



Background Memo

Trade and Trade Governance

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Reviving the Multilateral Trading System and World Trade Organization Reform

It is no secret that the World Trade Organization (WTO)—and the rule-based trading order it intends to safeguard—is under threat. In December 2019, the United States’ refusal to fill vacancies on the WTO’s Appellate Body left it without a quorum, allowing countries to avoid compliance with rulings they do not like or find difficult to implement. Despite multiple calls for swift action, the WTO has not reached an agreement to curb fishery subsidies or write rules for e-commerce and digital trade. Nor has the WTO been able to adopt rules to address growing concerns over China’s unfair trade practices, including intellectual property theft, forced technology transfers, and extensive reliance on subsidies and state-owned enterprises (SOEs). Reforms to the operations of the WTO itself are also left undone. Careful institutional reform, starting with a revitalization of the WTO’s Appellate Body, and an embrace of sustainable development issues can reinvigorate the WTO and help ensure the survival of the current global economic order.

Fundamentally, the WTO consists of three main pillars: First, the WTO serves as a venue for negotiations, enabling members to come together and create new trade rules. Second, the WTO serves as the central clearinghouse for important trade information—tariff schedules, subsidy notifications, etc.—and provides support for its committees’ work. Third, members can use the WTO’s dispute settlement arm to resolve disagreements between members.

None of these elements are functioning as intended. Apart from the 2017 Trade Facilitation Agreement, the WTO has been unable to agree upon new rules or amend old ones. Members routinely decline to provide timely notifications of subsidies and other actions, while the WTO committees have limited power. The United States’ blocking of new appointments to the WTO’s Appellate Body—the backstop of the dispute settlement system—has hamstrung the institution’s ability to resolve disagreements and reflects the United States’ skepticism in the WTO’s ability to safeguard U.S. national interests.

The first step to revitalizing the WTO is to reform its dispute settlement system. Without a system that can hold members to their commitments, countries will be less willing to negotiate new agreements and could become emboldened to disregard existing commitments. If the WTO cannot resolve differences between

members, states could take matters into their own hands or look to other venues to resolve disputes. While additional reforms are required, a functioning Appellate Body could have a beneficial downstream effect, reenergizing the WTO's negotiation and executive functions.

Any reform will have to address the United States' long-standing complaints that the Appellate Body has overstepped its bounds and failed to adhere to certain timing and procedural obligations. New Zealand's Ambassador to the WTO David Walker offered proposals to address many of these concerns, but the core of the United States' frustration—the Appellate Body's restrictions on the use of trade remedies intended to protect against unfairly priced or subsidized imports—remains unaddressed. This issue could be resolved through the use of a specialized appellate body that solely addresses trade remedy appeals or by foregoing appeals in trade remedy cases altogether, assuming that domestic tribunals already examine the facts and the law of each determination.

Beyond dispute settlement, WTO reform will require restoration of its negotiating function. New rules are desperately needed to address e-commerce and digital trade, combat climate change, and confront the various distortions caused by subsidies, SOEs, and trade with nonmarket economies. To do this, WTO members would need to abandon the one-size-fits-all notion that all 164 members are bound to the same rules. Some of the WTO's new or updated rules could be considered inappropriate for all members, so members will need to find ways to integrate plurilateral agreements into the WTO's rule book. Changes to encourage transparency among members, including insisting on timely notifications of trade measures such as subsidies, are also needed.

Addressing the roots of this crisis will also require reconsidering the purpose of the WTO. The General Agreement on Tariffs and Trade (GATT), predecessor to the WTO, focused on trade liberalization from its inception. Presently, with most basic tariffs at low levels, the world faces more pressing challenges: equitably resolving the COVID-19 crisis, encouraging global development, ensuring fair treatment of workers, and facilitating the transition to a green economy. The WTO should pivot so that its agenda, new rules, and sense of common purpose are directed at supporting sustainable growth and development.

