

THE CENTRAL ROLE OF THE WTO IN THE WORLD TRADING SYSTEM

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In 1947, a trade agreement called the General Agreement on Tariffs and Trade (GATT) was signed by 23 nations. Its lasting impact may not have been clear to its creators at the time. It was supposed to be part of a larger project called the International Trade Organization, but that institution was rejected by the U.S. Congress a couple of years later and never came into force.

The GATT could have been just another trade agreement that was surpassed by subsequent trade agreements. Instead, it became permanent, with new elements added over time, and was expanded to cover many new countries. In 1995, the GATT was transformed into the World Trade Organization (WTO), the overarching framework of rules that governs today's world trading system.

Like most trade agreements, the WTO consists of individual elements that cover a range of trade policy issues: tariffs, agriculture, domestic regulations, services, government procurement, and intellectual property, among others. Just as important, however, it is an institution. Early in the GATT era, a Secretariat was established to oversee the GATT's functioning. That Secretariat has continued under the WTO and is a key element of the WTO's

success in a number of areas. The WTO is far from being any kind of “world government,” but through its rules and its staff, it offers an international framework for promoting and managing freer trading relationships among most of the world's countries.

FUNDAMENTAL IMPORTANCE OF THE WTO

As bilateral, regional, and plurilateral trade agreements proliferate, it may seem that the WTO's role has diminished over time. However, there are several aspects of the trading system's liberalization that only the WTO has accomplished—or in some cases even could have accomplished—in comparison with preferential trade agreements. What follows are some key areas in which the WTO is vital and that make it unlikely that the system will be either replaced or abandoned.

Tariff Reductions and Trade Liberalization for Everyone. Free trade agreements (FTAs) make a lot of headlines these days. Hundreds of bilateral, regional, and plurilateral trade agreements are now in existence, and it seems as though there is always a new one being negotiated. Despite their number, however,

The Index of Economic Freedom includes coverage of every WTO member and observer except Andorra and the Holy See. While the European Union enjoys special status by joining its constituent countries as a full member of the WTO, the Index limits its EU coverage to individual EU member states.

WORLD TRADE ORGANIZATION AGREEMENTS

AGREEMENTS	DESCRIPTION
General Agreement on Tariffs and Trade (1947)	The legal framework that established the modern World Trade Organization as we know it. It has allowed for the removal of barriers to trade in an effort to build a more fair international trading system between members.
Agreement on Agriculture	Reduces domestic support for agricultural produces like export subsidies and limited market access. Also addresses issues of food security, environment, and concerns of developing countries.
Agreement on the Application of Sanitary and Phytosanitary Measures	Increases transparency for the trade of plants and animals produced with certain additives like pesticide. Prevents governments from restricting imports based on overtly restrictive additive rules.
Agreement on Technical Barriers to Trade	Removes non-tariff restrictions on trade like standards, testing, and certifications for products. Eases the regulatory process for trade between members.
Agreement on Trade-Related Investment Measures	Removes barriers to investment between members that could restrict or distort trade. This includes allowing members' equal treatment for investment as well as restrictions on local content requirements.
Agreement on Implementation of Antidumping	Limits members' ability to apply antidumping measures without first going through a sufficient investigation at the World Trade Organization.
Agreement on Implementation of Customs Valuation	Normalizes the customs value of imported goods between members.
Agreement on Preshipment Inspection	Ensures governments cannot excessively use preshipment inspections to restrict the outflow of trade.
Agreement on Rules of Origin	Increases transparency and a long-term standard for the trade of goods originating from certain areas that is not excessively restrictive.
Agreement on Import Licensing Procedures	Increases the information required, and the amount of restrictions applicable, for import licenses.
Agreement on Subsidies and Countervailing Measures	Establishes a more definitive definition and rules for subsidies for industry groups and the level of countervailing duties against imports.
Agreement on Safeguards	Sets limits on members' ability to enact safeguard measures to protect domestic industry from import competition.
General Agreement on Trade in Services	Establishes an equal treatment for services across members.
Agreement on Trade-Related Aspects of Intellectual Property Rights	Establishes rules and disciplines around the protection of intellectual property including a dispute settlement.
Understanding on Rules and Procedures Governing the Settlement of Disputes	Strengthens the existing dispute settlement system to enable members to litigate and resolve issues over other agreements.
Trade Policy Review Mechanism	Establishes a periodic review for members and whether they are upholding the various agreements.
Agreement on Trade in Civil Aircraft	Removes tariff and non-tariff barriers to civil aviation trade.
Agreement on Government Procurement	Increases transparency and non-discrimination for the goods and services purchased by members.

