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# Challenges Facing the World Trade Organization

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The agreement establishing the World Trade Organization (WTO) entered into force on 1 January 1995. In many respects, the “new” trading institution is very much like the “old” General Agreement on Tariffs and Trade (GATT) regime, which had governed world trade since the late 1940s. The WTO embodies 50 years of multilateral trade negotiations in the GATT, which liberalized trade and established a substantial body of trading rules.

As a result of the agreements negotiated in the Uruguay Round, which addressed issues previously not covered by world trading rules (e.g., trade in services, trade-related investment measures, and intellectual property rights), WTO obligations apply to a larger share of global commerce than the GATT did. For this and several other key reasons, the WTO is different from its predecessor.

The most significant difference is the “single undertaking” of the WTO agreement. WTO members must accept all of the obligations of the GATT and its corollary agreements (with a few exceptions) negotiated in the Tokyo and the Uruguay Rounds.<sup>1</sup> Countries that formerly received the benefits of some GATT codes without having to join and undertake new obligations must now end their “free ride.” For many developing countries, the single undertaking commits them to substantially more trade obligations than previously required under the GATT regime. For the

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1. Four plurilateral accords apply only to their signatories and thus are not subject to the single undertaking. The most important of these pacts is the Agreement on Government Procurement; the others cover civil aviation, beef, and dairy products.

United States and other developed countries that already adhere to almost all the existing pacts, this requirement entails few additional WTO commitments. Coupled with a scaling back of special provisions for developing countries, the single undertaking helps meet a key objective of the Uruguay Round and the WTO regime: integrating developing countries more fully into the trading system.

Interestingly, the Uruguay Round negotiations, like the NAFTA, resulted in agreements in which the developing countries committed to substantially more trade liberalization than their developed-country partners. Essentially, the overall deal balanced liberalization of trade barriers by developing countries with new WTO rules that commit developed countries to maintain their open markets (along with partial reforms of some of their long-standing tariff and nontariff barriers). Given the much higher level of trade barriers in most developing countries, the asymmetry of these trade deals is likely to reemerge in the future, as long as developed countries demonstrate that they will follow the rules.

To be sure, the agreements that constitute the WTO trading rules allow asymmetric *implementation* of WTO obligations for developing countries and countries in transition to market economies (i.e., longer periods for them to fully assume those obligations). In addition, the poorest countries are exempted from some requirements. However, in most instances the transition period afforded developing countries before they assume full WTO obligations is relatively short.<sup>2</sup> Within a decade, the WTO will essentially eliminate the free-rider problem.

The second major difference between the GATT and WTO regimes is the dispute settlement mechanism (DSM). The WTO consolidates the various dispute provisions of the constituent GATT accords into a unified dispute mechanism and thus precludes the “forum shopping” and overlapping cases that sometimes occurred in the GATT.

As a result of the reforms agreed in the Uruguay Round, the new WTO dispute settlement mechanism also remedies other basic flaws of the previous GATT rules: the overly long delays from the establishment to conclusion of panel proceedings, the ability of disputants to block the consensus needed to approve panel findings and authorize retaliation, and the difficulty in securing compliance with panel rulings. WTO procedures now operate under strict time limits; countries cannot veto judgments against them; panel findings are subject to review by a new Appellate Body; and procedures are in place to promote timely compliance, to monitor compliance actions, and to allow retaliation in the event of noncompliance (Schott 1994, 125-29).

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2. The 11-year period for patent obligations involving agricultural chemicals and pharmaceuticals in the Agreement on Trade-Related Aspects of Intellectual Property Rights is the lengthiest and most contentious transition provision.

Because it is now difficult to block the adoption of panel rulings, the new Appellate Body is particularly important. It basically checks that panels do not overstep their authority or make mistakes with regard to issues of fact and law. It thus provides a safeguard against panel errors (both factual and jurisdictional) that would otherwise be automatically adopted under the new WTO procedures.<sup>3</sup>

The third distinction between the GATT and the WTO lies in the membership of the organizations. In the WTO, many more countries have either joined or are seeking membership in the organization than signed onto the GATT in the past, and more countries actively participate than did so under the GATT regime. As of 31 July 1996, the WTO had 123 members, and 31 other countries were in the process of acceding to it.<sup>4</sup>

The fourth difference involves the institutional structure of the two trade regimes. The GATT was a trade accord serviced by a professional secretariat; the WTO is a membership organization. This change is particularly important because the new institutional structure of the WTO provides greater legal coherence among its wide-ranging rights and obligations, including a unified disputes procedure (as noted above), and it establishes a permanent forum for consultations and negotiations on an ever-broadening agenda affecting global trade and investment in goods and services.<sup>5</sup>

In addition, the biennial ministerials mandated by the WTO agreement give political leaders an opportunity to provide useful direction to the work of the WTO. Unlike the past, when meetings of the world's trade ministers were few and far between and arranged on an ad hoc basis, regular sessions should help avoid delays in launching initiatives and implementing agreements. These systemic delays provoked concerns about the efficacy of the whole GATT process and contributed to the regeneration of protectionist pressures in major trading countries after each GATT round.

