



Revitalizing the WTO

Settling Trade Disputes in a Turbulent Multipolar World

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Bertelsmann Stiftung High-Level Board of Experts on the Future of Global Trade Governance

In the light of rising threats to the multilateral trading system, the Bertelsmann Stiftung has set up a High-Level Board of Experts on the Future of Global Trade Governance. Composed of seasoned trade diplomats and distinguished experts, it is identifying feasible options for reinvigorating the World Trade Organization (WTO). To inform the Board's ongoing discussions, Bertelsmann Stiftung has commissioned additional research. This paper by Robert McDougall discusses the current controversies around the WTO Dispute Settlement Body which it views as an opportunity to reflect on the design of dispute resolution at the WTO and potentially modify its functioning. The views presented in this paper are the author's which are not necessarily those of the Board.

Further information on the High-Level Board of Experts and its work can be found on futuretradegovernance.org and ged-project.de.

Executive Summary

Despite growing consensus on the need to update the trade rules and strengthen the World Trade Organization, there is little agreement on which reforms are necessary. While some place priority on resolving the impasse over appointments to the Appellate Body, other reforms to the dispute settlement mechanism may be more important to respond to the challenges facing judicialized dispute settlement of trade disputes in the WTO. The changing balance of economic power, ageing trade rules and a backlash against globalization make it difficult to achieve legitimate outcomes through win-lose adjudication. Increasing demand, a potential for a chill on ongoing negotiations and an imbalance between the political and adjudicative functions of the WTO exacerbate these challenges. Resolving the impasse over the Appellate Body will not, on its own, resolve the more profound legitimacy crisis facing the trading system. Members should instead focus on pursuing broader improvements to the dispute settlement mechanism to ensure that it remains fit-for-purpose in the service of trade cooperation in a turbulent multipolar world.

Introduction

The deepening crisis in the multilateral trading system reflects a growing disconnect between the existing rules and the political, economic and technological realities they are meant to govern. The resulting erosion of confidence in the fairness of the trade rules threatens the functioning of the World Trade Organization (WTO). While governments have been slow to respond to the changing global economic dynamics, recent political shocks have forced a recognition that current approaches to trade cooperation are not working as well as they could. At their recent gathering in Buenos Aires, G20 Leaders acknowledged¹ that the trading system is “currently falling short of its objectives” and that “there is room for improvement”. They supported the “necessary reform of the WTO to improve its functioning”.

While there may be general agreement on the need to improve the trading system, there is less agreement on what constitutes “necessary reform”. In an important contribution to this question, the High-Level Report on “Revitalizing Multilateral Governance at the WTO” called first for revitalizing the mechanisms of trade cooperation in order to lay the foundation for the more difficult task of updating the substantive rules.² The Report also highlighted the importance of effective conflict resolution, but acknowledged a number of important challenges facing the WTO dispute settlement mechanism, not least of which is the ongoing impasse over filling vacancies on the Appellate Body.³

Some WTO members propose to treat the crisis over the Appellate Body as the top priority in WTO reform efforts.⁴ However, the weakening of the dispute settlement system is only a symptom, and not the cause, of disruption in the rules-based trading system. As current tensions illustrate, effective trade cooperation, and trade peace, depends on more than the availability of enforceable dispute settlement. Insisting on first restoring the capacity to engage in win-lose adjudication over the existing rules will therefore not resolve these tensions and indeed may even impede efforts to find solutions to them. Instead, efforts to strengthen the dispute settlement function of the WTO should start with a broader evaluation of its operation in order to identify reforms that address the more fundamental challenges to its effectiveness.

The Judicialization of Dispute Settlement at the WTO

The dispute settlement mechanism that emerged with the WTO capped a long period of incremental legalization and judicialization of cooperation on trade. There is no doubt that judicialized dispute settlement helps to de-

¹ G20 Leaders' Declaration: Building consensus for fair and sustainable development, Buenos Aires, Argentina, 1 December 2018, online: <http://www.g20.utoronto.ca/2018/buenos_aires_leaders_declaration.pdf>.

² Report of the High-Level Board of Experts on the Future of Global Trade Governance, “Revitalizing Multilateral Governance at the World Trade Organization” [Revitalizing Multilateral Governance], Bertelsmann Stiftung, 2 October 2018, online: <<https://ged-project.de/research/studies/revitalizing-wto-2>>.

³ Summary of the DSB meeting of 21 November 2018, online: <www.wto.org/english/news_e/news18_e/dsb_19nov18_e.htm>.

