enabling Clause also provides the necessary waiver from non-discrimination for GSP schemes; programmes such as AGOA require a separate waiver from the Members, and such a waiver is usually time-bound whereas the Enabling Clause is permanent.

26 The Understanding brought some clarity to this in the case of tariffs, but it remains an awkward, point-in-time calculation.

Dispute Settlement provide precedents. No RTA in its own right has been subject to a legal complaint at the WTO;²⁷ indeed, given the uncertainty about compliance, that would be almost like “people in glass houses throwing stones.”

Members have not been idle on the matter, being very aware that it is of systemic importance to the WTO. The Committee on Regional Trade Agreements (CRTA) was established in 1996 to oversee RTAs, but no reports have been issued on the compliance of an RTA. Besides the difficulty in determining compliance, no party will normally agree that its RTA is non-compliant, if only for fear of being drawn into dispute settlement, with the result that the compliance exercise has essentially fallen by the wayside.²⁸

In 2001 the clarification and improvement of RTA disciplines was entrusted to negotiators in the DDA. However, agreement has escaped them in the matter of rules, including guidance on the term “substantially”, coverage (whether, for example, all goods RTAs should include agriculture) and uniformity of rules or origin. Nevertheless, there has been considerable progress in the area of transparency.

Members decided at an early stage of the negotiations that they needed to know more about the facts and figures of the RTAs in force. This could lead to a better appreciation of the impact of RTAs on the multilateral system, could bring understanding to elusive concepts such as “substantially,” and, under peer review, might lead to an improvement in the nature and structure of RTAs, to the benefit of the system. This led, in December 2006, to the WTO General Council’s decision to apply, on a provisional basis, the Transparency Mechanism for Regional Trade Agreements.²⁹

The Mechanism provides for the early notification of RTAs. They are subsequently considered by the WTO Membership on the basis of a *factual presentation* prepared by the WTO Secretariat under its own responsibility but in close consultation with the parties involved.³⁰ The factual presentations, minutes and questions and answers are published, but no report is issued. To date well over 200 factual presentations have been distributed, providing a wealth of verified data. This information feeds into an RTA database, mandated by the Mechanism, maintained by the Secretariat and made available to the public and, hence, for purposes of research.

27 In two disputes RTAs have been an issue, essentially concerning whether they can be used as a legal defence for perceived discrepancies between some of their provisions and existing WTO rules.

28 Prior to the CRTA, individual Working Parties examined RTAs.

29 See WTO document WT/L/671 (18 December 2006) for the text of the decision. The Mechanism is also described in some detail on the WTO’s website at https://www.wto.org/english/tratop_c/region_c/trans_mecha_c.htm.

30 The consideration in the CRTA if the agreement is notified under GATT Article XXIV or under GATS Article V; if it is notified under the Enabling Clause, the discussion takes place in WTO’s Committee on Trade and Development.

The consideration of an RTA under the Mechanism does *not* include an assessment of its consistency with WTO provisions, and it is precluded from being used for purposes of dispute settlement. This is intentional, obviating a discussion of normative issues and encouraging a frank exchange on the facts of the RTA.

The Mechanism has certainly improved transparency with respect to RTAs. However, there is no escaping the fact that the WTO's legal provisions on RTAs remain very difficult – essentially impossible – to enforce. Thus, it is up to Members to ensure that their RTAs meet the *spirit* of the WTO's legal provisions – to benefit, or at least complement, the system, supporting the WTO.

RTAs: Do They Help or Hurt?

The question is seemingly of some importance. After 14 years of negotiations the DDA has yielded few results and may yet fail or be abandoned. This leaves many with the perception that the WTO has lost some credibility as the mainstay of the multilateral trading system, with an agenda that may not reflect the realities of the trading environment, particularly the very significant sway of China and the maturing of “new” technologies such as the Internet. The continued growth in the number of RTAs, including the steps towards new mega-RTAs, adds to – and is perhaps influenced by – the notion of a WTO on the wane, with the RTAs arguably more in tune with the trading needs of their parties.

A rebuttal could come in two intertwined parts: i) the WTO is about a great deal more than just the DDA; and ii) it is not clear that RTAs have seriously undermined the WTO, although the jury might still be out on the possible new mega-RTAs, which after all are not yet in place.

The WTO remains a valuable global public good. The important day-to-day work will continue in the WTO Committees that implement its various agreements such as that on agriculture, contributing to freer, more predictable trade flows. So too will its significant work on transparency, including the trade policy reviews of Member countries, the monitoring reports on protectionism that feed into the G20, and the discussion of RTAs; these functions fruitfully inform both Members and the public. And the dispute settlement mechanism continues to provide sterling service in ruling on disagreements between Members in their use of trade measures, fostering abidance by the rule-of-

law between parties. The WTO also curbed protectionism³¹ and kept markets open during the recent financial crisis, thus helping to contain contagion and perhaps a global depression.

Moreover, despite the DDA and intense RTA activity, the WTO remains an impressive negotiating forum for global trade rules, as evidenced by the recent Trade Facilitation Agreement. And, as noted, it is probably only in the WTO that disciplines in areas such as agricultural support could be agreed. Nor is it clearly the case that the WTO's ability to negotiate on market access has been impaired by RTAs, where the gains and trade-offs might already have been made. For example, the Information Technology Agreement (ITA), which eliminates tariffs on a large number of high-tech goods, has grown to 81 members, compared to fewer than 30 when it was first signed in December 1996, and covers some 97% of trade in the products concerned, with the liberalization applied also on a non-discriminatory, MFN basis to non-members.

In a like manner, precisely during the time when RTAs were showing spectacular growth in numbers, the number of WTO Members also grew rapidly. The WTO now has 162 Members, compared to the 128 members of the GATT, the WTO's predecessor. And, in fact, when the WTO was founded on January 1st, 1995, its 100 Members accepted a considerably higher level of multilateral obligations than they had under the GATT. Those agreeing and acceding to the WTO clearly sought to ground their trade policies in a non-discriminatory, stable environment. By this interpretation, the WTO has remained a firm anchor of the system.

The anchor could be firmer still if there were multilateral trade agreements in areas like competition and investment, and if progress could be made in services and preferential rules of origin. For their part, RTA parties might think about steps such as cumulating origin across their various agreements – as in the Pan-Euro-Mediterranean preferential rules of origin – and the mutual recognition of standards; these could certainly promote deeper integration within the RTAs but, as always with discriminatory measures, the net benefit is uncertain. Parties to RTAs might also consider extending their tariff preferences on a non-discriminatory basis in the case of products where the MFN rates are already low, say at a “nuisance” level, thus both obviating the need for rules of origin on these products and enhancing competition.

31 This point is not beyond debate. In their chapter in this volume, Simon Evenett and Johannes Fritz argue rather persuasively that there was a surge in protectionism early in the financial crisis, although not in the main through resort to “traditional” measures, such as tariffs and trade defence.

