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## Open Plurilateral Agreements, Global Spillovers and the Multilateral Trading System

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National policies can give rise to negative cross-border spillovers. Addressing cross-border policy spillovers requires identifying those that are systemically significant and international cooperating to attenuate negative effects. Insofar as the policies impact on trade, in principle this is the task of the WTO, the international apex forum for cooperation on trade policy and the negotiation and implementation of multilaterally agreed rules. The WTO has been unable to fulfill this role, reflecting differences in priorities across the membership, an erosion in trust, and deep-seated working practices that have impeded efforts to revise and update the rulebook. The result has been that since 1995 most new rulemaking has been through preferential trade agreements (PTAs), not the WTO.

There is growing recognition that reforms are needed to improve the functioning of the WTO, including a willingness to pursue agreements pertaining to only a subset of WTO members but that are open to all WTO members and where benefits in principle extend to all countries on a nondiscriminatory basis. Open plurilateral agreements (OPAs) on specific policy areas or sectors of economic activity can complement discriminatory, closed PTAs, in the process supporting the multilateral trading system.

Contrary to arguments that plurilateral initiatives are second best in a world where consensus is not obtainable, OPAs can be a first-best response. Cooperation aimed at identifying good regulatory practice and processes to determine whether different regulatory regimes are

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<sup>1</sup> This is a short summary of a paper by the same authors. The full paper is available here: <https://www.bertelsmann-stiftung.de/de/publikationen/publikation/did/open-plurilateral-agreements-global-spillovers-and-the-multilateral-trading-system>

equivalent does not require all WTO members to participate. Nor does it call for the package deals that characterize trade negotiations.

PTAs are inherently limited in their country coverage and are discriminatory by design – liberalization only applies among signatories. One consequence is that PTAs do relatively little to address global policy spillovers. Trade agreements are designed to address a specific problem: reducing the aggregate welfare cost associated with national trade-restricting measures. If countries are large (enough) such policies impose negative externalities on trading partners. Often such policies are also costly to the countries imposing them. They will reduce aggregate real income if countries are small (cannot affect their terms of trade). Efforts by large(r) countries to shift the terms of trade in their favor may have the same result if other countries in turn impose barriers on imports.

This terms-of-trade prisoner's dilemma rationale for trade cooperation is complemented by a corollary role that trade agreements can play. The structure of trade policy in a nation is determined by political economy forces. Trade agreements permit governments to "mutually disarm" by changing the domestic political equilibrium that underpins the use of welfare-reducing restrictive trade policies. They do so by offering exporters better access to partner markets, creating incentives for exporters to provide domestic political support for liberalization. Moreover, because trade agreements are self-enforcing, they can help governments make credible commitments to sustain liberalization over time.

These two conventional rationales for trade agreements ignore an increasingly important motivation for international cooperation. Changes in the structure and consequences of economic activity call for domestic regulatory measures to address associated market failures.

Governments confront significant uncertainty how best to design such regulation to attain underlying objectives. Moreover, differences in regulatory regimes for a sector, product or activity give rise to transactions costs for firms operating internationally. Experience with WTO negotiations and the Paris Agreement make clear that common approaches reflected in binding multilateral agreements are unlikely to be feasible given the difficulty of attaining

consensus. Instead, workable global solutions are more likely to emerge through encouragement of plurilateral initiatives (clubs) and efforts to ensure that over time these become the basis of a revamped rules-based multilateral trade regime.

OPAs among groups of countries are more appropriate instruments to address international collective action problems and the trade costs of regulatory heterogeneity because the problems are more complex than the "terms-of-trade"-cum-commitment problems trade agreements are appropriate for. Problems involving regulatory design and cooperation to respond to climate change, the rise of the digital economy and managing high-tech industrial policy conflicts call for cooperation to identify good practice and balancing the achievement of noneconomic objectives against competitive spillovers.

OPAs can help parties understand and learn about the effectiveness of alternative policy options and their effects on trade, and to identify approaches that are more effective as well as more efficient in terms of attenuating negative spillovers. International coordination and learning about good regulatory practice do not require a trade agreement because the problem is not internalizing terms-of-trade spillovers or addressing commitment problems.

Of the so-called "joint statement initiatives" that are now being pursued in the WTO – spanning e-commerce, domestic regulation of services, investment facilitation, and measures to enhance the ability of micro and small and medium enterprises (MSMEs) to utilize the opportunities offered by the rules-based trading system – most address coordination failures or entail joint efforts to identify good regulatory practices. The subjects of discussion are all areas where there are potential gains from cooperation. However, apart from the e-commerce talks, they do not address fundamental sources of recent trade tensions and conflicts. Nor do they deal with matters that will become increasingly prominent soon, such as the use of trade policies to combat climate change.

For the credibility of the WTO it is critical that at least some of the ongoing plurilateral discussions result in agreements. But what matters more for sustaining an open, rules-based multilateral trading system is to use OPAs to manage industrial policy spillovers, regulate the digital

economy and govern climate change-motivated trade policies.

The prospects for successfully using OPAs to do so would be enhanced if engagement extends beyond the trade community and efforts are made to agree to a code of conduct for OPAs to address potential concerns of non-participating countries.

### Supporting plurilateral engagement

Successful international agreements addressing regulatory policies such as the WTO agreements on sanitary and phytosanitary measures, technical barriers to trade and trade facilitation are all associated with a body of agreed technical knowledge and accumulated good will among the relevant national regulatory agencies. The same is true for all successful examples of international regulatory cooperation.