In sum, the WTO improves upon the GATT in terms of the content of the rights and obligations conferred on member countries, the number of countries participating, and its ability to promote trade negotiations

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3. In this regard, the Appellate Body essentially performs the same task as that envisaged by the proposed Dole Commission in the United States, whose "made in the USA" reviews to a large extent would cover the same ground as the WTO panel.

4. In comparison, the Protocol of Provisional Application (PPA) of the GATT had 8 "original signatories" in October 1947 (United States, United Kingdom, Australia, Belgium, Canada, France, Luxembourg, and the Netherlands), 23 countries signed the PPA in January 1948, 74 were members by the end of the Kennedy Round in 1967, 84 by the end of the Tokyo Round in 1979, and 91 at the start of the Uruguay Round in 1986 (*GATT Analytical Index* 1994, 1054-55).

5. In addition, the WTO makes permanent the Trade Policy Review Mechanism (TPRM), which provides regular monitoring of the trade policies of member countries.

and to process trade disputes among its members. As a result, the world trading system will be able to provide greater discipline over the \$5 trillion in annual trade in goods and services.

## The WTO and National Sovereignty

Some critics of the WTO equate the expansion of global trading rules with the loss of national sovereignty over trade policies. Does the acceptance of WTO obligations infringe the sovereignty of its member states?

International trade agreements confer rights to their signatories regarding the actions of other governments, but they also impose obligations and thus constrain a country's own actions. Countries accept these constraints because international trade accords provide beneficial bargains that strengthen their interests in world markets. Indeed, the very negotiation of trade accords is an exercise in the application of *national* sovereignty.

WTO signatories have delegated specific functions to the WTO and its secretariat involving the administration of the trading system. The WTO can rule on the conformity of national practices with the rights and obligations undertaken in the WTO, but member countries are then responsible for ensuring compliance (Croley and Jackson 1996). To be sure, WTO members have an obligation under *international* law to comply with the WTO rules, but the WTO itself has no means to force countries to honor those obligations.<sup>6</sup> Unlike other international bodies, WTO members explicitly did not establish supranational bodies with power to change laws or extract fines or other penalties from member countries.

Nonetheless, concerns about whether the WTO agreement infringes upon US sovereignty still resurface and merit a straightforward response. These concerns are based on two misperceptions: that the United States will be compelled to change its laws at the behest of WTO decisions and that majority voting by WTO members will rewrite the trade rules to the disadvantage of major trading powers.

If a US practice is found to violate US international obligations, the WTO *cannot* force changes in US law or regulations. To put it another way, WTO decisions are not self-executing in US law. In such a case, the United States can decide to bring its practices in compliance with its international obligations *or* affected WTO members have the right to demand compensation or to retaliate.<sup>7</sup> As argued by Jackson (chapter 9), WTO rules clearly favor the former approach for resolving trade disputes

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6. For example, countries do not have recourse to the International Court of Justice for GATT disputes, nor is there provision to expel members for bad behavior.

7. In practice, however, few countries ever retaliate against the United States because such actions impose costs on their own producers and consumers and sour relations with the world's largest trading nation.

but also sanction other remedial measures for redressing violations of WTO obligations.

Regarding the second point, as under the GATT, WTO decisions will normally be made by consensus (i.e., decisions become effective if no member officially objects). If a consensus cannot be reached, matters will be decided by majority vote. Votes were rarely taken in the GATT; if they do arise in the WTO, the WTO agreement includes important checks and balances to the voting rules that effectively institute a “big power” block on all but the most mundane WTO decisions and preclude majority votes from undercutting the rights of other participants.

## **WTO Report Card: The First 18 Months**

How well is the World Trade Organization working? The success of the WTO can be judged in part on how the organization is meeting its three basic responsibilities:

- to administer the new Uruguay Round accords and monitor compliance by WTO signatories;
- to demonstrate that world trade obligations are being enforced rigorously, objectively, and expeditiously;
- to reinforce support for global trade liberalization.

To date, the WTO generally has been performing these tasks quite well, despite its tight budget and small staff. The following subsections summarize the key results in each area.

### **Implementing the Uruguay Round Accords**

All the Uruguay Round accords are now up and running. In most instances, liberalization commitments are being fulfilled, the requisite domestic programs and practices have been notified to the WTO, and the new trading rules have been or are being implemented through changes in national law or regulation. In addition, negotiations on financial services, basic telecommunications, maritime services, and the movement of natural persons have been restarted. However, like most self-contained sectoral talks, they have produced or will likely yield a meager harvest (see discussion below).

To be sure, some countries have tried to “fudge” the calculation of their required reduction of import barriers, particularly in agriculture, and some notification deadlines have slipped. Indeed, the vast number of notification requirements (more than 200 in all) have created administrative burdens for many governments, and even the United States has

not fully complied with some provisions. In several cases, serious abuses have prompted conflicts that the new WTO dispute settlement mechanism is handling.

## Dispute Settlement Mechanism

Trading rules have little value unless they can be enforced. The dispute settlement mechanism provides a warranty that the bill of goods sold to participating countries during a trade negotiation will be dutifully delivered. For that reason, the effectiveness of the DSM is critical to the WTO's success.

