
Concluding Comments

The introduction to this analysis raised four major concerns about WTO dispute settlement: it has led to more protection, it is ineffective in enforcing compliance, it has undermined national sovereignty (through sanctions and judicial activism), and it is unfair to smaller participants. Are these concerns warranted?

Protection

Retaliation in response to violations under the WTO remains rare. Only one large member (the United States) has retaliated in two cases (beef and bananas). Now another large member (the European Union) is threatening retaliation in response to the foreign sales corporation–Extraterritorial Income Exclusion Act (FSC-ETI) case. In some cases, had the previous GATT system been in operation, with the possible exception of the FSC, similar measures would probably have been imposed unilaterally, without WTO authorization and oversight. Nonetheless, authorizations of the magnitude of \$4 billion given to the European Union in response to FSC-ETI are substantial and could seriously disrupt trade. They could also spur escalation. In addition, although they have so far decided not to exercise their rights, other countries (for example, Ecuador, Canada, and Brazil) have been authorized to suspend concessions. There is also a

real danger that in their rulings under the WTO Agreement on Subsidies and Countervailing Measures (SCM) the arbitrators are becoming increasingly punitive. It would surely be preferable if the WTO could devise a mechanism that avoided retaliation while remaining as effective as the current system in offering incentives for compliance, providing a legal escape clause, and maintaining reciprocity.

Compliance

Compliance with WTO and GATT rulings has generally been good although it has not always been rapid (Hudec 2002, 82). At times (for example, the *United States–FSC* and *EC–Bananas* cases), countries have made superficial changes in their policies, which have not actually brought them into compliance. Nonetheless, upon being found in violation, in every case members have announced their intention to comply, and the preponderance of the cases have been settled. Why is compliance common if retaliation is rare? In some economic models of trade negotiations, compliance depends only on the probability and size of retaliation. But other factors are surely more important. First, often important parties within each country have an interest in compliance—for example, consumers, exporters, and import distributors. Second, even when members disagree over a particular case, they comply because they continue to believe that overall a trading system based on rules will serve the nation’s interest. Third, officials and others value their reputations as rule-abiding participants because of the interests they have in the current agreement and because of their desire to be taken seriously when negotiating new agreements. Countries are aware that compliance on their part could influence the probability that other countries will comply in the future. They are aware that other members are unlikely to grant politically painful concessions if they have little faith that a negotiating partner will meet its commitments. And fourth, countries generally have ongoing relationships in other spheres. Countries that depend on the United States for aid and defense, for example, might be more willing to comply with findings of disputes in which it is involved.

However, it remains true that the prospect of retaliation aids compliance. Moreover, the system should itself not provide incentives for violations by preventing countries from rebalancing concessions in response to violations. Nonetheless, despite all the reasons for compliance, there will inevitably be cases, such as hormone-treated beef, in which a member prefers to violate the agreement notwithstanding the impact of retaliation and the harm that may be done to its reputation and relationships. In these cases, the system’s role is to prevent deadlock leading to escalation. In this respect, the WTO has generally been successful, although dangers remain in the current US-EU frictions.

Sovereignty

Sovereignty is a slippery concept that has been given a variety of meanings and connotations. As Stephen Krasner (2001) has argued, the invocation of the notion has often been associated with “organized hypocrisy.” One notion of sovereignty that does have a clear meaning is as a synonym for ultimate legal authority. Who has the right to make the rules? In this most meaningful sense, members of the WTO do not yield their sovereignty. The US Constitution places legislative authority with the US Congress, and US laws cannot constitutionally be made elsewhere. The US Supreme Court has held, for example, that even if Congress decides to delegate more power to the executive branch, it may not do so without a change in the Constitution. When Congress gave the president the authority to veto individual line items in the budget, for example, the Supreme Court declared this delegation unconstitutional.¹ If Congress cannot yield its authority to the president, it certainly cannot yield it to the WTO!

Article I of the Constitution gives Congress the (exclusive) power “to lay and collect taxes, duties, imposts and excises” and “to regulate commerce with foreign nations and among the several states,” and Congress has shown absolutely no inclination to try to delegate this authority to someone else. Indeed, it guards this power jealously. Even the US president cannot change US trade laws. While the president may negotiate trade agreements, if these involve changes in US law, he needs authority to do so from the Congress. Between 1934 and 1962, Congress allowed the president to negotiate tariff and other concessions under the Reciprocal Trade Agreements Act. But it did so only for specified periods of one to three years at a time. Once trade agreements began to cover measures besides tariffs, Congress made clear that if trade agreements would require a change in US laws, this could not happen without congressional passage of the changes.² Remarkably, perhaps, even after it has approved a trade agreement, Congress can adopt laws that are in conflict with it

1. Writing for the majority, Justice John Paul Stevens (in *Clinton v. New York*, no. 97-1374, United States Supreme Court Decision, June 25, 1998) wrote, “The Line Item Veto Act authorizes the President himself to effect the repeal of laws, for his own policy reasons, without observing the procedures [*132] set out in Article I, 7. The fact that Congress intended such a result is of no moment. Although Congress presumably anticipated that the President might cancel some of the items in the Balanced Budget Act and in the Taxpayer Relief Act, Congress cannot alter the procedures set out in Article I, 7, without amending the Constitution.”