⁴ European Union, “Concept paper: WTO modernisation”, undated, online: <http://trade.ec.europa.eu/doclib/docs/2018/september/tradoc_157331.pdf>.

politicise trade relations by delegating the resolution of disputes to impartial third parties and providing binding enforcement mechanisms. In the process, it mitigates (although does not completely eliminate) power asymmetries between states and brings greater clarity and coherence to the meaning of trade commitments. Importantly, since trade cooperation occurs in the “shadow of the law”, these effects are felt far beyond the specific disputes brought before it, contributing to the security and predictability of the rules-based trading system.

In its short life, the WTO dispute settlement mechanism has exceeded expectations. It is frequently celebrated as the “jewel in the crown”⁵ of the WTO and as one of the most prolific and successful systems of international adjudication in history. Due in part to this success, it has taken on an increasing share of the responsibility for the maintenance of trade cooperation, a burden that has been magnified by the relative underperformance of the negotiating function. However, the disproportionate centrality of judicialized dispute settlement to the trading system exposes it to a number of external and internal challenges. These will need to be addressed as part of efforts to strengthen the dispute settlement function and revitalise rules-based cooperation on trade.

External Challenges to Effective Dispute Settlement

The first set of challenges arise from the fundamental changes to the context in which trade cooperation and dispute settlement occur. The WTO was founded in a moment of optimism about global integration and growing acceptance of both market-oriented models of economic development and the legalisation of international trade relations. The trade rules that were codified in the WTO reflected this historical convergence. However, the context has changed in a number of interconnected ways that have diminished the effectiveness of WTO adjudication.

First, the trade rules have failed to keep pace with changing realities. The effect of the structural transformation of the global economy and technological change have modified the value of certain concessions and upset the existing balance of rights and obligations. As the balance of economic power shifts and negotiations over new rules stall, some WTO members may be tempted to pursue their market access objectives through adjudication, whereas others may seek to avoid the enforcement of rules they consider no longer reflect underlying economic realities (e.g., the “non-market economy” disputes).⁶ With waning consensus on whether the existing rules contain “reciprocal and mutually advantageous arrangements”,⁷ it becomes increasingly difficult for adjudication in certain areas to provide outcomes that will be accepted as legitimate by all parties.

Second, the disruption and economic insecurity caused by these changes in the global economy have led to political upheaval in some countries and a backlash against both globalisation and multilateralism. The resurgence of nationalism has led some to reassert sovereignty as the most important institution in international relations.⁸ At least some of the discontent reflects a lack of trust that the existing rules provide for an equitable distribution of the benefits of trade and a concern that certain dispute settlement outcomes may have contributed to this disequilibrium. Domestic political pressures simultaneously increase the willingness to take unilateral trade-distorting measures and decrease the willingness to abide by the findings of international tribunals on the conformity of those measures to the trade rules.

Third, emerging multi-polarity and the associated geo-political rivalry between the United States and China cause some to see the level of economic interdependence fostered by the trade rules as a liability. The equation of economic security with national security⁹ and the resulting pressure to “decouple”¹⁰ the two economies

⁵ WTO, “WTO disputes reach 400 mark”, 6 November 2009 (quoting WTO Director General, Pascal Lamy), online: <https://www.wto.org/english/news_e/pres09_e/pr578_e.htm>.

⁶ David Lawder, “U.S. formally opposes China market economy status at WTO”, Reuters, 30 November 2017, online: <<https://www.reuters.com/article/us-usa-china-trade-wto/u-s-formally-opposes-china-market-economy-status-at-wto-idUSKBN1DU2VH>>.

⁷ Preamble of the GATT, online: <https://www.wto.org/english/docs_e/legal_e/gatt47_01_e.htm>.

⁸ Michael Pompeo, US Secretary of State, “Restoring the Role of the Nation-State in the Liberal International Order”, Remarks at the German Marshall Fund, 4 December 2018, online: <<https://www.state.gov/secretary/remarks/2018/12/287770.htm>>.

⁹ See “Economic security is national security”, in White House, “National Security Strategy of the United States of America”, December 2017, online: <www.whitehouse.gov/wp-content/uploads/2017/12/NSS-Final-12-18-2017-0905.pdf>.