A necessary condition for successful OPAs is to create mechanisms that support informed deliberation in a given policy area and fosters substantive, evidence and analysis-based discussion. Without robust information on applied policies across countries and experience in implementing them it is not possible to identify either good practices, what policies create large spillovers that are systemically important, or efficient approaches to attenuate such spillovers in ways that reflect and respond to local capabilities and priorities. Integrating the relevant stakeholders, regulators, and sources of expertise (e.g., international organizations) in efforts to address such questions is necessary.

Different models can be envisaged to prepare the ground for new OPAs. One is to work through the G20 Trade and Investment Working Group, which spans G20 governments and the major international agencies. Another approach is to create a sector-specific platform serviced by one specialized agency, as was done by the G20 through the 2016 Global Forum on Steel Excess Capacity (GFSEC), which was tasked with producing reliable statistics on steel production capacity and identifying policies that affect steel production. Yet another option is to bring together a group of independent policy research institutes and provide them with a mandate and the resources to collect and analyze information to support engagement by countries to cooperate on a critical mass basis.

In practice effective OPAs are likely to be policy and/or sector-specific, bringing together the WTO (trade community) with other organizations that have a mandate in an area of overlapping interest. On climate change, for example, the Paris Agreement and the WTO provide a basis for the formation of linked OPAs to support domain-specific decarbonization regimes. The Paris Agreement authorizes countries to set national decarbonization targets and to form sector-specific 'climate clubs' for joint pursuit of national targets outside Paris and to count progress achieved there towards their voluntary goals. An implication of the voluntary nature of national commitments under Paris is that any penalty defaults defined by climate clubs involving trade restrictions fall outside the Paris Agreement. Although countries can invoke the general exceptions provision of the WTO to justify the use of trade measures as part of decarbonization initiatives, an OPA can make explicit how trade sanctions will be applied among members of the OPA to attain decarbonization targets they have agreed.

Reconciling sectoral differences in domestic regulatory requirements pertaining to decarbonization of economic activity is just one, albeit very important example where OPAs can reduce the costs of regulatory heterogeneity. The concept can be applied as well to other policy domains, with clubs of countries, without the consent of other WTO members, defining regulatory standards for themselves, but committing that cooperation be open to participation by any WTO member. As a result, participation would be selective, with a WTO member deciding to join some OPAs but not others.

### A governance framework for OPAs in the WTO

While not a panacea, OPAs are a good path forward for countries desiring to deepen cooperation in a given policy area or sector of economic activity. Although OPAs cannot alter the rights and obligations of WTO members that do not sign them, they do raise potential concerns for nonmembers. Even if – as we assume will be the case – agreements are applied on a nondiscriminatory basis, countries that decide not to participate may have an interest in what is discussed and agreed to constitute good practice.

Agreeing to a set of binding principles that OPA signatories commit to abide by can help recognize valid concerns of nonmembers that OPAs be fully consistent with multilateralism. Ensuring that agreements are truly open to any country wishing to join, are fully transparent, and include mechanisms to assist countries not able to participate because of weaknesses in institutional capabilities would do much to ensure OPAs support the goals of the multilateral trading system.

More broadly, developing a framework of general rules for registering OPA commitments, monitoring and evaluating results, establishing penalty defaults and establishment of financial facilities to support expanded participation over time can help facilitate coordination among governments, specialized international agencies and international business organizations.

A governance framework for OPAs can build on WTO precedent in the area of telecom regulation and take the form of a binding Reference Paper that would be incorporated into each OPA.

A Reference Paper on OPAs could include the following elements:

1. A provision making explicit that membership of an OPA is voluntary and that WTO members that decide not to participate cannot be obliged to join at a later date;
2. The OPA is open to subsequent membership by WTO Members that did not join when it was first agreed;
3. A section laying out the requirements and procedures to be followed for accession by aspiring members;
4. A commitment that accession to an OPA cannot be on terms that are more stringent than those that applied to the incumbent parties, adjusted for any changes in substantive disciplines adopted by signatories over time;
5. Where feasible and in instances where capacities must be built for a country to meet OPA requirements, consideration be given to establish a stepwise schedule of compliance;
6. A binding and enforceable provision committing signatories to provide assistance to WTO members that are not in a position to satisfy the preconditions for membership in terms of applying the substantive

provisions of the agreement but desire to do so;

7. Inclusion of consultation and binding conflict resolution procedures that may be invoked by non-signatories of OPAs if they perceive that incumbents impose more stringent conditions to accede to an agreement than apply to extant parties to the OPA, or if parties to an OPA do not live up to the commitment to respond to requests to provide assistance to nonmembers;
8. Provisions that ensure the OPA is open in the sense of including transparency mechanisms to ensure that nonparticipants have full information on the implementation and operation of the agreement. These should include:
  - a. Compliance with WTO requirements pertaining to publication of information on measures covered by the OPA;
  - b. Simple, robust notification requirements for OPA members;
  - c. Regular engagement of stakeholders in an ongoing conversation about how the agreement is working and future needs;
  - d. Annual reporting to the WTO General Council by the OPA on its activities.

These principles do not include a requirement to provide 'special and differential treatment' (SDT) of the type currently embodied in the WTO which permits developing countries to offer 'less than full reciprocity'. Instead, the focus is to assist countries to achieve the common regulatory objectives of OPA members. Including mechanisms to assist countries improve their regulatory regimes to be able to benefit from OPA is important for inclusiveness and for

enhancing their relevance to low-income countries.

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