SOURCE: World Trade Organization, "Legal Texts: the WTO Agreements," https://www.wto.org/english/docs_e/legal_e/ursum_e.htm (accessed September 27, 2019).

Table 1  heritage.org

these agreements do not cover all of the trading relationships covered by the WTO.

The GATT started with 23 “contracting parties,” but over the years, the accession process, with the assistance of the Secretariat, added many more. Most trade agreements remain static in their membership; the WTO has grown tremendously. The WTO now has 164 members, and many more accessions are underway. That means the WTO covers the trading relationship between each member and 163 other members.

At its core, the GATT/WTO has always been about trade liberalization. For each WTO member government, there have been commitments to reduce tariffs. “In eight rounds of negotiations between 1947 and 1994,” as a leading WTO textbook explains, “the average level of tariffs imposed by developed countries on industrial products was brought down from over 40 per cent to less than 4 per cent.”¹ In addition, for each WTO member government, there is a commitment not to use domestic regulations and taxes to discriminate against foreign goods.

The WTO provides an overarching framework of general principles and specific obligations that applies to the trading relationships of almost the entire world, including all of its major economies. FTAs can supplement that, but they cannot replace it.

Most Favored Nation Principle. One specific principle that FTAs cannot offer is most favored nation (MFN) treatment. This principle means that countries agree to treat all other WTO member countries equally in relation to trade. For example, if a government commits to lowering its automobile tariffs to 2.5 percent, it must charge that same rate to all countries rather than discriminate among them with a variety of rates. Along the same lines, where it has domestic regulations (for example, in the area of food safety), it commits to applying those regulations to all of its trading partners in the same way.

In contrast to this, FTAs are fundamentally at odds with the MFN principle. By their very nature, FTAs discriminate in favor of some countries and against others. They offer lower

tariffs to the FTA partners than they offer to other countries. They represent preferential trade rather than free trade.

While FTAs violate the MFN principle, WTO rules do allow FTAs, provided they meet certain conditions, as an exception, but the conditions in this exception act as a constraint on the development of sectoral trade alliances through FTAs. Only deep FTAs (or customs unions) that cover substantially all trade are allowed; sector-specific arrangements are prohibited. FTAs also must focus on lowering internal barriers between the partners rather than raising barriers to trade with outsiders. Without such constraints, FTAs could undermine the whole enterprise of multilateralism, and the trading system could see a downward spiral toward trade alliances and greater conflict.

Dispute Settlement Understanding. The WTO’s dispute settlement system is currently under attack. Nonetheless, for the past several decades, it has been the international trade dispute mechanism of choice for resolving trade conflict. As of this writing, in the years since the establishment of the WTO in 1995, under the Dispute Settlement Understanding (DSU), 586 complaints have been filed, in addition to which there have been 242 panel rulings, 141 appellate rulings, and 51 arbitration rulings. By contrast, the hundreds of FTAs in existence have led to only a handful of complaints. The most active non-WTO dispute mechanism has been the NAFTA’s, but in 2000, the United States blocked the appointment of a panel, and no panels have been set up since then.² When countries have complaints about trade barriers, they generally go to the WTO for resolution.

One of the key reasons for the WTO dispute settlement system’s continued success is the existence of an independent Secretariat to manage the process. Two divisions of the WTO Secretariat provide primary assistance to the panels, and a separate Secretariat assists the Appellate Body, the standing group of seven appellate “judges” who hear appeals of panel reports. The role of the WTO staff is crucial in making sure panels are appointed when needed,

as well as providing administrative and legal support in handling complex litigation. For FTA disputes, parties have to figure out the process from scratch each time. At the WTO, by contrast, an efficient and effective system is already in place for every dispute that might arise.