2. Section 12 (c) states: “If the President enters into a trade agreement which establishes rules or procedures of such agreement will change any provision of Federal law (including a material change in an administrative rule), such agreement shall take effect with respect to the United States only if the appropriate implementing legislation is enacted by the Congress unless implementation of such agreement is effected pursuant to authority delegated by Congress” (United States Code, Title 19—Customs Duties, Chapter 12: Trade Act of 1974, Subchapter I: Negotiating and Other Authority).

(Boyers 1998). Under US law, international treaties have the same authority as federal law, which implies that Congress can pass laws that violate US treaty obligations in precisely the same way it can pass new laws that conflict with earlier laws. In particular, Congress can legally pass trade measures that violate the WTO.³ Congress may thus later deny what it has previously given.⁴ As Patrick Low (1993, 48) notes, “In practice, this means that the status of the GATT and associated agreements under US laws gives virtually limitless potential in US trade policy for noncompliance with GATT.” In Europe, similarly, both legislatures and executives of the European Community assert domestic power to adopt “later-in-time legislation” and domestic implementing measures inconsistent with their international WTO obligations. And in both the United States and the European Union, legislation on the implementation of the WTO agreement prevents private citizens from invoking WTO rules before domestic courts vis-à-vis domestic legislation that is inconsistent with WTO law.

Sovereignty has other meanings in addition to the idea of legal authority. One of these refers to the ultimate power, the practical (as opposed to the legal) ability of the state to control behavior. Some states have difficulties in exerting such control domestically—the phenomenon of failed states exemplifies this dimension. But states also have an interest in controlling behavior beyond their borders. One mechanism for such control is the treaty. Paradoxically, therefore, concluding treaties is an act of sovereignty. By agreeing to constrain its own behavior, the state constrains the behavior of others. The WTO is just such an agreement.

Some object that by signing a WTO agreement, a country restricts its ability to act autonomously and as such entails a constraint on its freedom of action. This is true. For an agreement—whether between two individuals or many nations—to mean anything, it must constrain the future actions of those who sign it.

These constraints may be explicit parts to the agreement. They may also be implicit. According to Phillip Trimble (1997, 2), for example, the WTO erodes sovereignty in this fashion:

Although it is true that Congress may constitutionally pass legislation in derogation of WTO obligations, just as other parts of the federal government may violate WTO obligations without effective challenge under US domestic law . . . as a practical matter . . . the WTO's preference for international standards and the certainty of sanctions for violations will inevitably induce government

3. Under established constitutional law, US courts give precedence to an act of Congress over an inconsistent international agreement if the act is subsequent in time. Similarly, the courts have permitted the president to violate customary international law (Tiefer 2000, 17).

4. The United States' first major trade treaty, the Jay Treaty of 1794 with Great Britain, depended on the willingness of Congress to enact appropriations for its implementation, even after Senate ratification. The Congress enacted appropriations only reluctantly.

decision-makers to prefer compliance with international standards [emphasis added]. . . . The resulting practical devolution of decision-making authority to international institutions is the essence of the loss of national sovereignty.⁵

While the United States may indeed find its domestic behavior constrained, it could also find that in return, its overall ability to act is expanded. Paradoxically, therefore, these constraints may *expand* the options the United States has to act freely. By agreeing to constrain their own behavior, WTO members constrain the behavior of others, and this may increase the choices they can make. In an interdependent world, for example, the ability to participate in creating international standards may be more important than the ability to determine standards unilaterally.

After all, in general international trade provides countries with more choices about what to produce and what to consume. Without the assurance that their products will have entry to foreign markets, for example, America's farmers may choose not to grow as much wheat, and American industry may choose to produce fewer computers. Without the assurance that imports will not be stopped at the border, America's department stores would be less willing to stock imported products and America's factories less willing to rely on imported inputs. Farmers, stores, and factories may still choose to buy and sell domestically, but trade gives them more options and trade agreements help make these options more secure.

In sum, claims that the WTO authorizes penalties are (with the exception of export subsidies) false. Those who make this claim forget that violators have in principle failed to keep their part of a deal for which they received concessions from the plaintiffs. The WTO allows rebalancing through suspension of concessions to allow the plaintiff to redress some of the harm from the breach, but it does not permit sanctions. Such suspension also provides countries with a *de facto* opt-out mechanism that allows them to avoid compliance and is thus also a mechanism for dealing with the dangers of excessive judicial activism. The WTO Dispute Settlement Body (DSB) has no authority to add to the members' obligations, and in any case, members need not grant WTO rulings direct effect in their domestic law.