Contrary to the concerns of some GATT critics, the WTO dispute settlement mechanism has gotten off to a good start (chapter 9). Four specific developments bear mention.

First, the WTO dispute settlement mechanism is being used. In its first 19 months (January 1995-July 1996), the WTO dispute settlement body has handled 51 requests for consultations. Many of these cases already have been resolved; the rest are subject to continuing consultations or panel review (table 1).

Second, a significant number of developed *and developing* countries are using the DSM. The United States has been the most active plaintiff, challenging foreign practices in 18 cases. Practices of the European Union (11), the United States (9), and Japan (8) have been the most frequent subject of consultations. Practices of developing countries have been brought to the DSM in 13 cases, including 4 challenges by other developing countries. Sixteen developing countries have initiated or joined in 20 cases challenging practices of other WTO members—some of which are major trading powers. Such actions indicate that developing countries believe that a rules-based system will protect them from unwarranted retaliation.

Third, the fact that the dispute settlement reforms ensure that decisions will be taken promptly and will not be blocked by disputants has encouraged countries to settle their differences bilaterally rather than await panel rulings. "Out-of-court" settlements have occurred in about one-third of the cases in which consultations have been initiated (including the US-Japan dispute over autos in the summer of 1995).

Fourth, the appeals process has worked. By coincidence, the first panel decision prompted the first appeal, which upheld the panel ruling on the WTO violation but rejected argumentation in the panel report that "would have narrowed the scope of an exception to international trading rules for measures relating to the conservation of exhaustible natural resources."<sup>8</sup> The balanced approach taken by the Appellate Body in its

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8. The case involved a complaint by Venezuela and Brazil that US regulations on reformulated gasoline were being applied in a discriminatory manner (Office of the US Trade Representative, press release 96-38, 29 April 1996).

inaugural case should reassure WTO members that panels will be neutral arbiters of whether national practices are consistent with WTO obligations.

Overall, the United States has used the DSM to successfully challenge numerous foreign trade practices, including various Korean measures affecting US farm exports and Japanese liquor taxes. Because the DSM has helped the United States achieve its goals in those cases, US officials have taken care to comply with DSM rulings affecting US practices, lest they weaken a system that amply benefits the United States. For example, the United States has agreed to comply with the few decisions that have gone against it, including a complaint by Venezuela and Brazil on reformulated gasoline. Further, consistent with WTO rules, the United States has withdrawn long-standing retaliatory duties against the European Union pending a DSM panel review of the EU import ban on hormone-treated meat.

One additional aspect of WTO dispute procedures should be noted. Disputes often arise over issues that fall in the gray areas of multilateral trade obligations. If prior negotiations failed to clearly define rights and obligations regarding an issue under dispute, then WTO dispute panels will have a difficult time ruling on the conformity of that issue with WTO obligations.

While expert panels could develop compromise solutions to pending disputes in such instances, there is understandable reluctance to adopt an approach in which panels could change or expand the interpretation of WTO provisions and thus alter the negotiated balance of concessions. In other words, panels cannot and should not “negotiate” new WTO rules through their deliberations. Indeed, Article 3.2 of the Dispute Settlement Understanding clearly states that “[r]ecommendations and rulings of the DSB [Dispute Settlement Body] cannot add to or diminish the rights and obligations provided in the covered agreements.”

Nonetheless, the DSM allows challenges to practices that “nullify or impair” benefits that a member would expect to receive from trade agreements, even if they do not violate WTO obligations. These nonviolation nullification and impairment (NNI) cases have been rare. In such cases, an NNI finding does not require that a country modify its practices, since it did not violate WTO obligations, but the country should offer compensation (chapter 9). Although they cannot call for changes in a country’s practices, panel reports in NNI cases can highlight problems that need to be resolved through new WTO obligations and thus help prepare WTO negotiations in new areas.

## **Ongoing Services Negotiations**

The Uruguay Round negotiations on services produced a solid framework of trading rules and obligations but yielded disappointing results with

**Table 1 WTO dispute settlement cases, January 1995-July 1996**

	<b>Disputed action</b>	<b>Complainant</b>	<b>Consultation requested</b>	<b>Panel established</b>	<b>Outcome</b>
DS-01	Malaysian prohibition of imports of polyethylene and polypropylene	Singapore	10 Jan 95		Settled: Malaysia withdrew measure.
DS-02	US standards for reformulated and conventional gasoline	Venezuela	24 Jan 95	10 Apr 95	Appellate Body report of 20 May 96 upheld 21 Feb 96 panel finding that US measures violated WTO rules. US has announced intention to bring these measures into conformity with the GATT.
DS-03	Korean measures for testing and inspecting farm products	US	4 Apr 95		Partially settled; new consultation request May 96 (to include new measures). Same as DS-02.
DS-04	US standards for reformulated and conventional gasoline	Brazil	10 Apr 95	31 May 95 (examined by same panel as DS-02)	
DS-05	Korean measures concerning the shelf life of products	US	3 May 95		Partially settled.
DS-06	Proposed US import duties on autos from Japan	Japan	17 May 95		Settled; Japan withdrew complaint.
DS-07	EU trade description of scallops	Canada	19 May 95	19 Jul 95	Settled after interim panel report; settlement circulated.
DS-08	Japanese taxes on alcoholic beverages	EU	21 Jun 95	27 Sep 95	Appellate Body report of 4 Oct 96 upheld panel finding of 11 July 96 that Japanese taxes were inconsistent with GATT Article III.
DS-09	EU import duties on cereals	Canada	30 Jun 95	11 Oct 95	Settled.
DS-10	Japanese taxes on alcoholic beverages	Canada	7 Jul 95	27 Sep 95	Same as DS-08.