The question remains as to whether the situation could be significantly changed by the emergence of new mega-RTAs: TPP, TTIP and also the Regional Comprehensive Economic Partnership (RCEP) between the 10 members of ASEAN, Australia, China, India, Korea and New Zealand. One might envisage a situation in which TPP and TTIP share the same template for their RTAs, grant each other cumulation in origin, agree on the mutual recognition of standards and apply each other's dispute settlement rulings. This would create, *de facto*, a new trade regime for some 50% of world output, and would exclude major traders such as Brazil, China and India. In this context, RCEP might well be defensive. And while the political obstacles to the realization of this thought experiment are substantial, it does give some idea of the possible significance of these potential mega-RTAs for the multilateral trading system. That said, the economic impact of these agreements may be less than overwhelming, with zero MFN rates already in place – due to the Uruguay Round and ITA – on a wide range of products (particularly manufactures) and most other rates low. There could be significant diversion in some areas, however, particularly agriculture in TPP, and perhaps regulations and investment.

Nor is this the system's first experience with mega-RTAs, with the European Union and NAFTA already forming part of the landscape. Both have often played positive leadership roles in the WTO, and indeed its founding hinged in part on critical work and compromises by the European Union and the United States. Similarly, the new mega-RTAs could be important in updating the WTO with their experience in investment agreements, for example – they could lead on setting the frameworks. In this regard, with the United States being central to both TPP and TTIP, its commitment to multilateralism will be critical – and the answer to that may be as much political and economic.

Conclusion

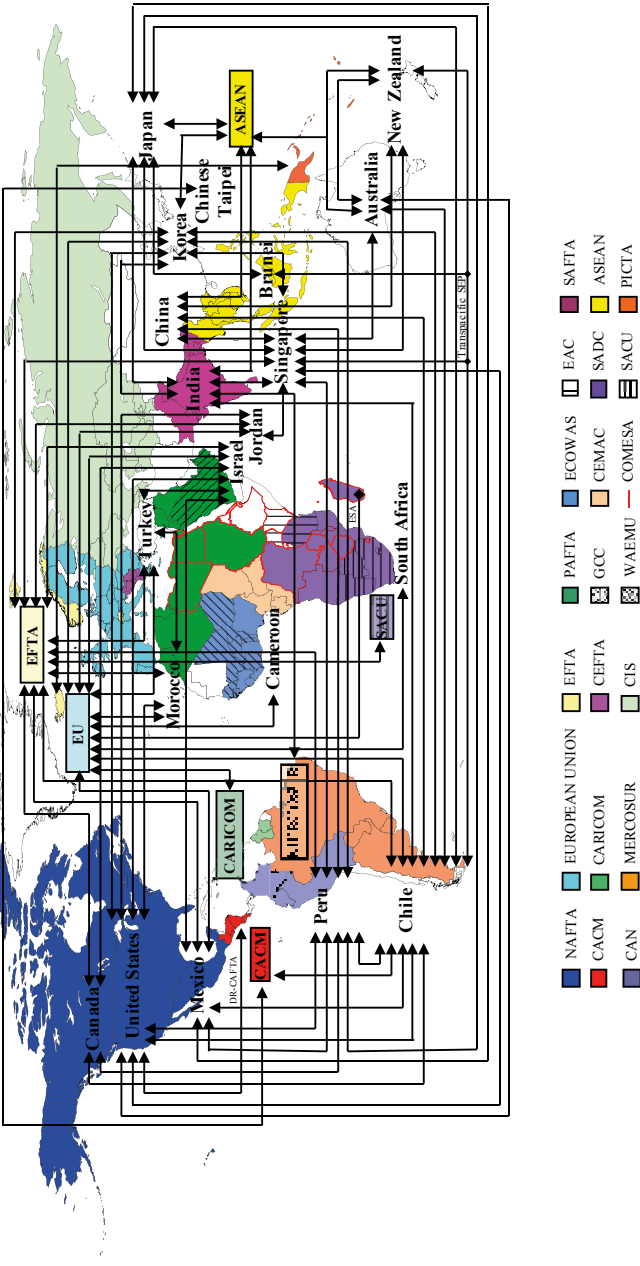
RTAs have certainly complicated the trading environment, but is not clear that they have undermined the WTO; they may have supported integration into the multilateral system. This system has provided significant benefits, including – and perhaps in particular – for the major traders. It is in their own interest to safeguard the integrity of this global public good. Given the past record, hiccups and the DDA notwithstanding, they are likely to do just that.

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Annex 1

The “Spaghetti Bowl”¹: What a complex web we weave when first we set out to ... negotiate RTAs



This chart is an example of the complexity that arises—it still leaves out quite a lot as otherwise it would become completely unreadable
Source: Acharya (2015).

CHAPTER 8

What Is the “Networked Economy”?

Nick Ashton-Hart

When most people think of the Internet, they think of what they use online – search engines, social media, streamed video and audio services, and email. That’s not a good definition for the digital economy, though – it’s too limited.

The “business-to-consumer” (B2C) services like those we use everyday are only about 10% of the economic value proposition of services with a digital dimension. The other 90%¹ is business-to-business services (B2B), such as “Cloud” and supply chain management systems and “industrial Internet”² applications.

The Internet has made many services exportable in a way that was previously impossible. While outsourcing may be controversial, it is a good example of this phenomenon, as networking technologies have made distance and geography irrelevant to the competitiveness of payroll services, legal discovery services and customer relationship management, including, famously, call centers. This has contributed to making services the largest segment of the world economy in GDP terms (Lanz and Maurer, 2015) and the largest employer even in developing countries since the turn of this century, 20 years after it became true for OECD countries.³

Beyond services, 75% of the economic value of the digital economy accrues to the benefit of traditional bricks and mortar businesses of all kinds (McKinsey Global Institute, 2011a,b). Think for a moment about the economic consequences of that fact, given that the size of the digital economy – in direct

1 There are various sources for this figure, but perhaps the most useful reference is the UN Conference on Trade and Development’s Information Economy Report 2015 (UNCTAD, 2015).

2 For a good overview that’s layman friendly, see Bruner (2013).

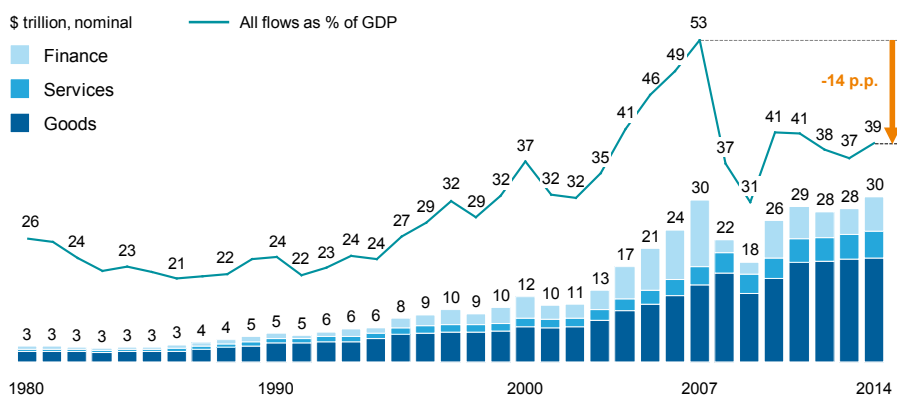
3 See the supporting datasets for the International Labour Organization’s Global Employment Trends 2014, at http://www.ilo.org/global/research/global-reports/global-employment-trends/2014/WCMS_234879/lang-en/index.htm.

and indirect terms – is estimated as being in the order of 3.4% of GDP in developed economies alone (OECD, 2013: Table 2).

