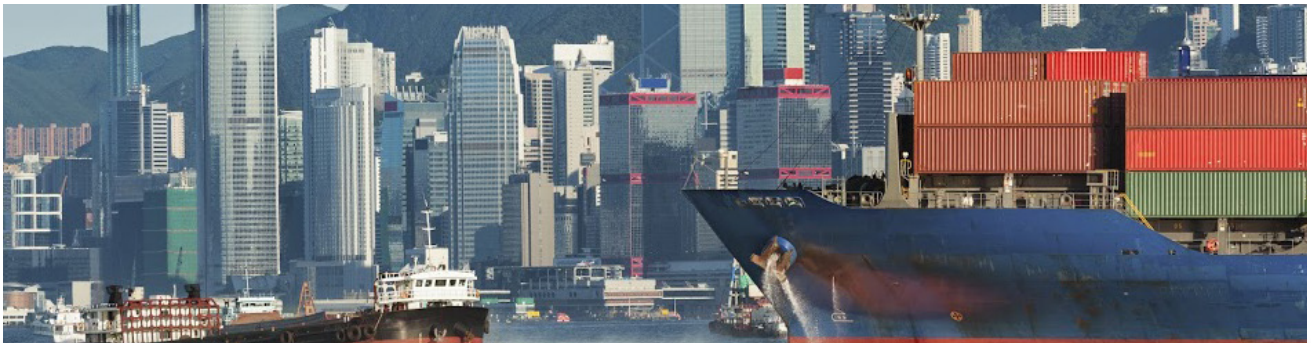




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STRENGTHENING THE GLOBAL TRADE SYSTEM



Will the WTO have Functional Value in the Mega-regional World of FTAs?

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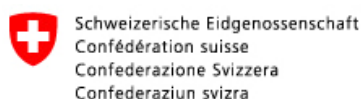
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ABSTRACT

If all mega-regional trade and economic integration projects under negotiations are successfully completed, it would see the most important international goods, services, and investment transactions of the participants comprehensively covered by preferential free trade agreements. Even more significantly, all the agreements are focused on dealing with the behind-the-border regulatory and other issues that are of greater concern to business in the 21st century. Most of these behind-the-border questions would be addressed through so-called "WTO-plus" commitments, meaning that they either deal with issues beyond the scope of today's WTO coverage or take a WTO-covered subject and employ a different approach that produces a superior result in a regional agreement. The central question explored in this paper is whether the WTO could be expected to retain a meaningful functional value for its members in the soon-to-be-realized world of WTO-plus mega-RTAs. There is no possibility of stopping the mega-regional juggernaut at this point in time, so developments on that front must be taken as a given, as well as assumptions for the future. This means that the change has to take place in the WTO if the institution is to survive. That said, the WTO of the future will almost certainly be a different WTO than we see today.

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LIST OF ABBREVIATIONS

APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
CRTA	Committee on Regional Trade Arrangements
DSU	Dispute Settlement Understanding
EU	European Union
GDP	gross domestic product
FDI	foreign direct investment
FTAs	free trade agreements
ICSID	International Centre for Settlement of Investment Disputes
IP	intellectual property
MFN	most favoured nation
NAFTA	North American Free Trade Agreement
NAMA	Non-Agricultural Market Access
OECD	Organisation for Economic Co-operation and Development
RCEP	Regional Comprehensive Economic Partnership
RTA	regional trade agreement
SOEs	state-owned enterprises
TBT	Technical Barriers to Trade
TPP	Trans-Pacific Partnership
TTIP	Trans-Atlantic Trade and Investment Partnership
US	United States

INTRODUCTION

The negotiation of a Trans-Atlantic Trade and Investment Partnership (TTIP) agreement between the United States (US) and the European Union (EU) would create an integrated market accounting for 40 percent of global gross domestic product (GDP). The bilateral trading relationship is the world's largest, with the US annually exporting USD 458 billion in goods and services to the EU and buying 17 percent of EU goods exports and 25 percent of EU services exports. The stock of foreign direct investment (FDI) that the US and EU have in each other's markets amounts to USD 3.7 trillion.