DS-11	Japanese taxes on alcoholic beverages	US	7 Jul 95	27 Sep 95	Same as DS-08.
DS-12	EU trade description of scallops	Peru	18 Jul 95	11 Oct 95	Settled after interim panel report; settlement circulated.
DS-13	EU import duties on grains	US	19 Jul 95	11 Oct 95	Settled.
DS-14	EU trade description of scallops	Chile	24 Jul 95	11 Oct 95 (with DS-12)	Settled after interim panel report; settlement circulated.
DS-15	Japanese measures on purchase of telecom equipment	EU	18 Aug 95		Not pursued.
DS-16	EU importation, sale, and distribution of bananas	Guatemala, Honduras, Mexico, and US	18 Sep 95		Superseded by new consultation request in 1996.
DS-17	EU import duties on rice	Thailand	3 Oct 95		Settled.
DS-18	Australian import ban on salmon from Canada	Canada	5 Oct 95		After consultation, Australia is reevaluating import ban.
DS-19	Polish import regime for autos	India	28 Sep 95		Settled.
DS-20	Korean measures on bottled water	Canada	23 Nov 95		Settled.
DS-21	Australian import ban on salmonids	US	17 Nov 95		Consultations held mid-December 1995; Australia is reevaluating import ban.
DS-22	Brazilian measures on desiccated coconut	Philippines	27 Nov 95	4 Mar 96	Panel report circulated 17 Oct 96.
DS-23	Venezuelan antidumping case on certain oil country tubular goods	Mexico	5 Dec 95		Antidumping investigation had already been terminated.

**Table 1** WTO dispute settlement cases, January 1995-July 1996 (*continued*)

DS-24	US quotas on Costa Rican underwear	Costa Rica	22 Dec 95	5 Mar 96	Panel report expected mid-November 1996.
DS-25	EU implementation of Uruguay Round commitments on rice	Uruguay	12 Dec 95		Consultations held; case not pursued.
DS-26	EU import ban on hormone-treated meat	US	26 Jan 96	20 May 96	Panel report expected February 1997.
DS-27	EU regime for the import, sale, and distribution of bananas	US, Ecuador, Guatemala, Honduras, and Mexico	5 Feb 96	8 May 96	Panel report expected February 1997.
DS-28	Japanese measures on protection of sound recordings	US	9 Feb 96		Consultations held 4 Mar 96; further discussions in progress.
DS-29	Turkish import restrictions on textiles and clothing	Hong Kong	12 Feb 96		Consultations were scheduled, but Turkey failed to appear.
DS-30	Brazilian measures on desiccated coconut and coconut milk powder	Sri Lanka	23 Feb 96		See DS-22.
DS-31	Canadian import restrictions on certain periodicals	US	11 Mar 96	19 June 96	Panel report expected in early 1997.
DS-32	US measures on imports of women's and girls' wool coats (category 345)	India	15 Mar 96	17 April 96	Panel established on 17 Apr 96. Settled: US dropped the restraint.
DS-33	US measures on imports of woven wool shirts and blouses (category 440)	India	15 Mar 96	17 April 96	Panel report due early 1997.

DS-34	Turkish import restrictions on textiles and clothing	India	19 Mar 96	Consultations were scheduled, but Turkey failed to appear.
DS-35	Hungarian agricultural export subsidies	Argentina, Australia, Canada, New Zealand, Thailand, and US	27 Mar 96	Three rounds of consultations held.
DS-36	Pakistani patent protection for pharmaceutical and agricultural chemical products	US	30 Apr 96	Panel requested 4 Jul 96.
DS-37	Portuguese patent protection	US	30 Apr 96	Consultations held; Portugal will change its law; parties now drafting settlement.
DS-38	US measures pursuant to Cuban Liberty Act	EU	3 May 96	After three rounds of consultations, panel requested 3 Oct 96.
DS-39	US retaliation measures in EU hormone dispute	EU	17 Apr 96	EU requested panel. US withdrew measures on 15 Jul 96. EU not pursuing request.
DS-40	Korean laws, regulations, and practices in telecom procurement	EU	9 May 96	Settled.
DS-41	Korean inspection of agricultural products	US	24 May 96	Consultations held 20 Jun 96.
DS-42	Japanese sound recordings	EU	24 May 96	Consultations held 24 Jul 96 with US participation.
DS-43	Turkish taxation of foreign film revenues	US	12 Jun 96	Consultations held 25 Jul 96.