At the same time, the latest studies we have show that while flows of non-digital goods and services have actually declined relative to GDP, data flows have expanded 45-fold, with an estimated positive contribution to GDP of 10% (McKinsey Global Institute, 2016).

Figure 1: After 20 years of rapid growth, traditional flows of goods, services and finance have declined relative to GDP

Flows of goods, services, and finance, 1980–2014



Source: Exhibit E1 from McKinsey Global Institute (2016); IMF Balance of Payments; World Bank; McKinsey Global Institute analysis.

Taken together, this macro picture suggests a definition for the Internet or the digital economy similar to that from the 2008 OECD Ministerial: “... the full range of our economic, social and cultural activities supported by the Internet and related information and communications technologies” (OECD, 2008).

A key foundational objective of “offline” trade policy is to progressively reduce tariffs and other barriers to trade between countries, with an ideal end objective of “free” and fair, frictionless trade worldwide. The Internet is by nature friction- and barrier-free – it makes any company that uses it a global business from the moment it takes itself online. That remarkable facility is at the heart of why research has repeatedly found that for each 10% increase in broadband penetration, GDP rises by between 0.25% and 1.38% (ITU, 2012: 17).

You will notice considerable variability in these statistics; that’s because measuring the digital economy holistically is famously difficult. Perhaps the best approach from an economist’s perspective is that of the OECD (2013: 7), which divides the Gordian knot into three elements:

1. The “direct impact”: the value added generated by Internet-related activities
2. The “dynamic impact”: net GDP growth generated by all activities related to Internet-related activities
3. The “indirect impact”: consumer surplus and welfare gains generated by Internet-related activities.

Rather than presenting an economic theory view of the networked economy, this chapter will relate it to how networks are actually structured and explain how world trade rules relate to that “real world” paradigm. This presentation also corresponds more closely to the way trade rules are structured. It is hoped that this combination will aid both trade policy practitioners and those more familiar with the Internet in forging a common understanding.

Finally, aside from everything else, the networked economy is important for all countries, not just for a few; moreover, it is at the heart of economic activity. Despite that fact, countries are increasingly implementing measures that add friction in online trade – this chapter will explore several. Understanding these measures is a key and pressing challenge for trade policymakers.⁴ The chapter ends with some ideas of policy options that can help trade and non-trade specialists understand the subject better whilst exploring what additional trade rules may add value.

The Network and the Data It Carries: Two Different Things

To understand the Internet in a trade context is a challenge for many policymakers. This is partly because they are confronting a subject area that is new to them, but also because those who advocate for networked economy provisions in trade often don’t explain the fundamentals so that policymakers can relate the unfamiliar to the existing “bricks and mortar” trading system they know.

4 There have been many efforts to quantify the elements that prepare a country to take maximum advantage of networked technologies for economic benefit; perhaps one of the more interesting is the Digital Evolution Index developed by the Fletcher School at Tufts University, with participation by many private- and public-sector stakeholders (see <http://insights.mastercard.com/digitalevolution/>).

The starting place is that the Internet from a trade perspective is really two different things:

1. The network that makes communications between any connected devices possible (in this chapter, the “network as a platform”)
2. The data and associated services that use that network as a communications platform (or “everything else”).

Where to draw the line between them is crucial, so let’s use the “digital holiday” scenario to illustrate that boundary.

Let’s say every person who uses the Internet took a “digital holiday” on the same day, and every single online application service provider (search engines, video services, email providers, etc.) did the same thing. The network itself would still continue exchanging addresses and related information. The next morning when people go online, everything would work as normal.

The data that the network carries, then, are the applications and services that people use and the data that those applications and services create. The network is the hardware, interconnections and essential communications between them.⁵

The Network

The network is an interrelated web of hardware and software that utilize common standards to ensure each component is interchangeable with others performing the same function. This concept – referred to as “interoperability”⁶ by technical stakeholders – is important because it allows maximum flexibility in designing networks and related systems. It is a close functional cousin to the concept of technology neutrality that is so fundamental to trade agreements.

The grouping of standards that make communications interconnection in the network possible are known as the “Internet protocol (IP) stack.” IP-based networks are designed to operate with maximum efficiency, and a continuous process of evolution of these standards responds to the need for greater performance, interoperability, resilience, trust and security over time.

What we call the public Internet is actually a “network of networks,” the large majority of them privately owned and managed by corporations, whether for

5 For the technically minded, the network as a platform corresponds to the lowest four layers of the OSI model and the lowest three of the TCP/IP (RFC 1122) model.

6 For a user-friendly overview of the Internet and the “network of networks” that it is comprised of, the Internet Society’s “An Introduction to Internet Interconnection Concepts and Actors” (Internet Society, 2012) is recommended (see www.Internetsociety.org/sites/default/files/bp-interconnection.pdf).

the use of their employees or, in the case of Internet service providers (ISPs), for the public to connect to the rest of the Internet.

Keeping things simple, there are three types of entity that collectively make basic connectivity, and therefore the public Internet, possible:

- Internet service providers (ISPs): entities that provide connectivity for end-users (ranging from single mobile devices to the largest corporations), of which most countries have from several to dozens
- Backbone providers: entities that connect ISPs to one another but that do not have end-users as customers; these entities are often responsible for making connections between countries and continents possible
- The processes and institutions that manage allocation of unique identifiers, such as IP addressing and the domain name system (DNS). These are analogous to telephone numbers or postal addresses in that they allow any “node” (of which your mobile phone is one, and your desktop PC or laptop is another) of the network to be identified and reached from any other node, and ensure that worldwide every single address is used only once.

Each ISP or backbone provider must do two things aside from connecting to its customers:

- Connect to other ISPs so the exchange of data between their respective customers is possible, and connect to backbone providers (either directly or indirectly) to allow international traffic exchange. Without these agreements (often known as “peering” or “interconnection” agreements), the Internet would cease to be a global platform and exist solely as ISP-specific “islands” that would only allow users to connect to the other customers of their own ISP.
- Acquire the various types of technical addresses necessary for its equipment and that of its customers to use to connect to others, and implement the related services (like DNS servers) that allow every single device on the public Internet to have a unique address and to allow its customers to be found and to find all others.