¹⁰ Richard McGregor, “US and China -- the great decoupling”, Nikkei Asian Review, 22 October 2018, online: <<https://asia.nikkei.com/Opinion/US-and-China-the-great-decoupling>>.

undermines the voluntary restraint traditionally in effect against taking measures and pursuing legal disputes that could undermine the integrity of the rules-based trading system. There are now sixteen dispute proceedings in the WTO that involve national security justifications for trade-distorting measures.¹¹ Regardless of the legal merit of each side's claims, these proceedings will not resolve the underlining tensions and may even further erode respect for the existing rules and institutions.

Internal Challenges to Effective Dispute Settlement

The WTO dispute settlement mechanism also faces a number of challenges that are internal to its operation. The innovations adopted in the Dispute Settlement Understanding¹² (in particular reverse consensus and appellate review) overcame the weakness of dispute settlement under the GATT and have contributed significantly to the success of the WTO. However, the unprecedented degree of judicialization in the multilateral trading system may have had several unforeseen, and unforeseeable, consequences for cooperation on trade.

First, even prior to the impasse over the Appellate Body, the dispute settlement mechanism was increasingly struggling to deliver results within the prescribed time periods,¹³ which increases the risk of opportunistic trade-distorting measures. Worsening delays are likely attributable to a combination of rising demand, the changing nature of disputes and the techniques employed by increasingly sophisticated parties. While rising demand is often presented as evidence of the system's success,¹⁴ it may also reflect a growing emphasis on win-lose adjudication at the expense of other conciliatory, and often more timely, approaches to resolving trade irritants. Moreover, there is some evidence that much of the demand is from a sub-set of WTO members bringing repeat disputes over a narrow range of issues.¹⁵ The combination of a cultural shift toward adversarial dispute resolution and the dominance of a few repeat members raises concerns about whether the system is as inclusive and accessible as it could be.¹⁶

Second, while judicialized dispute settlement is effective in resolving disputes over the existing rules, its effect on efforts to advance cooperation in new areas is unclear.¹⁷ The dispute settlement mechanism, and the parties that take their disputes before it, seem committed to address all issues and clarify all ambiguities in the existing rules.¹⁸ However, there is anecdotal evidence that this emphasis on clarity and certainty may actually impede the emergence of consensus on new rules by narrowing the scope for "constructive ambiguity" in ongoing negotiations. Similarly, the regular WTO bodies seem to be increasingly reluctant to document or codify the results of their deliberations for fear that these might have unintended effects on the interpretation of their existing obligations. Some members may even be tempted to pursue adjudication rather than negotiations in the hope that they can achieve their objectives without the compromises and trade-offs inherent in a negotiation.¹⁹

Third, while the design and architecture of the WTO legal framework reserves the ultimate authority over the interpretation of WTO commitments to members,²⁰ in practice WTO adjudicators have nearly unchecked

¹¹ Summary of the DSB meeting of 21 November 2018, *supra* note 3.

¹² WTO, "Understanding on rules and procedures governing the settlement of disputes", Annex 2 of the Marrakesh Agreement (DSU), online: <www.wto.org/english/tratop_e/dispu_e/dsu_e.htm>.

¹³ WTO, "Azevêdo says success of WTO dispute settlement brings urgent challenges", 26 September 2014, online: <https://www.wto.org/english/news_e/spra_e/spra32_e.htm>.

¹⁴ WTO, "WTO disputes reach 500 mark", 10 November 2015, online: <https://www.wto.org/english/news_e/news15_e/ds500rfc_10nov15_e.htm>.

¹⁵ Joost Pauwelyn and Weiwei Zhang, "Busier than Ever? A Data-Driven Assessment and Forecast of WTO Caseload", 26 June 2018, online: <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3179713>.

¹⁶ Robert McDougall, "Making Trade Dispute Settlement More Accessible and Inclusive", Centre for International Governance Innovation, 2 November 2017 [Inclusive Dispute Settlement], online: <<https://www.cigionline.org/articles/making-trade-dispute-settlement-more-accessible-and-inclusive>>.

¹⁷ Judith Goldstein and Lisa Martin, "Legalization, Trade Liberalization, and Domestic Politics: A Cautionary Note", International Organization 54.3, Summer 2000: 603–632, online: <http://www.columbia.edu/itc/sipa/S6800/courseworks/legal_goldstein.pdf>.

¹⁸ Article 17.12 of the DSU provides that the "Appellate Body shall address each of the issues raised in accordance with paragraph 6 during the appellate proceeding".

¹⁹ The United States raised this concern in its opening statement at the 2017 WTO Ministerial Conference, 11 December 2017, online: <<https://ustr.gov/about-us/policy-offices/press-office/press-releases/2017/december/opening-plenary-statement-ustr>>.