**Table 1 WTO dispute settlement cases, January 1995-July 1996 (continued)**

DS-44	Japanese consumer photographic film and paper	US	13 Jun 96	16 Oct 96	Panel report pending.
DS-45	Japanese distribution services	US	13 Jun 96		(GATS case) Consultations held 10 Jul 96.
DS-46	Brazilian export financing for aircraft	Canada	19 Jun 96		Consultations held July 96; revised panel request 3 Oct 96.
DS-47	Turkish import restrictions on textiles and clothing	Thailand	20 Jun 96		
DS-48	EU livestock and meat (hormones)	Canada	28 Jun 96	16 Oct 96	Panel report pending.
DS-49	US antidumping investigation on fresh and chilled tomatoes	Mexico	1 Jul 96		Consultations held 21 Aug 96.
DS-50	Indian pharmaceutical and agricultural chemical product patents	US	2 Jul 96		Consultations held 27 Jul 96.
DS-51	Brazilian auto import restrictions	Japan	30 Jul 96		Consultations held 13 Aug 96; attended by Japan, US, EU, Korea, and Canada.

Sources: World Trade Organization, USTR data.

respect to the liberalization of barriers to trade in several important sectors. Nonetheless, the General Agreement on Trade in Services (GATS) was accepted as part of the single undertaking, and WTO members committed to launch new negotiations by 1 January 2000 “with the view to achieving a progressively higher level of liberalization” (GATS Article XIX:1).

However, because of concerns raised by some countries (especially the United States) about the paucity of liberalization commitments in national schedules, Uruguay Round participants agreed to reopen negotiations for a limited period in several areas (including financial services, basic telecommunications, maritime services, and movement of natural persons). These talks were designed to allow countries to modify (and hopefully expand) their liberalization commitments—or to invoke exceptions to most-favored nation (MFN) status as permitted under the Annex on Article II Exemptions of the GATS.

To date, the three sectoral negotiations have produced modest results. The financial services talks stalled in late June 1995, when the United States stated that liberalization offers by other participants were insufficient to warrant committing to MFN treatment for all foreign firms in the US market.<sup>9</sup> Efforts by the European Union prompted a month-long extension in the talks, additional concessions from a few countries, and agreement by all parties to maintain their schedule of commitments until November 1997, when countries would have 60 days to improve or amend their offers, or invoke the MFN exemption of the GATS.<sup>10</sup>

The negotiations on basic telecommunications followed a similar path. By the late April 1996 deadline, talks yielded both liberalization commitments from a number of developed and developing countries and new draft regulatory principles regarding access to and use of the public telecommunications transport network. The principles, which are included in whole or part in many of the participants’ schedule of commitments, are particularly noteworthy since they commit governments to take measures (e.g., ensuring interconnection rights, setting up independent regulators) to prevent anticompetitive practices by major suppliers in their telecommunications market.<sup>11</sup> Here again, however, US negotiators found the national offers wanting, and talks were deferred until later in the year, with a new target completion date of 15 February 1997.<sup>12</sup>

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9. The US commitments in financial services filed on 30 June included MFN treatment for existing foreign participants in the US market but did not guarantee MFN treatment for new entrants. (For an explanation of the US position, see the article by Deputy USTR Jeffrey Lang and Treasury Under Secretary Jeffrey Shafer, *Financial Times*, 4 June 1995.)

10. See the text of the WTO decision on financial services issued on 24 July 1995 (published in *Inside U.S. Trade*, 28 July 1995, 19-20).

11. For the text of the draft regulatory principles, see *Inside U.S. Trade*, 26 April 1996, 10-11.

12. Petrazzini (1996) underscores the substantial welfare gains that would result from the successful resolution of the telecom talks.

The maritime talks held the least promise of success and met most expectations by making almost no progress by their target completion date of 30 June 1996. Unlike the other sectoral talks, there was little to salvage from the work of the negotiating group; WTO talks were suspended until the end of the decade and participants given until 28 July 1996 to amend their GATS commitments in this sector.<sup>13</sup>

To be sure, the issues covered by these sectoral negotiations are complicated, and the task of sorting through both the economic and political implications of new trade obligations is vexing, so expectations of quick results in these talks were unjustifiably optimistic. But the sectoral approach itself has a number of drawbacks. The architects of these talks seem to have based their design on two fragile assumptions.

First, they assumed that WTO members, especially high-growth developing countries in East Asia and Latin America, would open their markets to foreign competition to promote their development objectives.<sup>14</sup> While not unreasonable, it does not necessarily follow that those countries would “lock in” their domestic liberalization in WTO commitments in return for effectively no change in access to industrial-country markets. Thus, even if countries undertake domestic reform in their financial and telecom sectors, they have little incentive to use these “negotiating chips” in the current sectoral negotiations in the WTO.<sup>15</sup>

Second, the talks’ planners assumed that US negotiators did not mean what they said during the Uruguay Round regarding their unwillingness to undertake MFN *obligations* in these sectors if other countries did not offer US service providers improved access to their markets. Contrary to the rhetoric of some Geneva negotiators, the US position was generally consistent on this point throughout the Uruguay Round.