The result of all this is that these networks (if left to themselves and the web of stakeholders who operate and maintain them) can:

- **Automatically find the optimal (which is not necessarily the most direct) route between any two points at any given time.**⁷ An important fact to remember is that the route between any two points may traverse third countries, and that route may pass through different third countries at different times of the same day. This is especially common in border areas where two countries have dense populations in close proximity to a shared border.
- **Create a communications connection between any two points in a way that optimizes performance in the networks through which that communication passes.** This can result in a route being taken that is *geographically* complex to ensure the communication “performs” better.
- **Ensure that anyone may extend the public Internet** simply by connecting a device called a router⁸ to the “edge” of the network and applying for a unique address for that router. Acquiring that address is often automatic, though public Internet addresses are ultimately assigned by regional Internet registries (RIRs)⁹ to ensure every single device on the public Internet has a unique address.

As you can see from these characteristics, the public Internet as a platform is inherently blind to geography in a way that the “offline” world is not. Goods trade, for example, would generally be biased against shipping via third countries to deliver a package sent from, and bound for, destinations in the same country to avoid the potential “friction” of border measures such as customs, tax compliance and other formalities.

7 Throughout this chapter illustrations refer to connections between two points (“point to point”), in order to make key points easy to follow. There certainly are communications where a single origin is connecting to multiple endpoints simultaneously and each of these endpoints may be in different countries from one another.

8 A router is a device that “talks” to other such devices to figure out how to forward requests from any device connected to it to any other part of the network. The standards used ensure that this can happen automatically, and as the network topology changes in real time these changes are “learnt” by those devices that need to know about them. Pretty much every business and residence has a router, in the latter case generally provided by the Internet service provider.

9 These organisations are responsible for managing the key forms of addressing on the Internet, which are akin to the various types of addresses in the worldwide postal system in the functions they perform. All of them are ultimately linked to the Internet Assigned Numbers Authority (IANA), managed by the Internet Corporation for Assigned Names and Numbers (ICANN). IANA and the RIRs work together (more information is available at <http://www.iana.org/numbers>).

The Objectives of Trade Agreements Related to the Network as a Platform

Looking at the network as a platform suggests several policy objectives to pursue in trade agreements:

- **Avoid actions that impede or distort basic functions such as addressing and traffic routing.** Where a country needs to prevent some communication from taking place, or prevent access to certain information that the network carries for whatever reason (such as to block child pornography), it must do so in a way that does not affect the operation of the network that carries those communications.
- **Avoid actions that might impact upon “transit traffic.”** As we have seen, traffic often – for very good reasons – transits a country for which it is neither the destination nor the source. This argues strongly for such transit traffic to remain untouched and unhindered – after all, failing to respect transit traffic of others could lead to reciprocal lack of respect for your own.
- **Avoid obligations that distort private-sector choices about how equipment or services integral to the functioning of the network as a platform are made.** Measures of this type – often called “local hosting” obligations – can refer to elements of the network as a platform (like submarine cables, routers or related equipment), but they are most often intended to influence where applications, data and related services are hosted. Obligations that distort investment choices that would otherwise seek to optimize performance and resilience in the network everyone uses as a platform should be avoided as a clearly trade-distorting measure. An example from the offline world is roads: we want roads to be well maintained and with enough lanes to handle peak traffic, and ideally to have multiple connections between locations so that when traffic congestion affects one road we have alternative routes to take.

How Existing Trade Agreements Relate to the Network as a Platform

Thanks to the principle of technology neutrality in trade agreements like the General Agreement on Trade in Services (GATS), the network as a platform has been subject to extensive coverage in WTO Members’ commitments as basic telecommunications services for decades. International commitments in this area are anchored to the WTO Agreement on Basic Telecommunications Services.¹⁰ Part of the problem is that this agreement is an annex of GATS,

10 https://www.wto.org/english/tratop_c/serv_c/12-tel_c.htm.

and GATS is a “positive list”¹¹ agreement – meaning that the only obligations countries have are those they specifically commit to.¹²

There are 108 WTO Member countries with commitments in telecommunications, though the commitments are worded differently¹³ so the only way to determine what common commitments there are is through laborious searching and comparing all of the commonalities. What the Internet really needs is not a “positive list” approach to commitments but the opposite – a “negative list” approach coupled with the political will to agree upon robust framing of the obligations themselves.

The concepts in the WTO Agreement though are sound and have been taken forward by bilateral and regional free trade agreements in the intervening decades,¹⁴ the most comprehensive treatment being that of the Trans Pacific Partnership finalized in 2015.¹⁵

Data Flows (or “Everything Else”)

When the term “data flows” or the “free flow of data” is referenced in a trade context, what is meant is the exchange of any and all information in electronic form unrelated to maintenance of the network connectivity that makes those data exchanges possible.¹⁶

Data flows, not surprisingly, are where everything becomes complicated as data can and do relate to any activity that can be conducted electronically at distance.

In order to understand the flow of data, one must start by understanding two key facts about the fundamentals of IP-based networks:

- Each and **every communication is broken into little pieces called “packets” and sent to its destination independently**, and then reassembled on reception; if (and this often happens) a packet goes “missing” along the way, the receiver asks the sender to send it again

11 For those unfamiliar with some of the trade terms used in this chapter a good glossary, provided by the Organization of American States’ SICE project, may be found at http://www.sice.oas.org/dictionary/SV_e.asp.

12 A layman-friendly description of the flavor of existing commitments may be found at https://www.wto.org/english/tratop_e/serv_e/telecom_e/telecom_highlights_commit_exempt_e.htm#country.

13 Commitments may be found by searching the WTO’s ‘i-Tip’ database at <http://i-tip.wto.org/>.

14 For a good history of GATS and international services negotiations at the WTO and in regional trade agreements see Adlung and Mamdoh (2013).

15 For the relevant provisions, see Chapter 13 of the Trans-Pacific Partnership (*inter alia*, Articles 13.4.3 and 13.4.5.6) at <https://ustr.gov/sites/default/files/TPP-Final-Text-Telecommunications.pdf>.

16 Again for the technical, this essentially corresponds to the application layers of both the OSI and TCP/IP models.

- The result of this “packetizing” of data is that **only the sender and receiver of any online communication know what is being communicated.**¹⁷

These two facts are critical, as they show that data flows operate opposite to offline trade: offline transactions require a package bound for international destinations to clearly indicate what it contains and can be opened to verify that the contents are as stated. The Internet is the opposite and cannot fundamentally change; there are simply too many hundreds of billions of communications taking place simultaneously 24x7 to make the contents transparent. That would not only require a complete redesign of the network, it would create such overhead throughout the transmission path of every communication as to render the network either unusable or unaffordable, or both.