Regional Agreements and Fragmentation of the Trading System

One striking feature of the current trading system has been the rapid rise in bilateral and regional trade agreements. In 1990, when states were negotiating the WTO rules, 50 such agreements were in force. Today, that number is 341, with many agreements such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and Regional Comprehensive Economic Partnership (RCEP) encompassing large swaths of global trade flows.

The WTO's failure to develop new rules on issues such as digital trade has contributed to rise of regionalism. Additionally, many of the forces that once pushed the world toward globalization—lower transport costs, labor costs, technology—are now encouraging regional trade. Robots, 3D printing, and semiautomated assembly lines have changed where and how many products are made. Labor costs, which once drove companies abroad, are rising in China and other markets, making overseas production less of a bargain. Consumers are demanding custom-made goods delivered overnight to their doorsteps, undercutting the appeal of mass production in far-flung locales.

If trade and trade rules are going regional, the future role of the WTO and the multilateral rules-based trading system will depend in large part on whether the WTO succeeds in modernizing its governance practices and reforming its dispute settlement system. If it does, then the following issues should remain squarely in the WTO's corner:

- *Subsidies and State-Owned-Enterprises:* The basic rules and disciplines on subsidies will need to be global, particularly in areas such as agriculture, in which the goal is both overall caps on the amount of spending and rules for disciplining subsidies themselves. As the world works to address the global crises of climate change and COVID-19, developing clear rules on appropriate subsidization is of paramount importance.
- *Services:* The basic rules on trade in services will need to be global; countries cannot easily or efficiently implement one set of regulations for services with regional trading partners and develop another set for other partners.
- *Digital Trade:* The rules and standards around digital trade will need to be set at a global level. While the trend in trade in goods and even certain services could be going regional, digital trade is not bounded geographically. Moreover, regional standards could lead to a lack of interoperability between different blocs.
- *Trade Facilitation:* At its core, the goal of trade facilitation is simplifying customs clearance and other border procedures. Differentiating between trade coming from regional partners versus non-regional trade would undermine such efforts and increase the cost of all trade.
- *Transparency:* The WTO currently provides, and should continue to provide, comprehensive databases where global traders can understand tariff schedules, services commitments, and other rules of the road for trade.
- *Intellectual Property Protection:* While trade in goods and services could become more regional, ideas will continue to move globally, meaning the basic rules governing intellectual property will need to be global.
- *Relationship with Global Standards:* Standards-setting organizations, such as the International Telecommunications Union or the World Organization for Animal Health, currently establish global standards on technology, food, and other goods. The WTO expressly incorporates aspects of these standards into its own rules. The development and enforcement of these standards at a global level is unlikely to change.

National Security Exceptions

Another troubling development laid at the feet of the WTO has been the blurring of the line between economic and national security. From its inception, the WTO (and before it, the GATT) recognized that all countries needed the freedom to take measures to protect their national security, but that such a right should be circumscribed to ensure that national security claims did not undermine basic trade rules. As a result, an exception (Article XXI of the GATT) was crafted to permit countries to block trade or violate their trade commitments to protect their essential security interests. However, the exception is only applicable to trade in nuclear materials, arms or ammunition, or measures taken during war or international emergencies.

The exact meaning of Article XXI and how to evaluate actions relevant to national security interests had been the subject of mainly academic debate until 2017. That year, Ukraine brought the first challenge to Article XXI before the WTO, alleging that the myriad of trade and transit restrictions Russia placed on the movement of its goods were illegitimate. Russia, joined by the United States, contended that because only countries can determine what is in their national security interest, a WTO panel could not judge Russia's restrictions. The panel disagreed, ruling it could review actions taken under the national security exception and

determine if an action has a plausible connection to one of the specifically identified bases for national security-based trade restrictions. While the ruling makes clear that a WTO panel can scrutinize actions taken in the name of national security, it suggests that the well-understood and widely accepted distinction between economic measures and security measures is no longer clear.