To date, many countries have not bound new liberalization in their WTO schedules in the GATS and have threatened to invoke Article II exemptions at the conclusion of the extended negotiation period. This situation does not reflect a lack of support for new liberalization efforts in the WTO, but rather demonstrates the tactical flaw of pursuing sectoral negotiations. For the most part, sectoral talks have succeeded, on either a bilateral or multilateral level, only in textiles and steel—and in these cases, the result was to raise barriers to trade, not lower them!

Far more promising are efforts under way in the GATS working group on professional services to develop sector-specific guidelines for certifica-

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13. For the text of the WTO decision on maritime transport services, see *Inside U.S. Trade*, 5 July 1996, 13.

14. Implicit in this assumption is the expectation that developing-country officials—unlike their industrial-country counterparts—would weigh “user” interests above the protectionist pressures of import-competing domestic industries.

15. In essence, the US threat to deny MFN treatment in its market had little sway on developing countries, which felt they had little to lose.

tion and licensing requirements. In this case, industry associations in participating countries are working together, along with their respective governments, to elaborate how GATS obligations should be applied and interpreted for their sectors. While these efforts have not received the publicity (or notoriety) of the other sectoral talks, the work on professional services demonstrates that the GATS can provide a useful framework for the development of multilateral disciplines that support the expansion of global commerce.

## Future Challenges

To maintain the credibility of the world trading system, WTO rights and obligations must continue to adapt to the new challenges arising from the increasing globalization of economic activity. To do so, WTO members need to both sustain the progress to date in implementing the results of the Uruguay Round and begin to address issues likely to dominate world trade in the 21st century. Four challenges deserve priority attention on the WTO agenda:

- promoting new trade liberalization initiatives, including the “built-in” negotiating agenda mandated by the Uruguay Round accords;
- expanding the WTO agenda to new issues (e.g., investment, competition policy, and trade-related environment and labor issues);
- ensuring the complementarity of regional and multilateral trade reforms;
- augmenting WTO institutional reforms.

WTO members must act quickly to launch initiatives in each of these areas. From past experience, we know that delays in starting new talks have often spawned a political backlash against multilateral reforms. Similar reactions already have surfaced, even though the Uruguay Round concluded just three years ago. The new threats to the trading system arise from:

- traditional efforts to maintain existing trade barriers and undo liberalization commitments or offset them with other protectionist measures;
- new strains of protectionism embedded in domestic regulatory practices;
- proliferating regionalism, which threatens to sap support for WTO initiatives and create new obstacles to multilateral liberalization.

The WTO should meet these challenges head on and dispel the doubts generated by recent services negotiations that it cannot solve these pressing problems.

## Promoting New Trade Liberalization

While the Uruguay Round achieved historic results, much work remains to liberalize the residual trade barriers that have survived eight rounds of GATT negotiations. Fortunately, WTO members already have a mandate, incorporated in the Uruguay Round accords, to undertake a broad range of new initiatives. Indeed, this so-called “built-in” agenda comprises more than 200 items. Many of these tasks involve reviews and refinements of the new WTO accords after several years of operations, but some require fundamental recommitments by WTO signatories to pursue new negotiations toward the progressive liberalization of trade barriers in politically sensitive areas such as agriculture and services.

Therefore, the first challenge facing the WTO is to refocus efforts on liberalizing barriers to trade in areas that have been resistant to past reforms and that generate constant friction among trading partners. In particular, WTO members need to address both tariff peaks in their national schedules (in specific industrial sectors and in agriculture) and restrictions on public procurement.

### Tariffs

While average nonagricultural tariffs in industrial countries generally will be reduced to low levels once the Uruguay Round cuts are fully implemented, many of these countries will still maintain exceedingly high tariffs in selected industrial and agricultural products. For example, tariff peaks in textiles and apparel and in electronics mar the tariff profile of the United States and the European Union, respectively. Furthermore, as a result of the tariffication of farm trade barriers in the Uruguay Round, the level of tariff bindings in agriculture is orders of magnitude higher. By 2000, EU bindings on dairy (178 percent) and sugar (152 percent), US bindings on dairy (93 percent) and sugar (91 percent), and Japanese bindings on dairy (326 percent) and wheat (152 percent) will still be in the stratosphere!<sup>16</sup>

Developing countries also have much to contribute to this liberalization process. To a large extent, trade concessions by developing countries in the Uruguay Round involved the acceptance of new trade rules and the binding of tariffs well above applied rates. These ceiling bindings allow these countries to increase their tariffs substantially, effectively offsetting

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16. See Hathaway and Ingco (1995) for details on other products.



(or worse) tariff reforms implemented in recent years.<sup>17</sup> Just as developed countries need to further reduce their peak tariffs, so too do developing countries need to reduce the gap between their bound rates and their currently applied rates.

## Government Procurement

Government contracts often represent a sizable share of domestic economic activity, yet public officials seem to disdain competition for this procurement so that the sales can benefit domestic firms and political allies. Despite rules to guide public tenders developed after two decades of negotiations in the Organization for Economic Cooperation and Development (OECD) and the GATT, few countries adhere to WTO disciplines in this area, and the obligations themselves are rife with exceptions.

For economic efficiency reasons alone, WTO members should devote more attention to liberalizing government procurement. Furthermore, because tenders for government contracts often are not subject to competitive bidding, they can provide fertile ground for corrupt practices.<sup>18</sup> It is inconceivable that such a large volume of economic activity in so many countries falls outside the trading rules.