The DSU has been successful in part because it strikes a good balance between enforcement and flexibility. It strongly encourages compliance with panel and Appellate Body rulings, but it does not force governments to take actions that are politically infeasible. If a government is found to have violated WTO obligations, it can choose not to change its policies and instead accept retaliation from the complainant. In this way, the balance of commitments is maintained.

Disguised Protectionism Jurisprudence. The DSU has dealt with a wide range of issues, but there is one in particular where clarifications by panels and the Appellate Body have been helpful: the rules on disguised protectionism, such as those in GATT Article III, paragraphs 2 and 4, or the agreements on Technical Barriers to Trade and on Sanitary and Phytosanitary Measures. These provisions explain in broad terms that domestic regulations and taxes are not to be used to protect domestic producers of goods from foreign competition. How to apply these rules to specific government measures, however, is not always straightforward.

Over the years, WTO panels and the Appellate Body have applied these obligations in specific cases in a way that has provided a great deal more certainty about the boundaries. In cases where the tax or regulation explicitly treats foreign goods worse than similar domestic ones, the protectionism is obvious, but sometimes the discrimination is implicit. For example, a Chilean law that taxed liquor products on the basis of alcohol content looked neutral on its face. However, the panel and the Appellate Body were able to figure out that most foreign goods had a high alcohol content, most domestic goods had a low alcohol content, and the true purpose of the law was thus to protect domestic producers.³

In theory, cases of disguised protectionism could be handled in an FTA if one applies between two countries, but because of the well-developed jurisprudence under the DSU, the WTO has become the natural place to hear these cases.

Obligations on Trade Remedies and Subsidies. While there is a great deal of overlap in the coverage of the WTO and FTAs, there are certain policy areas for which the WTO has extensive disciplines but that FTAs do not cover and are unlikely ever to cover. Two of particular significance are trade remedies and subsidies.

“Trade remedies” refers to certain tariffs and other measures that can be used in response to both “unfair” and “fair” trade that causes or threatens economic injury to domestic producers. These measures include antidumping and countervailing duties and safeguards. Such remedies may be politically necessary in order to get trade deals completed, but they are potentially subject to abuse by domestic industries seeking protection from foreign competitors. What the WTO rules in this area do is offer a set of procedural and substantive rules that help to prevent this protectionist abuse.

Over the years, trade remedies have been one of the main subjects of WTO dispute settlement. Of the 586 complaints that have been initiated under the DSU, 196 have been related to trade remedies. In such cases, without the WTO disciplines, it would be much more difficult to keep the often disguised protectionism of trade remedies in check.

As for subsidies, the WTO provides general constraints on the use of subsidies for goods. It specifically prohibits export subsidies and domestic content subsidies, and it also has obligations related to any subsidies that cause “adverse effects” (loosely speaking, economic harm to foreign competitors). In addition, through the WTO’s Agreement on Agriculture, governments have made commitments not to provide subsidies to designated products beyond a certain amount, and these amounts are subject to reduction commitments over time.

Unlike tariffs, which can be applied on a country-by-country basis, subsidies have a broad

effect on all trading partners. As a result, they are not likely to be disciplined through FTAs.

Transparency. Many of the WTO's benefits, like those described above, are well known, but others are more subtle and receive less attention. One that gets less acclaim than it should is the transparency on laws, regulations and other trade measures that the WTO provides. It does this in a number of ways.

First, through several specific obligations, the WTO requires governments to publicize and notify all of their measures that might affect trade so that other governments will be aware of them. In this regard, Article X, paragraph 1 of the GATT requires the publication of a wide range of measures:

Laws, regulations, judicial decisions and administrative rulings of general application... pertaining to the classification or the valuation of products for customs purposes, or to rates of duty, taxes or other charges, or to requirements, restrictions or prohibitions on imports or exports or on the transfer of payments therefor, or affecting their sale, distribution, transportation, insurance, warehousing inspection, exhibition, processing, mixing or other use, shall be published promptly in such a manner as to enable governments and traders to become acquainted with them.⁴

In addition, each of the individual WTO agreements on particular subjects requires that the covered measures be notified to the WTO.