Equity

While a small country could still decide to employ retaliation to try to teach a larger trading partner a lesson and discourage future defections,

5. Likewise, although he does not believe this applies to trade agreements, Jeremy Rabkin argues that "the real threat is not that the US will be forced to act against the determined resolve of the American political system. Rather, the threat is that international commitments will distort or derange the normal workings of our own system, leaving it less able to resolve policy disputes in ways acceptable to the American people" (quoted in Rogowsky et al. 2001).

it will find such actions relatively more costly to undertake than its larger counterparts because it cannot obtain favorable movements in its terms of trade. Smaller countries may also feel more vulnerable to other kinds of political pressures. Since they can do little to improve their terms of trade, economic theory suggests that small countries will on balance reduce their own welfare by suspending concessions. Their limited market power therefore gives small WTO members less capacity to induce compliance through retaliation. This feature of the WTO system is, however, the mirror image of the advantages smaller countries may enjoy during negotiations from being able to free ride on the most favored nation (MFN) principle and, for less developed members, from special and differential treatment. Moreover, with the negotiation of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), developing countries acquired an area in which they are now able to retaliate more effectively. Indeed, in the bananas case, Ecuador requested authorization to retaliate against the European Union by suspending the intellectual property rights of EU exporters.⁶

Despite their disadvantages in threatening retaliation, complaints by developing countries have generally been successful in obtaining compliance—presumably because of the other motivations for compliance mentioned above.⁷ Nonetheless, the WTO is a system in which members are supposed to have equal rights, and it would be desirable if the imbalance between small and large countries could be redressed.

In sum, overall the WTO has contributed to liberalization and been effective in establishing a system in which members comply with the rules. The WTO system is actually remarkably deferential to national sovereignty, and the difficulties smaller members experience in retaliating are the mirror image of the benefits they derive in obtaining concessions. Nonetheless, introducing contingent liberalization commitments (CLCs) could eliminate the possibility of the WTO contributing to protection, aid in compliance and respecting national sovereignty, and eliminate the unfair treatment of smaller members.

Final Observations

WTO members seek to promote their economic welfare by negotiating and enforcing a rules-based system that promotes trade liberalization. National self-interest lies at the core of the WTO system. Members join the organization and comply with its rules and rulings because, through

6. Despite being granted such authorization, Ecuador chose not to retaliate.

7. According to Robert Hudec (2002, 82), "Over the GATT's history, out of 22 complaints brought by developing countries that were based on a valid legal claim, satisfaction was achieved in 18."

their own decision-making processes (democratic or otherwise), on balance, they deem membership and compliance in their interest. The WTO operates by consensus, and since every member has the ability to veto any agreement, agreements can be presumed to reflect (so-called Pareto optimal) arrangements that make no member worse off.

The consensus decision-making rule under which the WTO operates helps enhance its legitimacy by requiring all members to concur with all agreements. But the vague and incomplete language that helps achieve agreement also leads to implementation problems. Members signing agreements appreciate that they could find themselves on the losing side in WTO panel disputes. But even under these circumstances, they cannot be compelled to comply and have the option of accepting retaliation, providing compensation, and living with whatever opprobrium is associated with failing to meet an obligation under international law.

The WTO is an agreement among sovereign nation-states, and the belief that the organization enhances national self-interest is the ultimate source of WTO legitimacy. The WTO system in general and the dispute settlement system in particular should be designed to enhance this belief. The rules analyzed in chapter 2 suggest that the remedies in the dispute settlement system are constructed in a way that aims at encouraging members to sign agreements that are *ex ante* in their interest. *Ex post*, countries can again implement policies they view are in their interest. In principle, while it removes the incentives the system provides for non-compliance, retaliation does not punish. Unlike tort systems, in which damages are required in the event of breach, WTO remedies, *at worst*, leave plaintiff countries in the same position they were before the agreement. By revealed preference, when they choose to opt out and to sustain their violations despite retaliation, defendants are in a position that they prefer to compliance.

In the final analysis, members of the WTO have to make hard choices. If they wish to sign agreements to cover more complex forms of behavior, they will face greater risk in the form of legislative interpretations that they cannot control or anticipate. *But this risk has to be weighed against the benefits that they derive from extending the rules of the trading system to new areas and policies.* To be sure, these risks would be mitigated, first, by making sure that the draft language in agreements was clearer and, second, by speeding up the process of negotiating agreements so that errors could be more readily corrected and ambiguities clarified. But both these worthy suggestions are more easily said than done.

An individual who signs a contract does not forfeit his or her liberty. Similarly, WTO membership does not require countries to yield ultimate legal authority. WTO members do not lose their ability to determine their own laws when they join the WTO. The WTO also cannot coerce compliance. The organization has no police force that investigates violations and no judiciary that imposes penalties on its behalf. Members found to

violate an agreement do face consequences. Implementation problems aside, however, they are not punished.

But this is only the case if WTO remedies are allowed to operate as an escape clause. If, in fact, they are calibrated to “compel compliance” and applied punitively, countries could ex post actually be worse off. To those who believe that the institution’s rules reflect principles that, like codes of ethics, have a higher ultimate moral authority, this might not be a bad thing. But the gains from imposing compliance under existing agreements need to be weighed against the costs in discouraging future agreements and the toll such measures will take by fanning concerns that the WTO is undermining national sovereignty.