## Expanding the Trade Agenda

The WTO will be pressed to deal with an increasingly broad array of issues that have not been traditionally associated with trade negotiations. Two sets of problems command immediate attention.

First, the reduction of border restrictions has refocused attention on domestic regulatory policies that can effectively block market access by impeding foreign investment or otherwise limiting competition. New WTO initiatives in the area of investment and competition policy will have to be considered that go beyond the charge in the Uruguay Round agreement on trade-related investment measures (TRIMs) to “consider” complementing that accord with new rules in these areas.

Second, the WTO needs to seriously address the nexus of trade and environment and trade and labor issues—both to highlight areas of immediate relevance to the trading system (e.g., transboundary pollution) and to reinforce support for WTO initiatives among important US and European political constituencies. Environmental issues have been the subject

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17. Indeed, Brazil sharply increased tariffs (especially in the auto sector) in 1995 to stem its burgeoning trade deficit, and Malaysia threatened to impose higher duties and/or quotas on nonessential goods in August 1996 because of its large current account deficit (*Financial Times*, 6 August 1996, 12).

18. For anecdotal evidence of such practices in Latin America, see *Latin Trade*, September 1996, 34-41.

of WTO discussions from the outset, and the new Committee on Trade and the Environment is charged with preparing recommendations for the Singapore ministerial meeting regarding the future WTO work program in this area. In addition, concerns about “social” issues such as labor rights, democratic reforms, and human rights have fueled demand for WTO consultations to determine whether—and, if so, to what extent—problems in these areas could be usefully addressed in WTO negotiations.

## Investment

The WTO needs to develop comprehensive investment rules to discipline countries’ deployment of carrots and sticks to induce industries to invest in their markets. The TRIMs agreement in the Uruguay Round provided a tentative first step in this regard, but much more needs to be done. In particular, WTO efforts in this area should focus on three sets of problems:

- the application of national treatment and MFN treatment to foreign investors and investments, and the reduction of national exceptions to these obligations;
- the strengthening of disciplines on investment incentives and establishment restrictions, which are not adequately addressed in the TRIMs accord;
- the integration of new WTO investment obligations with those in the GATS and the TRIMs accord.

Some countries may also want to raise the sensitive issue of national-security exceptions, which have become particularly contentious due to the controversy over the extraterritorial application of US sanctions. However, if this issue were to be raised, it would provoke legitimate concerns about WTO efforts to limit national sovereignty. Efforts to renegotiate WTO national-security exceptions would substantially erode US political support for the WTO and thus do more harm than good to the trading system.

WTO members should draw on efforts in other forums—including current talks in the OECD and investment accords under development in regional arrangements—to inform their work. In that regard, the NAFTA provisions on investment provide particularly good precedents for prospective WTO negotiations.

## Competition Policy

Most major industrialized countries have domestic competition policies. Common elements include prohibition of domestic cartels, price fixing, market share allocation, and surveillance of mergers and acquisitions. However, they differ significantly in such areas as transparency, remedies against infringement, and the extent of coverage.

As a result, the subject does not easily lend itself to common international rules since the conditions of competition may differ markedly both between countries and between sectors within an economy. Graham and Richardson (1996) highlight four problems that could complicate efforts to develop WTO rules:

- differences in national competition laws regarding which practices are deemed to enhance competition and promote economic efficiency;
- sectoral exemptions from national antimonopoly rules;
- absence or inadequate enforcement of national competition policies in many WTO signatories;
- implementation of other trade policies (e.g., antidumping) or regulatory measures that can act to constrain competition.

WTO members will have to sort through these issues to determine whether a WTO accord on competition policy is feasible and, if so, how broad or limited its coverage should be and how the WTO dispute settlement mechanism would apply. Clearly, much more work needs to be done in this area before WTO negotiations could be contemplated.

## Environment and Labor Issues

While environment and labor are not entirely new issues in the trade debate, there has been heightened concern that countries can gain unfair trade advantages through disregard for the environment or through unfair labor practices (particularly child labor). In some instances, trade restrictions have been imposed as a stick to prompt acceptance of environmental and social standards. Indeed, some multilateral environmental agreements (e.g., the Montreal Protocol on chlorofluorocarbons) condone the use of trade sanctions to enforce treaty obligations (Esty 1994).

On the other hand, trade measures designed to be environmentally friendly or to promote worker rights have occasionally masked protectionist motives. For example, developing-country concerns over such measures have been fed by their experience with the Generalized System of Preferences (GSP) programs, for which eligibility is conditioned in part on labor standards and human rights. WTO members need to examine the extent to which new international trade rules could resolve or mitigate problems in both these areas in order to lay the foundation for the negotiation of new WTO rights and obligations.