The Regional Comprehensive Economic Partnership (RCEP) negotiations aimed at producing a regional trade agreement (RTA) grouping Association of Southeast Asian Nations (ASEAN) members with China, Japan, Korea, India, Australia, and New Zealand would cover 50 percent of the world's population, 30 percent of global GDP, and 25 percent of global exports.

The Trans-Pacific Partnership (TPP) negotiations, assuming they one day reach the goal of an Asia-Pacific Economic Cooperation (APEC)-wide RTA, would cover 40 percent of global trade, including 60 percent of US merchandise exports, and 39 percent of the country's services exports. The decision by Japan to join in the negotiations and recent expressions of interest by China in the project greatly increase the potential economic value of the TPP as well as its potential to attract additional participants in the near future.

In addition to these projects, the EU and Japan have launched comprehensive trade and investment negotiations and the leading countries of Latin America's Pacific rim have initiated regional talks aimed at consolidating an Alliance of the Pacific—a market integration effort that would amount to the ninth economy of the world.

These are all mega-regional trade and economic integration projects, which, if successfully completed, would see the most important international goods, services, and investment transactions of the participants comprehensively covered by preferential free trade agreements (FTAs). Even more significantly, while the agreements promise to eliminate tariffs, all are focused on dealing with the behind-the-border regulatory and other issues that are of greater concern to business in the 21st century. Most of these behind-the-border questions would be addressed through so-called "WTO-plus" commitments, meaning that they either deal with issues beyond the scope of today's WTO coverage or take a WTO-covered subject and employ a different approach that produces a superior result in a regional agreement.

The WTO system is generally considered to have three principal functions—liberalizing international trade in goods and services through multilateral trade negotiations; overseeing the implementation of the system of multilateral trade agreements; and settling disputes among WTO Members where those disputes relate to "covered agreements." The central question explored in this paper is whether the WTO could be expected to retain a meaningful functional value for its members in the soon-to-be-realized world of WTO-plus mega-RTAs.

An important caveat is in order at this point. The proponents of the mega-regionals have promised much in their characterization of the new trade pacts as 21st century trade agreements. To qualify as such, the new agreements will need to go beyond what has been negotiated regionally in the past. For now, we will assume that the ambitious objectives of the TPP, TTIP, and others will be met, and that agreements with these characteristics will be the comparator with what is on offer in the WTO. Obviously, if the mega-regionals fail to attain the objectives set for them, we will be looking at a different (and less satisfactory) international reality.

THE MEGA-REGIONAL PROBLEM FOR WTO

What do business people and policymakers in economies where international trade and investment are important want from trade agreements in the 21st century? Naturally enough, they want to participate in agreements that deliver real additional access to key markets, remove discrimination from regulatory environments, and improve and guarantee the legal safety of their valuable commercial rights and investments.

Against this background, does the WTO system deliver—particularly when judged against the mega-regionals?

LIBERALIZATION AND ACCESS TO MARKETS

The failed Doha Round of multilateral trade negotiations certainly calls into question whether the WTO can any longer deliver on liberalization and market access. But even if the Round had not failed, would it really have produced new access to markets? Probably not. There is so much "water" in most WTO Members' bound tariff rates that even huge cuts would not affect real market access. The bound Australian tariff for automobiles is 40 percent ad valorem, compared to a currently applied rate of 5 percent. The December 2008 modalities for the Non-Agricultural Market Access (NAMA)

negotiations suggest the use of a "Swiss formula" with a coefficient of 8 for developed countries—which would cut Australia's bound rate for automobiles to 6.7 percent—with no improvement in access. For a developed country with average MFN tariffs around 4.5 percent, post-Round tariff averages would still be 2.9 percent—scant improvement to access.

In the case of market access for agricultural products, the last version of the Doha Round modalities was so riddled with exceptions, exemptions, special product and sensitive product designations and safeguards that it is a sure bet that the result of the negotiations would not have produced increased access for any agricultural products other than those which countries had to import because they did not produce them at home.