Keeping this in mind, there are ways to break the monolith of ‘data flows’ down in a rules-based trading context and below is a résumé of the principles that should apply:

1. The principle of technology neutrality of trade agreements means that **any online activity should be treated the same as its offline equivalent.** This principle actually provides substantial coverage today as regards many economically significant activities online, from the purchase of goods of every variety via online storefronts to services of many kinds. The data associated with these activities are therefore covered to the same extent as the activity that produces them, as they are integral to covered activities.
2. It naturally follows from the first principle that wholly **Internet-based services should receive the benefit of national treatment and market access commitments related to their offline equivalents.** In practical application this has been disputed, or simply disregarded, when it is inconvenient for WTO Members in certain circumstances. For example, countries have alleged foreign search services to be purveyors of pornography even where domestic equivalent services allow users to legally link to similar adult content (Elegant, 2009). Numerous other foreign Internet-based services, including social networks, blogging and photo sharing sites, have over time been blocked for varying lengths of time or severely restricted by government action while domestic versions

¹⁷ This is a slight simplification – it is possible to “inspect” packets to divine information about what each contains to a certain degree, but doing this is technically burdensome and necessarily imperfect, and where a communication is encrypted (as an increasing number of communications are) inspection is rendered useless.

of the same services are permitted to operate.¹⁸ There is also very little transparency about what material is removed from online services, when, for what purpose and at whose instruction. Even where companies would like to release details of these requests, they are routinely legally prevented from so doing. Companies have increasingly begun unilaterally publishing information about this.¹⁹ In the trade context, voluntary measures that must accommodate unharmonized, nationally specific legal restrictions on disclosure do not produce the certainty or transparency that a rules-based international regime can.

3. As a corollary to national treatment, competing **equivalent lawful economic activities online should be treated the same by the network wherever any part of an economic transaction is in another country**. In national and regional debates this is often referred to as “network neutrality” and is hotly debated. Net neutrality is discussed in more detail below.
4. Any **data not bound for, or coming from, the territory it is passing through shall not be subject to any impediment**. This is a corollary to the rule on the network as a platform and for the same reasons.

Existing Protection of Data Flows

The level and scope of existing coverage of data flows *per se* is a subject of considerable debate.

At least 60 countries have undertaken commitments on “data processing” and 76 “on-line information and/or data processing” (Berry and Reisman, 2012) under the WTO agreements. Given the latitude that countries have in the wording of their commitments, of course there is considerable variation. More definitively, a moratorium on customs duties on “electronic transmissions” covers all WTO Members and while it is not permanent, it is renewed at each WTO Ministerial.

With respect to services themselves, where there is little functional difference between their online and offline versions the extensive market access and national treatment obligations should apply. Again, the wording of commitments may be read in different ways depending upon the interests of

18 The OpenNet Initiative compiles information on the types of blocking, monitoring, and filtering that countries engage in (see <http://map.opennet.net/>). A layman-friendly explanation of the different types of interference that exist is at <https://opennet.net/about-filtering>.

19 Transparency reporting has greatly increased globally in the wake of the Snowden disclosures; the Global Network Initiative is an example of an Internet industry initiative to promote disclosure of such requests (see <http://www.globalnetworkinitiative.org/>).

the reader – or more to the point, the country the reader represents if he or she is a trade negotiator.

Many books have been written about the extent to which existing CPC classifications cover the digital equivalents of offline activities and the problems associated with the trading system’s dependence upon classifications last revised in 1991.²⁰ Because commitments often refer to these classifications, given their generality it can make commitments even more subject to interpretation.

This does argue for straightforward commitments on data flows as a policy object and the Trans-Pacific Partnership (TPP) is the most substantive step in this direction of any trade agreement.²¹

ICT Hardware: The Common Thread

While it is the main purpose of this chapter to explore the networked economy as a wider phenomenon rather than its specific impacts on the ICT sector, it is important to highlight that the Internet exists in physical form not just as cabling and wireless signals, but also in the physical ICT hardware that makes interconnection in the network as a platform possible. The data that platform carries are generated by people using the multitude of network enabled devices, from cloud services’ server farms to your smartphone.

Goods trade in these forms of ICT-related hardware is economically significant – reaching US\$4 trillion in 2014. One of the crown jewels of the WTO System relates to ICT hardware like this – the Information Technology Agreement (ITA) was concluded as a plurilateral agreement in 1996 that removed all tariffs on the products the agreement covers.

The rapid advance of technology increasingly made revision of the agreement a priority (as the original agreement covered only items specifically listed, rather than product families), and this was finally agreed in December 2015 at the 10th Nairobi WTO Ministerial. It is at least arguable that the ITA is the greatest achievement of the WTO in normative terms after the WTO agreements themselves, and it is understood to be profoundly beneficial to developed and developing countries alike.²² It is estimated that the expansion

20 The “current” classification list for services trade is online at https://www.wto.org/english/tratop_e/serv_e/mtn_gns_w_120_e.doc.

21 See the Electronic Commerce Chapter of the Trans-Pacific Partnership (*inter alia* Article 14.11) at <https://ustr.gov/sites/default/files/TPP-Final-Text-Electronic-Commerce.pdf>.

22 There are many studies of the application of the ITA to developing countries, but a particularly good one is Ezell (2012).

alone may add \$1 trillion in annual global trade benefits in covered goods and increase global GDP by \$190 billion.²³

Digital Issues and their Trade Dimensions

It has always been the case that public policy issues that arise in a non-trade context can have profound trade implications, and the networked economy is not exempt from this reality. Here are several of the most topical.

Network Neutrality

“Network neutrality” has been debated for a decade in a few advanced economies, but is now being discussed by regulators in many countries as the Internet’s impact spreads.

The debate about net neutrality is a struggle that is both economic and political and has enormous consequences in three respects:

- Who gets to decide how the value generated by product and service providers is apportioned – application providers themselves, or ISPs?
- How much control should each part of the value chain of digital commerce have over the public Internet in each country?
- Who controls the power position of each part of that chain – shareholders and markets, or regulators?

Boiled down to the essentials – there are considerable nuances, especially in markets where competition between ISPs is impaired – the main question is this:

- **If network neutrality is obligatory**, then ISPs must treat all applications or services the same as any other that is functionally similar. In other words, YouTube could not pay ISPs in order to make it perform better for the user than a startup video service.
- **If network neutrality is not obligatory**, then ISPs can charge service and application providers fees to prioritize paying services over their competitors.

An additional dimension to this question relates to peering and whether these agreements are entirely private or regulated by the same kinds of rules.

²³ See, *inter alia*, United States Trade Representative, *Supporting Economic Growth at Home and Abroad by Eliminating Trade Barriers on Information Technology Products*, July 2015, at <https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2014/November/Supporting-Economic-Growth-Home-Abroad-Eliminating-Trade-Barriers-on-IT-Products>.

The trade policy community has yet to engage with this discussion much. Aside from the European Union (where a Regulation for the Union as a whole was finalized in 2015 but with important definitional elements left to the member states), net neutrality debates have focused on how they will apply within countries.

These national debates miss the impacts these decisions have on the Internet as a globalized trading platform. Since the private sector owns and controls the international links between countries, net neutrality rules that impact international peering arrangements could have profound impacts.

This is magnified by the fact that a few backbone providers handle the vast majority of international Internet traffic. Many of these so-called “Tier 1” (Zmijewski, 2014) providers are actively lobbying on network neutrality in key economies.²⁴

In addition, there’s also the reality that all countries are not created equal with respect to the flow of data. As a consequence, national decisions about net neutrality may well have consequences far beyond their borders.