²⁰ Article IX:2 of the Marrakesh Agreement reserves to WTO members the "exclusive authority to adopt interpretations" of the obligations contained in the WTO agreements. Article 3.9 of the DSU acknowledges the hierarchy of "authoritative interpretations" over the results of dispute settlement.

autonomy to affect the meaning of WTO rights and obligations. Indeed, the decision of the United States to block appointments to the Appellate Body is motivated in part by grievances, some of them longstanding, about how the tribunal has exercised this autonomy.²¹ While there may be a good faith disagreement among members about whether the Appellate Body has discharged its mandate with sufficient circumspection, there is no question that the unintended imbalance between the political and adjudicative bodies of the WTO threatens the legitimacy of the dispute settlement mechanism.²²

Dispute Settlement in the Service of Trade Cooperation

Despite its procedural pretexts and systemic justifications, the impasse over the Appellate Body is a symptom of a more profound legitimacy crisis in the trading system. The combination of the changing balance of economic power, ageing trade rules, and scepticism about whether the benefits of globalisation have been distributed equally present considerable challenges for continued rules-based cooperation on trade. The WTO dispute settlement mechanism cannot, on its own, resolve any of these issues. Indeed, efforts to prioritise the restoration of the Appellate Body may only distract from, and in the worst case even become an obstacle to, more fundamental reforms to the rules and institutions of international trade.

Contrary to the concerns expressed by some, the incapacitation of the Appellate Body does not “threaten the survival of the WTO”²³ and will not make the existing rules “count for little”.²⁴ It will not even bring about the collapse of the entire dispute settlement mechanism, which is about more than its appeal and enforcement mechanisms.²⁵ Of course, strengthening the dispute settlement function of the WTO, including compulsory, impartial and enforceable third-party adjudication, should be an important outcome of the reform effort. But simply restoring the appellate function will be insufficient to adapt it to the changed context and overcome some of its current limitations.

Instead, the dispute settlement mechanism should be evaluated for its contribution to overcoming problems in trade cooperation. Recourse to adjudication reflects a failure to resolve cooperation problems by other means and should normally be considered a last resort. However, a system that places a disproportionate emphasis on win-lose adjudication relieves members of the responsibility, and in some circumstances deprives them of the opportunity, to pursue more timely and conciliatory resolution of their trade disputes. As part of efforts to restore trust in the benefits of rules-based trade, reform of the dispute settlement mechanism should focus on restoring the “proper balance” between the political and adjudicative functions of the WTO.²⁶

Restoring Balance Between the Political and Adjudicative Functions

There is increasing acknowledgement that updating the trade rules and strengthening the WTO may require new forms of flexibility for both the content of commitments and the legal frameworks within which they are codified.²⁷ Likewise for the dispute settlement mechanism, it may be necessary to introduce greater flexibility to address the challenges to its legitimacy and restore balance in its operations. This rebalancing could be accomplished by

²¹ “Statements of the United States at the August 2018 Meeting of the Dispute Settlement Body”, items 4 and 15, online: <https://geneva.usmission.gov/wp-content/uploads/sites/290/Aug27.DSB_Stmt_as-delivered.fin_public.pdf>.

²² Robert McDougall, “Crisis in the WTO: Restoring the Dispute Settlement Function”, Centre for International Governance Innovation, CIGI Paper No. 194, 16 October 2018, online: <<https://www.cigionline.org/publications/crisis-wto-restoring-dispute-settlement-function>>.

²³ MOFCOM Press Release, “China, the EU and other Members Submit Joint Proposal to the WTO to Promote the Selection of Members of the Appellate Body”, 27 November 2018, online:

<<http://english.mofcom.gov.cn/article/newsrelease/significantnews/201811/20181102811583.shtml>>.

²⁴ Letter from Chair of the Appellate Body to Heads of Delegations to the WTO, 14 December 2018, obtained by Bloomberg, online: <<https://twitter.com/bbaschuk/status/107362432111875584>>.

²⁵ Robert McDougall, “Impasse in the WTO Dispute Settlement Body: Consequences and Responses”, ECIPE Policy Brief No 11/2018 [Impasse in the DSB], online: <<https://ecipe.org/publications/impasse-in-the-wto-dispute-settlement-body>>.

²⁶ Communication from Australia, Singapore, Costa Rica, Canada and Switzerland to the General Council, “Adjudicative Bodies: Adding to or Diminishing Rights or Obligations Under the WTO Agreement”, WT/GC/W/754/Rev.2, 11 December 2018 [Adjudicative Bodies], online: <<http://bit.ly/wto-gc-754-2>>.