However, publication and notification are not the end of the story. The WTO has a number of committees where governments meet to discuss measures that have been notified and raise concerns about their trade effects. In this way, many trade conflicts can be resolved without reaching the formal dispute stage.

Finally, the WTO periodically conducts country-specific "trade policy reviews" of each member. During these reviews, governments provide detailed information on their trade policy actions and respond to questions from other governments. With assistance from the Secretariat, this is a very useful exercise that allows governments to enhance their understanding of

each other's trade policies and raise issues outside of the more contentious litigation process.

CURRENT CRISES AT THE WTO

Despite all of these benefits, it is clear that not all is well with the WTO. After the immense success of the Uruguay Round, which led to the establishment of the WTO, expectations were high for the future. However, protests at the 1999 Seattle Ministerial Conference and the failure of the Doha Round talks launched in 2001 have caused a great deal of angst about the future of the WTO as a negotiating forum. There have been some successes, such as the Trade Facilitation Agreement, but broader liberalization has remained elusive.

One source of problems is the broader membership that exists today and the growing power of certain middle-income countries, which makes agreement harder to reach. In the past, agreement among the United States, the European Union, Japan, and Canada might have been enough to bring the rest of the membership along and serve as the basis for a deal. Now, though, China, Brazil, India, and others have to be on board as well. Some have suggested that perhaps the WTO negotiations should focus on plurilateral agreements by which countries willing to move forward can do so on their own without having to seek others' consent. E-commerce and services are two areas where attempts are being made, but the success of this approach has not yet been demonstrated.

In addition, the Trump Administration has put forward several serious criticisms of the existing system, and it is not clear at this point how these issues should be resolved.

- **Role of the Appellate Body.** In the view of the United States, the Appellate Body—the WTO's appeals "court"—has been engaged in "judicial activism" (exceeding its mandate in various ways) and has deviated from the agreed upon rules. The Bush and Obama Administrations voiced some criticisms of the Appellate Body on this basis and blocked the reappointment of certain appellate "judges," substituting new judges

in their place. The Trump Administration has ratcheted up the criticism and tactics and has refused to appoint any new judges until its concerns are addressed. As a result, by the end of 2019, there may not be enough judges to hear new appeals.

- **Notifications.** The United States has expressed concern that some countries (China in particular, but many other developing countries as well) are not properly notifying their laws, regulations, and other measures and has proposed harsh penalties for governments that fail to notify properly.
- **Development Status.** The United States believes that some countries are claiming developing country status without a proper basis, thus allowing them to avoid taking on their fair share of commitments. The United States would like to apply objective criteria to determine whether a country should be classified as developing rather than letting it be purely a matter of self-selection as it is now.

These issues have put the future functioning of the WTO in a state of uncertainty. With regard to the Appellate Body crisis, which is the most serious and pressing issue, other WTO members have responded with various reform

proposals, but none of these has satisfied the Trump Administration. The Administration has insisted that the system should reflect the rules as written in 1995 but has not put forward its own ideas about how to achieve that. In all likelihood, there will be workarounds that members can adopt, such as agreements not to appeal a case or the use of *ad hoc* arbitrations for appeals, but the potential disappearance of the Appellate Body poses a real threat to the dispute settlement system.

CONCLUSION

The WTO is a fundamental and foundational part of the world trading system. U.S. Trade Representative Robert Lighthizer, although a long-time critic of the WTO, has emphasized its importance: “The WTO is a valuable institution, and offers many opportunities for the United States to advance our interests on trade. As I have said before, if we did not have the WTO, we would need to invent it.”⁵ Bilateral and regional FTAs can supplement the WTO, but they cannot replace it.

Nevertheless, no organization or set of rules is ever perfect. The current crises at the WTO represent an opportunity to address some weaknesses and concerns about its functioning. A good-faith effort on all sides should lead to a strengthening of the WTO in order to preserve its place at the center of the world trading system.

ENDNOTES

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