Local Hosting Requirements

Local hosting obligations are widely discussed in the trade community, in part because they are easy to relate to offline trade. There are few measures more disruptive to the networked economy – that’s a broad statement, but justifiably so since we know that the largest beneficiary of the networked economy is traditional businesses.

We know that all commercial activity depends upon access to a wide variety of products and services available at competitive prices as inputs. If your competitor is allowed to choose the inputs he or she wants based solely upon price and suitability for the purpose at hand and you are not, you are at a disadvantage. This is just as true for inputs related to the Internet.

For example, let’s say you manufacture hats and sell them online as well as in shops. If you’re obliged to host all records of customers in your country on local servers, that will limit the services that you can choose to take credit cards for payment to those willing to follow your local data localization rules. If you are from a smaller or developing country and you have burdensome data localization requirements, the major online marketplaces may not make their service available to you or your countrymen. If that happens, you lose

24 With respect to lobbying spend in the United States on its net neutrality decision, three of the biggest backbone providers were active: Verizon and AT&T opposed, and Level3 was in favor (Furmas and Drutman, 2014). European-headquartered Tier 1 providers are active participants in the net neutrality debate at the European Union as well.

incredibly valuable opportunities for marketing and selling your goods to a global market of buyers.

One of the most authoritative studies of data localization (Bauer et al., 2014) found that the impact of rules being planned or implemented in several countries (Brazil, China, the European Union, India, Indonesia, Korea, and Vietnam) were expected to reduce GDP from 0.1% to 1.7% depending upon the country.

Given all this, you might ask: why are countries considering these rules in the first place? They are proposed to solve all manner of ills, from protecting access to nationals' personal information from foreign national security agencies, to providing greater protection of personal information in commerce, to creating jobs by incentivizing the development of more data hosting centers. Data localization is at best a poor instrument, and at worst entirely ineffective, in pursuit of these policy objectives. In the first two cases, the perception that geography has anything to do with data access is a holdover from the analogue world. In reality it is the measures taken to protect data, and not the location where they are stored that matters.²⁵ With respect to access by foreign powers' national security services, these organizations are not known for respecting borders and localizing data may simply make it easier for the country creating these obligations to surveil its own citizens. Finally, there are few jobs in data centers – even very large ones are automated and require only a literal handful to run, and those are largely lower-wage jobs to manage the physical security of the buildings.

In a trade context, presence requirements are generally specifically related to business presence (i.e. registration) and other “offline world” requirements. The most comprehensive local hosting provisions relating to the digital economy are to be found in the TPP – and they prevent TPP parties from creating these obligations:

“No Party shall require a covered person to use or locate computing facilities in that Party’s territory as a condition for conducting business in that territory.”²⁶

25 For those interested, the standard reference for best practices in securing information is the ISF's Standard of Good Practice for Information Security; more information is available at <https://www.securityforum.org/tool/the-standard-of-good-practice-for-information-security/>.

26 See the Electronic Commerce Chapter of the Trans-Pacific Partnership (Article 14.13.2) at <https://ustr.gov/sites/default/files/TPP-Final-Text-Electronic-Commerce.pdf> and the Telecommunications Services Chapter (*inter alia* Articles 13.4.3 and 13.4.5.6) at <https://ustr.gov/sites/default/files/TPP-Final-Text-Telecommunications.pdf>.

The Industrial Internet of Things

The industrial Internet of things (IIoT) is fascinating for many reasons, one being that it relates to solely machine-to-machine communications in manufacturing, agriculture and many other market segments. Since these are communications between machines about their activities, the IIoT is largely devoid of personal information of individuals.

As an example of the IIoT in application, imagine if every machine associated with a car factory were networked and reporting on everything that it does. This would allow operators to know when any aspect of manufacturing was deviating from design tolerances – or even if a specific part being installed in a specific car was damaged during the installation process or couldn’t be installed because it deviated from design tolerances. Clearly, this would greatly increase both the value of automation and also the quality of finished goods.

Major manufacturers have banded together to create standards for how devices and processes can interoperate with one another. A report by Accenture suggests that the GDP value that the industrial Internet may unlock is in the trillions of adjusted US dollars just for the G20 countries by 2020, and up to \$14 trillion by 2030 (Purdy and Davarzani, 2015).

There are of course profound trade dimensions to the industrial Internet, such as:

- How can trade policy ensure that standards impacting such massive economic effects remain open and not subject to capture by a few powerful multinationals? The Technical Barriers to Trade (TBT) process has been successful in ensuring that standards are not used in trade-distorting ways, but will evolutions of that process be necessary to deal with the transformative impact of IIoT standards?
- How will SMEs that are part of global value chains be impacted by, for example, the much lower tolerance to deviation from design specifications that IIoT manufacturing and assembly processes will likely require of them?

Data Protection and Privacy

Trade agreements provide for exceptions so that signatories may deviate from normal treaty obligations in order to deal with key policy priorities.²⁷ The general exceptions of GATS are the de facto standard by which data protection and privacy are handled in trade agreements – directly and by transposition into bilateral and regional trade agreements. That said, the increasing political importance of data protection in key economies is straining continued reliance on exceptions-based privacy regimes. At a practical level, measures related to personal information are a key consideration since we know that data online routinely crosses borders. The simple act of tracking visits to a website²⁸ can reveal who that visitor is, at least to the level of an IP address.²⁹ This differs from the offline world where the commercial use of personal information across borders is less routine and often far less detailed.³⁰

It is also the case that measures taken to protect national security in the online environment can create barriers to efficient network operation and introduce legal uncertainty that is damaging to commerce.³¹ An early example of this from the “pre-Snowden” period is the US Patriot Act.³² Provisions of this act have resulted in reluctance by other countries to allow storage of their nationals’ data in the United States.³³ The Snowden disclosures greatly aggravated this situation to the point where several heads of state announced national plans to build submarine links to other continents specifically to avoid their traffic entering the United States’ territory.³⁴ More recently, the US government is pursuing Microsoft in US courts to force it to hand over personal data of a non-US-based customer that are held in Ireland simply because Microsoft is headquartered in the United States. This despite the fact that should the government prevail, it will instantly make all US-headquartered technology firms lose competitiveness to the tune of billions in annual revenue

27 Contained in Article XIV and available at https://www.wto.org/english/docs_e/legal_e/26-gats_01_e.htm#articleXIV

28 Website usage tracking tools (“web analytics”) are used by many, if not most, public websites as, amongst other uses, they help web designers understand how sites are used and when.

29 As an example of how fundamental the differences are in what constitutes “personally identifying information” (PII), IP addresses are considered PII in some countries but not in others.

30 While the volume of literature on the subject is considerable, for those in the trade community we recommend the February 2013 WEF report “Unlocking the Value of Personal Data: From Collection to Usage” available at <http://www.weforum.org/issues/rethinking-personal-data> (WEF, 2013).