²⁷ Revitalizing Multilateral Governance, *supra* note 2.

strengthening the capacity for political decision-making on the one hand while reducing the emphasis on win-lose adjudication on the other.

On the political side of the ledger, in addition to improving the negotiating function to modernize the rules, there could be more opportunity and greater responsibility for political cooperation to resolve trade disputes and clarify the meaning of trade commitments. This could be accomplished by providing better safety valves for politically sensitive disputes, through diversion to political bodies or, during the current trade tensions, a moratorium of certain kinds of disputes.²⁸ Strengthening the deliberative function of the regular WTO committees would also help.²⁹ More systemically, the exclusive but as yet unused authority of members to adopt “authoritative interpretations” of their WTO commitments could be better operationalised. For example, procedures could be developed that regularise the deliberation and adoption of negotiated interpretations,³⁰ either to proactively clarify ambiguous WTO provisions or to override or disallow dispute settlement findings that exceed what is acceptable to members.³¹

On the dispute settlement side of the ledger, there could be a reduction of the reliance on, and the consequences of, compulsory adjudication. For starters, the opportunities for mediation and conciliation could be improved to place more emphasis on reconciling interests rather than determining legal right and wrong.³² As the experience in dispute settlement under the WTO has already shown, there are some disputes that simply cannot be resolved through adjudication. In cases where adjudication becomes necessary, the scope of adjudication could be narrowed and the procedures streamlined to make them more timely and accessible.³³ Finally, to mitigate the risk of a chill on ongoing negotiations and committee deliberations, some categories of information and some types of deliberations could be declared inadmissible in dispute settlement proceedings.³⁴ Most of these changes can be implemented through “authoritative interpretations” adopted by the General Council of the WTO.

The pending incapacitation of the Appellate Body is serious and concerning but is not itself fatal to rules-based trade cooperation or even necessarily to the WTO’s capacity to settle trade disputes. Given the lack of confidence among some members that the current rules provide a framework for balanced and reciprocal trade relations,³⁵ it is not yet clear whether the dispute settlement mechanism can even be fully restored separately from an update of those rules. If the Appellate Body does become incapacitated, members can use “no-appeal agreements” during an interim period to reserve access to the enforcement function of the WTO.³⁶ More importantly though, members should also be thinking about broader improvements to the dispute settlement mechanism to ensure that it remains fit-for-purpose in the service of trade cooperation in a turbulent multipolar world.

²⁸ Communication from Canada, “Strengthening and modernizing the WTO: Discussion paper”, JOB/GC/201, 24 September 2018 [Strengthening the WTO], online: <<http://bit.ly/wto-job-gc-201>>. For example, a political agreement could exclude from dispute settlement, or suspend ongoing disputes related to, issues that are unlikely to be resolved through legal proceedings, such as those currently related to national security and non-market economy status or similar to those raised in the *US—Helms Burton* dispute (DS38).

²⁹ Communication from Canada, “Strengthening the deliberative function of the WTO: Discussion paper”, JOB/GC/211, 14 December 2018, online: <<http://bit.ly/job-gc-211>>.

³⁰ Adjudicative Bodies, *supra* note 26.

³¹ One example of such an interpretation in a different context is the “Notes of Interpretation of Certain Chapter 11 Provisions”, adopted by the NAFTA Free Trade Commission on 31 July 2001 to “clarify and reaffirm the meaning of certain of [the] provisions” of NAFTA Chapter Eleven, online: <http://www.sice.oas.org/tpd/nafta/commission/ch11understanding_e.asp>.

³² Inclusive Dispute Settlement, *supra* note 16.

³³ Strengthening the WTO, *supra* note 28.

³⁴ See, for example, Paragraph 10 of the Decision of the General Council, “Transparency Mechanism for Regional Trade Agreements”, WT/L/6711, 4 December 2006, online: <<http://docsonline.wto.org/imrd/directdoc.asp?DDFDocuments/tWT/L/6711.doc>>.

³⁵ Statement by Ambassador Shea at the 14th WTO Trade Policy Review of the United States, 17 December 2018, online: <<https://geneva.usmission.gov/2018/12/17/u-s-statement-by-ambassador-shea-at-the-14th-wto-tpr-of-the-united-states-of-america>> (stating that “the WTO is not well equipped to handle the fundamental challenge posed by China”).

³⁶ Impasse in the DSB, *supra* note 25.

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