In the agriculture negotiations, there are roughly 620 six-digit HS tariff lines from Chapters 1 to 24 that are subject to market access modalities. Under these modalities, developed countries would be able to completely exempt 37 lines from liberalization and developing countries could exempt up to 162 tariff lines from cuts. Worse still, there would be multilateral acquiescence that the exempted items are justifiably "sensitive" or "special"—seriously compromising future efforts to liberalize trade in these products.

The situation is no better for services trade, where it is generally recognized that WTO Members' scheduled services commitments reflected the status quo at the end of negotiations 20 years ago in 1993 and where the offers tabled in the Doha Round rarely came close to matching the commitments the same countries were prepared to make in regional negotiations.

Modern 21st century mega-regionals have a WTO-plus approach to liberalization and market access. Generally, the objective is tariff elimination—although this may be phased-in in some cases and occasionally subject to special transitional safeguards. For services trade, the mega-regionals tend to follow the "top-down" or "negative list" approach, which is both far more liberalizing and much more transparent than the "bottom-up" approach dictated by the WTO General Agreement on Trade in Services (GATS) agreement.

So, even if the Doha Round had not failed, there is no reason to believe that the WTO would have been perceived to have delivered on its liberalization/market access function. This is particularly true when those potential Round results are looked at in relation to the expected outcomes of the mega-regionals.

IMPLEMENTATION OF SYSTEM AGREEMENTS

It could be argued that the WTO Councils and Committees have done a reasonably good job of overseeing the implementation of the existing WTO agreements and arrangements—but that would be based essentially on a static view of the world and whether the disciplines agreed in 1993 should have been expected to evolve and improve over time.

Viewed from the standpoint of a trading enterprise, some of the most important agreements in the multilateral system are addressed to critical questions such as product standards, conformity assessment, quarantine regulations, customs procedures, and intellectual property protection. Unfortunately, in most cases, these existing agreements tend to reflect what could be agreed on as a "lowest common denominator" and, for a variety of reasons; they tend not to impact on real, specific border and behind-the-border problems and regulatory issues.

The difference between the WTO and the WTO-plus approach of mega-regionals can be illustrated by two of the objectives for the TTIP listed by the Acting US Trade Representative in his 20 March 2013 letter to Congress.

- Seek to build on key principles and disciplines of the WTO Agreement on Technical Barriers to Trade through strong cross-cutting disciplines and, as appropriate, through sectoral approaches, to achieve meaningful market access, and establish ongoing mechanisms for improved dialogue and cooperation on TBT issues.
- Seek greater compatibility of US and EU regulations and related standards development processes, with the objective of reducing costs associated with unnecessary regulatory differences and facilitating trade, inter alia by promoting transparency in the development and implementation of regulations and good regulatory practices, establishing mechanisms for future progress, and pursuing regulatory cooperation initiatives where appropriate.

Once the US and EU begin to use the TTIP to set the standards and cement an approach to regulatory coherence, that will be their template for their future relations with non-TTIP members in the rest of the WTO. With the template thus set, the influence of others will be minimized, no matter what is said in the general principles of the Technical Barriers to Trade (TBT) and other agreements.

And it is not just the TTIP. Similar "regulatory coherence" objectives characterize the TPP negotiations in the Pacific. Current Geneva-centered activity in the implementation of WTO agreements does not come close to matching such ambitious objectives in these areas of real practical concern to the people who actually engage in international trade.

What the mega-regional negotiators have appreciated is that the world has moved on from 1993 and whether you are discussing TBT or customs procedures or other areas where WTO-plus has become a part of modern trade agreements, we need to see the possibility of concrete results on discrete problems affecting trade—not just a respect for the principles of multilateral agreements.