31 Cloud services are particularly susceptible to this; for an example of the harms, see “Dutch government to ban U.S. providers over Patriot Act concerns,” Zdnet, September 19th, 2011 (at <http://www.zdnet.com/blog/btl/dutch-government-to-ban-u-s-providers-over-patriot-act-concerns/58342>). This decision was subsequently reversed.

32 An accessible summary of the Act and subsequent amendments may be found at Wikipedia at http://en.wikipedia.org/wiki/Section_summary_of_the_Patriot_Act_Title_II.

33 Perhaps the most well-known being Canada (Clement and Obar, 2013).

34 Just one of the many examples is Brazil and the European Union (Emmott, 2014).

and undermine international law.³⁵ The case is of such significance that the European Union itself has filed an amicus brief asking the US government to drop it. Microsoft has taken the extraordinary step of designing a cloud service offering through Deutsche Telecom that both companies believe will withstand any attempt by US authorities to force Microsoft to hand over data held in those data centers – despite Microsoft being a US-headquartered company (Ribeiro, 2015).

The US is far from alone – China is promulgating rules that would create obligations on foreign businesses related to personal information that have very clear trade impacts, arguing that to do otherwise risks Chinese nationals’ exposure to foreign secret services and privacy violations by foreign companies (McDougall, 2015).

The debate about privacy and trade generally focuses heavily on business-to-consumer (B2C) services, as by their nature these generate and use large amounts of personal information. Since we know that these services are only a small fraction of the total economic value proposition even of networked economy services, it is easy to argue that the debate we are having is deeply unbalanced. This is not to suggest that data privacy is not important – put simply, people count – but having a debate almost exclusively focused on that isn’t balanced or sensible.

The imminent widespread advent of the “Internet of things” (IoT), where devices as mundane as refrigerators and home fire alarms are connected to the Internet, will further complicate such concerns; there are additional issues with respect to product safety.³⁶

These issues will continue to trouble trade negotiators, partly because they’re complex but also because many countries are in the throes of national debates about interrelated questions that impact the networked economy, such as:

- What is the balance between the privacy of individuals in the networked environment and the commercial or government use of information about them?
- How does each country ensure that key information needed for regulators – such as that related to financial transactions and institutions – is protected and remains accessible to them when it leaves national boundaries?
- How can we create rules to protect users against online fraud and abuse and use of public networks for criminal activity without undue consequences to fundamental freedoms – or commercial activity?

35 For an accessible resume of the case, see Endler (2014).

36 A good overview for the non-specialist may be found in Wiesman (2015).

- Where is the dividing line between national security issues and everyday commercial and end-user security?

Ideas for Future Work

It is certainly true that the WTO's normative processes are currently under stress, as discussed in the Introduction to this book. That said, there are many things that WTO Members can do, short of negotiations related to the networked economy, which would help them collectively understand the state of their current economic dependence upon it and the competitive advantages (and disadvantages) they have. In order to have a successful negotiation, you need negotiators with sufficient knowledge of the subject matter to be confident of the choices they make as well as a shared base of understanding of the objects they're discussing.

Given that the capital of the trade community is Geneva, the WTO community is a good forum to begin discussing issues in a low-risk way and the flexibility in the Electronic Commerce Work Programme means that any country can propose relevant discussions and make contributions – and if the Membership as a whole doesn't choose to take them up, those who are willing can always do that in smaller groups. After all, that's how the Trade in Services Agreement (TISA) negotiations on services began.

Better Understanding of How ICT Services Act as a Multiplier, or Facilitator, of the Traditional Economy

Below are just a few areas where WTO Members could ask the Geneva-based institutions with trade or statistical gathering activities to collaborate on reporting or symposia organization or both.

- **There's a great deal we don't know about how traditional services leverage the digital environment to compete, innovate and export, and the role ICT services play in making this happen.** To illustrate the stakes, European services overall account for 73% of the Eurozone economy (ECB, 2011),³⁷ while those related to ICT-specific services represent just over 3%. In a trading context understanding these interrelationships is not optional, it's essential – for both developed and developing countries.

37 Also see the online statistical interrogation tool at <https://www.ecb.europa.eu/mopo/caec/html/index.en.html>.

- **Understanding how traditional non-services industries leverage the digital economy to compete and the trade rules that apply is another key subject that needs more research.** Just one aspect of this is how after-market services that leverage networked technologies impact the competitiveness of manufactured goods. An example of this is Volvo, the world’s largest manufacturer of commercial diesel engines. Volvo offers a 100% uptime guarantee for their commercial vehicles made possible by networking technology reporting when parts need servicing before they fail.³⁸ What trade rules apply in these circumstances – and what barriers too – and how can developing economies compete in the value chain of products like these?
- **Analyzing the extent of trade-related data flows and what they consist of.** If digitally connected commerce between businesses is ten times that between businesses and consumers, it is logical that much of that data flowing across borders does not consist of personal information. You would think that this a question about which we have a lot of information, but sadly the opposite is true. Remedying this deficiency will require a concerted effort across public and private organizations, as much of the base data needed for analysis are in private-sector hands.

Improving the quality of Statistical Information on Networked Economy Transactions

Measuring the economic impact of the networked economy, as well as ICTs more generally, is notoriously difficult.³⁹ It is equally true that acquiring better data is widely accepted as desirable and necessary – and the trade community should be at the forefront of that effort given the trade impacts of these technologies. As a first step, the WTO ought to convene the various public sector institutions – from UN agencies to multilateral and regional development banks – to see what data are being gathered and where they are; this would also help make clear what we need and do not yet collect. **WTO Members should ask them to do this and encourage the other institutions to help.** The UN has acknowledged that better information about the impact of technology is a priority⁴⁰ and the process

38 See http://www.volvotrucks.com/trucks/uk-market/en-gb/parts_service/Genuine-Volvo-Service/service-contracts/volvo-gold-contract/Pages/gold-contract.aspx.

39 For an excellent tour d’horizon of the issues with measurement accessible to non-specialists see OECD (2013).

40 There are many examples, but the most significant is to be found in the Addis Ababa Action Agenda for financing of the Sustainable Development Goals, where an entire chapter is dedicated to measures on how data and data analysis are integral to the achievement of the SDGs (see the “Addis Ababa Action Agenda of the Third International Conference on Financing for Development” (Addis Ababa Action Agenda), adopted by the United Nations General Assembly on July 27th, 2015, (A/RES/69/313, Section III, page 35, at http://www.un.org/en/ga/search/view_doc.asp?symbol=A/RES/69/313).

of defining the indicators that will be used to evaluate whether or not the Sustainable Development Goals are in fact being met are in the process of development. It is important that the trade dimension of technology's impacts are a part of these indicators to ensure that the link between development and the economic impact of technology on development are better understood. The trade community should take a leading role in ensuring that both these processes are informed by the community's needs – doing so will pay dividends for decades to come.