## Linking Regionalism and Multilateralism

Over the last decade, regional trade arrangements have proliferated, new pacts covering large geographic areas have been created, and established

regional groups have been revitalized. More than 60 percent of world trade is now covered by regional pacts (chapter 14), and almost all major trading nations are members of at least one large regional trade arrangement.<sup>19</sup>

In the past, regional pacts generally reinforced multilateral trade initiatives, and the trade diverted by regional preferences was more than offset by the trade created by the increased growth resulting from these regional groups. Indeed, in some cases liberalization initiatives in one region were immediately emulated in another to ensure that those countries kept pace in the global competition for foreign investment. The most important example of such “competitive liberalization” among regions occurred in 1994, when the commitment by the Asia Pacific Economic Cooperation (APEC) forum to free trade and investment in the region by 2010/2020 at its Bogor, Indonesia, meetings in November was followed three weeks later by the declaration of the Summit of the Americas to negotiate a Free Trade Area of the Americas by 2005 (chapter 14).<sup>20</sup>

Nonetheless, the size and complexity of the new arrangements reopen questions of whether regionalism will now hamper multilateral trade liberalization. Not only do the new pacts discriminate against nonmember countries, but the evolving crazy quilt of trading rules and customs regulations required to implement the preferential trading arrangements increase transactions costs for both members and nonmembers—and may constitute important new barriers to market access (e.g., industry-specific rules of origin).<sup>21</sup>

WTO obligations seek to promote the complementarity of regional and multilateral trade objectives. However, the rules are vague or incomplete and thus subject to abuse. In particular, GATT/WTO reviews of regional pacts allow significant sectoral exceptions (e.g., agriculture), skirt problems caused by contingent protection measures (especially antidumping duties) and rules of origin that often significantly distort trade and investment flows between the region and third countries, and fail to track regional pacts after they are signed, when transition provisions or rule changes can significantly affect market access for third-country suppliers.<sup>22</sup> Thus, even if regional pacts follow the letter of WTO law, they can still pose obstacles to the trade of third countries. Countries need to revisit WTO rules and procedures regarding regional pacts to ensure that they

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19. For a review of the growth of regional trading arrangements, see WTO (1995).

20. Competitive liberalization was also pursued by individual countries in the 1980s. Leading examples include Australia, Chile, and Mexico.

21. However, the largest regional group, APEC, has explicitly avoided such discrimination in its actions to date.

22. This latter problem may be mitigated by the work of the new WTO committee on regionalism, which was established in late 1995 to improve surveillance of regional pacts.

continue to remove rather than erect roadblocks to further multilateral trade reforms.

## **Augmenting WTO Institutional Reforms**

The Uruguay Round accords strengthened the structure of the multilateral trading system. However, the growing demands that those accords place on the trading system, as well as the rapidly expanding membership in the WTO, will likely require additional institutional reforms if the WTO is to manage and administer the new trading rules and procedures effectively. Three problems merit immediate attention.

First, the WTO faces significant resource constraints. The WTO staff and budget both pale in comparison with those of other international organizations.<sup>23</sup> Governments clearly have not distributed resources commensurate with the responsibilities accorded these respective organizations. The small size of the WTO Secretariat already strains its ability to conduct legal and economic analysis. Staffing constraints also will inevitably limit the scope of joint activities that might be undertaken with other international economic institutions, particularly cooperative efforts with the International Monetary Fund (IMF) and the World Bank to help promote “greater coherence in global economic policymaking.”<sup>24</sup> Such efforts are particularly needed to assist countries in transition in order to fully integrate them into the world economy.

Second, expanding membership will place additional pressures on the WTO’s management structure, which, unlike other international membership organizations, is directed by a council comprising all current members. Both the IMF and the World Bank have an executive board to direct the senior officers of the organization, with permanent participation by the major industrial countries and weighted voting. Attempts to form a small executive body in the WTO, including proposals put forward in the Uruguay Round, were unsuccessful, and smaller WTO members remain strongly opposed to the concept. Consequently, the United States and other major trading countries continue to resort to ad hoc, extralegal processes such as the Quad (the United States, European Union, Canada, and Japan) to fill the void. This situation is already controversial and will become increasingly untenable as WTO membership expands to politically powerful entrants such as China and Russia.

Third, the process of admitting new members to the WTO needs to be standardized. Current procedures are cumbersome and often duplicative.

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23. For example, the WTO budget is less than half that of the OECD or the International Labor Organization.

24. This initiative was mandated by signatories of the Uruguay Round accords in a declaration signed at Marrakesh, Morocco, in April 1994.

In many cases, WTO working parties could benefit from work done on the economy of candidate countries by staff at the World Bank and the IMF. Finally, as is evident from the long history of negotiations with China, some accession talks become overly politicized and thus further complicate the negotiation of protocols of accession by raising foreign policy as well as economic issues.

## The Next Step

The Singapore ministerial in December 1996 provides the first opportunity for WTO member countries both to take stock of the progress achieved to date in getting the WTO up and running and to elaborate a WTO work program to guide members of the trading system as they approach the 21st century. Both tasks are crucial to maintain the credibility of, and political support for, the WTO.

To that end, the Singapore ministerial should begin to develop a strategy for addressing the multiple and diverse challenges facing the trading system. Not all of these problems need be resolved at that meeting, but ministers should at least begin preparations for WTO consultations and prospective negotiations in these areas. The success of the new trading regime will rest in large measure on how well WTO members address those challenges.

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