DISPUTE SETTLEMENT

It is often argued that notwithstanding the explosion of RTAs over the past two decades, the trading system will always need the WTO because it has shown itself to be very effective in the management of dispute settlement. It is certainly true that relative to other international tribunals, the WTO Dispute Settlement Understanding (DSU) system has been a great success story. But whether or not the WTO's dispute settlement function and its attractiveness to its members can stand up to the challenge from the mega-regionals and their WTO-plus elements in the future depends on the answers to a few important questions.

First, will the mega-regionals be successful in terms of their hoped-for country coverage or will important WTO Members be left out of these new arrangements? Second, will the WTO system be able—in the reasonably near future—to expand its “covered agreements” to include the topics dealt with today only in RTAs and the mega-regionals? Third, will the dispute settlement mechanisms of the mega-regionals be seen as robust as the WTO DSU system we have benefitted from in the post-Uruguay Round period?

If all major trading countries—and bearing in mind that not all countries that are in positions of influence in the WTO today are major trading countries—are covered in the next few years by WTO-plus mega-regionals, then it is quite possible that the functionality of the WTO DSU would be called into question.

Why do major trading powers like the US and the EU abide by the outcome when they lose disputes to the likes of Costa Rica and Ecuador in the WTO? It is because they do not want their big trading partners to accuse them of bad faith if they do not, in which case the system will start to break down. But one needs to wonder whether the same incentive to live up to WTO dispute settlement rulings will be there if a WTO Member can depend on effective dispute settlement with its most important partners through a mega-regional agreement's dispute settlement system.

The bigger problem is that the demise of the Doha Round has demonstrated that the functionality of the WTO's DSU is certain to be compromised to a very important degree by the shortcomings of the system in terms of its limited “covered agreements.” We already know that investment disputes must go to other bodies like the World Bank group's International Centre for Settlement of Investment Disputes

(ICSID). Other questions, like North American Free Trade Agreement (NAFTA) trade remedy disputes, have specific avenues of resolution expressly limited to the RTA's own procedures.

Finally, the mega-regionals under negotiation are likely to bring on board some of the innovative developments in dispute settlement that have evolved since the end of the Uruguay Round. For example, some FTAs allow for the imposition of monetary fines on offending governments in place of trade retaliation. The WTO system needs to account for developments like this.

WHAT CAN WTO HOPE TO DO TO REMAIN RELEVANT?

We have so far looked at the principal functions of the WTO and how these functions might well be undermined by developments on the mega-regional front. The discussion shows that the problem for the WTO is not limited to the failed Doha Round's inability to deliver on liberalization and market access but in fact is more generalized—likely affecting all three of the WTO system's main functions. It is about much more than the Doha Round.

A great deal of effort has gone into the GATT/WTO system over the years and it would be a great pity if it were to become irrelevant due to its failure to address current challenges to its viability. We need to be conscious of the fact that the extra-WTO mega-regional environment is evolving at an accelerating pace and if we are not already out of time to save the WTO, we are rapidly approaching the point where it could be too late. So what can be done? There is no possibility of stopping the mega-regional juggernaut at this point in time, so developments on that front must be taken as a given, as well as assumptions for the future. This means that the change has to take place in the WTO if the institution is to survive. That said, the WTO of the future will almost certainly be a different WTO than we see today.

WTO-PLUS ELEMENTS OF MEGA-REGIONALS

A starting point in the discussion of potential responses is to understand what the challenges for the WTO are in terms of the WTO-plus elements of the new mega-regional trade agreements. Leaving aside for now the assumed impracticality of 159 WTO Members agreeing to follow the mega-regional approach to market access (that is, going to free trade in

goods and services), and using the stated objectives of the TTIP as a basis for the discussion, WTO Members need to try to meet the challenges of mega-regionals in the following areas.

Investment: All the mega-regional projects will have an important focus on FDI, including the RCEP negotiations to which India is a party. WTO Members made a serious mistake in 2004 when as part of the so-called framework agreement they stopped work on investment in Geneva. In the TTIP, investment negotiations will seek to establish a national treatment regime that eliminates artificial or distorting barriers to investment and an agreement that provides meaningful procedures for resolving investment-related disputes.