Data Protection and Privacy in International Trade

Data protection and privacy issues are already a thorny subject in trade negotiations – the recently concluded Trans-Pacific Partnership talks are evidence of this.⁴¹ The reality is that the global nature of data flows in the networked economy raises issues that will be the subject of debate at the national level for some time, and laws made nationally in response will continue to evolve. Trade negotiators will be wary of agreeing to binding international obligations where national discussions are not mature.

A first step would be for **a group of interested WTO Members to convene a few meetings of their data protection and trade officials to compare notes on how different countries' legal systems handle personally identifying information.** That conversation could also **ask experts to consider how interoperable (or otherwise) different approaches are in a trading context.**

An informal discussion like this regularly in Geneva would allow these charged issues to be discussed outside of negotiations but still involve negotiators – removing political risk from an already fraught subject. It is hoped that over time, meetings could at least periodically include other stakeholders to build understanding. The provisions of the TPP on privacy already call for its parties to engage in a dialogue like that suggested above,⁴² but why stop with TPP parties? Such a conversation amongst the combined TPP and TISA parties would seem sensible, as the two agreements have substantial overlap in participating countries and it is reasonable to suggest that the ultimate TISA agreement will have congruent, if not very similar, provisions in this area.

⁴¹ There are literally thousands of articles discussing different views on this subject.

⁴² See the Electronic Commerce Chapter of the Trans-Pacific Partnership (inter alia Articles 14.15 and 14.8.5) at <https://ustr.gov/sites/default/files/TPP-Final-Text-Electronic-Commerce.pdf>.

Creating Greater Certainty for the Network as a Platform

While it is true that issues with data and their use in sectoral trade applications can rapidly become very complex, that should not be true with the network as a platform.

A group of WTO Members could make unilateral MFN commitments to some of the principles articulated above without any “free riding” problem. A commitment that traffic that is only transiting a Member’s territory would not be subject to interruption or delay would make a political and practically important statement without a downside, since it is not practical to know what the contents of transit traffic is in any case.⁴³

Second, **a group of WTO Members could commit to making the moratorium on customs duties on electronic transmissions permanent on an MFN basis.** This is now in enough bilateral and regional agreements⁴⁴ that, for many countries, it would be difficult to derogate from in any case – and it would send a very strong signal, especially if the group were large enough and cross-regional.

Creating Better Clarity on the Existing Commitments for Both the Platform and the Data that It Carries

There are existing commitments across a large proportion of WTO Members on key aspects of the networked economy, but no authoritative comparison of how different commitments interoperate with one another. Surfacing this information in a neutral way that simply compares how commitments are worded and how congruent those are with others is essential information. The meaning would then be argued by some, but at least the argument would be taking place based upon a reasonable foundation. **A group of WTO Members should jointly ask the WTO Secretariat for such a report** – if the sensitivity were seen to be too great for this to be published as an official WTO Secretariat product, it could be commissioned as part of the WTO Working Papers series.⁴⁵

43 For textual inspiration, see the Telecommunications Chapter of the Trans-Pacific Partnership (Articles 13.4.3 and 13.4.6.5) at <https://ustr.gov/sites/default/files/TPP-Final-Text-Telecommunications.pdf>.

44 Including all TPP Parties; see the Electronic Commerce Chapter of the Trans-Pacific Partnership (inter alia Articles 14.15 and 14.8.5) at <https://ustr.gov/sites/default/files/TPP-Final-Text-Electronic-Commerce.pdf>.

45 WTO Working Papers that presently exist are to be found at https://www.wto.org/english/res_e/reser_e/wpaps_e.htm.

Exploring Issues like Network Neutrality in a Global Trading Context

As outlined above, the debate about network neutrality being confined to national (or inter-regional) dynamics is far from optimal. **A dialogue between trade officials, backbone operators and ISPs, and other stakeholders in Geneva to explore the international dimensions would be valuable.** It would expose very different views on the subject, but it would also help create a shared understanding of the impacts of different policy choices that are being made. It would also help expose any analysis that is needed to better understand the market landscape. These conversations could (and should) be held at least partly in public, and other Geneva-based institutions stakeholders invited to participate, given that the impacts of these choices have profound implications beyond trade.

Discussing, and Creating, a Disclosure Process for Digital Information Blocking, Filtering and Removals

While undoubtedly controversial, countries are increasingly blocking and filtering content and monitoring what their citizens do online. These activities have an inherent risk – and in some cases the certainty – of trade-distorting effects. **A disclosure process that would ensure a basic minimum of information on when content online may be blocked by a Member would be of great benefit.** The WTO notifications process in other areas of trade law has been very successful and future agreements that incorporate digital issues should build upon this legacy.

The starting place is a conversation amongst willing WTO Members to compare experiences and practices. Far more studies on the economic impacts of measures for blocking connectivity or reducing access to online resources are needed to complement the many that exist on how such measures can impact on freedom of expression.

In Conclusion

The networked economy presently only connects about half of humanity. We are only at the beginning of its transformation of society and our economies. Its inherent nature is frictionless by design to an extent that the “bricks and mortar” trade community can only dream of for the traditional economy.

If for no other reason than that it is long past time for the international trade community to make a priority of better understanding it as an economic

force. That will require leadership from WTO Members to bootstrap the conversation but, as the TISA talks and large regional trade agreements have begun to show, it can be done. All countries need this conversation, as trade agreements will inevitably incorporate more and more provisions related to the networked economy. Trade negotiators of all countries – including those from developed countries – will need to understand its impacts and opportunities better to negotiate the future agreements that will bind them.

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The world economy is going through major economic and geopolitical shifts, fostering tensions in the global economic governance structure centered on the IMF, the World Bank and the WTO. The impacts of globalization are being questioned while disruptive technologies continue to change the economic landscape. This collection of papers focuses on one of the pillars of global governance: the multilateral trade system, anchored by the WTO.

Membership of the WTO is now close to universal, with the accession of China in 2001 representing a landmark achievement. While the organization plays a major role in enhancing the transparency of trade policies and enforcing the rules of the game that have been agreed by Members, it has not been successful at negotiating new rules. The private sector is frustrated with the WTO, as are civil society groups seeking to address issues of interest to them. There is a general perception that WTO disciplines and modus operandi are outdated and have not kept pace with globalization. Governments have increasingly turned to preferential trade agreements (PTAs) that are better attuned to the changing dynamics of international trade and investment flows.

The papers in this volume focus on some of the major critical issues that confront the WTO Membership. They review developments in trade policy and technology and regulation. They make clear that PTAs are at best a partial solution to the global governance gap. Regulation of the “Internet of things,” e-commerce, cross-border services, digital trade and data flows will become ever more important. Global rules of the game are required. The same is true for old fashioned protectionism. The future of the WTO is an important topic for the health and expansion of global trade in the 21st century.

ISBN: 978-92-9084-410-5

doi:10.2870/560499

Catalogue number: QM-01-16-444-EN-N

European University Institute (EUI)

Badia Fiesolana, Via dei Roccettini 9,
I-50014 San Domenico di Fiesole (FI), Italy
www.eui.eu