Competition policy and consumer protection: The objectives of the TTIP include addressing matters of mutual interest on competition policy and process, and improving cooperation on competition policy, as well as in e-commerce-related consumer protection initiatives.

Regulatory coherence and convergence: This is about TBT and Sanitary and Phytosanitary (SPS) measures but also more. As already noted, the mega-regionals aim to eliminate barriers that exist just because partners have historically chosen different ways of achieving the same shared regulatory objectives. Mutual recognition arrangements and cooperation in the development of new standards and conformity assessment procedures can go a long way to achieving the objective of regulatory coherence.

Trade facilitation: Even if a new WTO agreement on trade facilitation was reached, it would not be the same as what we see in mega-regionals where the emphasis is on concrete measures to speed border crossings and reduce the red tape associated with international trade. Trade facilitation, of course, is perhaps the single most important thing governments can subscribe to if they want to make it possible for their producers to link to global value chains.

Electronic commerce: Agreements like the TPP and the TTIP will contain provisions designed to facilitate the use of electronic commerce, including through commitments not to impose customs duties on digital products; procedures for authentication of electronic transactions; electronic filing of customs documentation; and setting the rules for international data flows.

Government procurement: This is an area where the WTO commitments apply to only a very limited number of members. In most modern 21st century agreements (and certainly in all the mega-regionals), government procurement markets are recognized as major opportunities that need to have rules guaranteeing fair, transparent, and predictable conduct of purchases by participating governments. In the WTO, there are not even any GATS procedures for services procurement, but services are normally covered in RTAs.

Intellectual property rights protection: The TRIPS agreement dates from 1993. Developments in technology, particularly in copyright for digital products, have led to the need for new protections not afforded adequately by TRIPS. Existing and future RTAs recognize this problem and deal with it through updated WTO-plus protections for intellectual property (IP).

State-owned enterprises: The negotiation of rules to set globally relevant disciplines on state trading enterprises, state-owned enterprises (SOEs) and designated monopolies appeared as an issue for the first time in the TPP negotiations and has been (wrongly) interpreted by some as being aimed at China and its multitude of SOEs. The issue is broader than China and the TPP and features as an objective of the TTIP as well.

Other areas: Provisions addressed to labor standards and environmental protection are also likely to feature in the mega-regionals under negotiation. Since there is no “root” to these questions in existing WTO agreements, we will leave them aside for the moment—but without prejudice to the reader’s consideration whether their treatment in the WTO materially affects the WTO’s ability to function effectively in the future.

POTENTIAL RESPONSES

In some respects, it is probably already too late to save the functionality of the WTO from the impact of mega-regional trade agreements. This is almost certainly the case when one looks at trade liberalization and real improvements to market access, especially when one looks at the backward-moving proposals contained in the Doha Round draft modalities for market access in agricultural trade. That said, there are probably some things that WTO Members could consider doing if they want to preserve some credibility in the system, post-mega-regionals.

In the next—and final—section of this contribution, I will try to explain why I think we must accept that the nature of the WTO in the future must change in some fundamental respects, compared to the 20th century institution created in 1995. Before coming to that discussion, I would like to revisit a couple of points made in an earlier paper on a related topic. These points relate to the need to at least initiate a dialogue in the multilateral system on the WTO-plus elements now so prevalent in RTAs and foreseen for the mega-regional projects.

Kati Suominen has proposed the creation in the WTO of an “RTA Exchange” that could help make the best out of RTAs in the interest of the global trading system. She has suggested that such an exchange could serve as a clearing house and forum where all matters related to RTAs and their practices could be discussed among all WTO Members. The exchange could also help to transfer best RTA practices from one RTA to another. In an era of mega-regionalism, this could be

particularly important for new RTAs among smaller groupings to ensure that their practices align with those of the major trading powers.

I have previously backed a very similar idea and drawing on that earlier contribution I believe that participation in the exchange should also be open to both global and regional organizations and groupings with experience in dealing with WTO-plus issues. The discussion would be enriched by the participation of the Organisation for Economic Co-operation and Development (OECD), regional development banks, regional UN economic commissions, and the secretariats of the APEC, ASEAN, and regional economic cooperation agreements in Africa and Latin America. Recognizing that the business community is the natural constituency for action on these behind-the-border measures, some form of participation by relevant international business groupings should also be facilitated. The creation of the exchange would be without prejudice to discussion of these topics, as appropriate, in existing WTO bodies, including the GATS and TRIPS Councils, the Committee on Trade and Development, and the Committee on Regional Trade Arrangements (CRTA). In fact, these specialized committees and councils should be encouraged to develop inputs to the discussion in the exchange.

In his contribution to this project, Robert Lawrence has suggested that RTAs, especially the mega-regional RTAs of the future, might be usefully subjected in the WTO multilateral impact assessments (akin to environmental impact assessments required for major projects in many countries). To my way of thinking, this idea could be sensibly added to the RTA Exchange-type proposals that both Kati Suominen and I have raised in other think piece papers.

But WTO Members have to buy into these ideas and embrace them recognizing the constructive spirit in which they are advanced. They need to understand that the functionality of the institution is at stake and act accordingly.

Establishing a dialogue on the mega-regionals and their attendant WTO-plus issues in Geneva on this basis would add to the credibility of the organization by demonstrating that WTO Members are supportive of a multilateral discussion designed to enhance coherence between trade agreements negotiated regionally and bilaterally and that Members are capable of responding to the challenges of today. Even better, if a multilateral discussion led to harmonized approaches, then the exercise would facilitate the eventual multilateralization of key parts of RTAs, including mega-regionals. If we could reach agreement that these would be the objectives of the exercise, why should any WTO Member raise an objection to such an "exchange"? But this will merely help to keep the WTO relevant in a changed role from that which was originally envisaged for the organization. As we look to the future, we need to realize that, for better or worse, the functional utility of the WTO will be different than it has been in the past.

CONCLUSION AND RECOMMENDATIONS

The WTO has to accept that it has to proceed in the future on the basis of something other than the single undertaking. WTO members should recognize that the WTO of the future will necessarily be different from the WTO of the past. In this connection, and in the spirit of a constructive contribution, I offer the following recommendations for consideration by WTO Members.

MARKET ACCESS AND TRADE LIBERALIZATION

- In a new era of mega-RTAs and proliferation of RTAs more generally, we should accept the fact that real market access is effected through RTAs and not through multilateral agreements. The exception to this should be accession negotiations of new members of the WTO that (obviously) need to commit to trade liberalization as a part of the accession process.
- The Doha Round is dead. Over the years—and particularly since the framework agreement in 2004—the trade liberalization "modalities" of the Round have become so distorted that they are a real step backwards and the sooner they are buried and forgotten the better.
- No future attempts at trade liberalization through a "single undertaking" process should be considered at the WTO.

CONDITIONAL MFN AND CRITICAL MASS PLURILATERALS

- If the Doha Round has demonstrated anything, it is that the WTO's membership now precludes the idea of moving forward with negotiations based on a one-size-fits-all approach. This means that any progress on rules-based questions (my comments above explain why I do not believe this works for market access) should be on the basis of conditional most favoured nation (MFN) and critical mass plurilateral agreements.
- If WTO Members do not accept that future rules-related agreements should be negotiated on this basis, they must recognize that they will be driving all such activity into the RTA and mega-regionals context.

RTA EXCHANGE AND IMPACT ASSESSMENT

- As explained above, it is critically important for the future relevance of the WTO that it initiates a meaningful multilateral dialogue on the issues and commitments developed in the context of today's RTAs and tomorrow's mega-regional agreements.
- One important objective of such an exercise should be to try to gauge the impact of future mega-regionals on the multilateral system (and its functionality).
- Another objective of the exercise should be to develop shared understandings of ways in which problems can be best addressed and the creation of some shared views on best practice approaches that might be "multilateralized" at some future date.

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