Uphill Battle for WTO Reform Toward MC12

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Status Quo of WTO & Need for "Modernisation"

The World Trade Organization (WTO), which has been the cornerstone of the free trade system since its establishment in 1995, now faces its greatest crisis as it approaches its 30th anniversary. The Doha Round, launched in 2001, has effectively come to a stop, with its only notable outcome being the 2014 adoption of the Agreement on Trade Facilitation, which went into effect in February 2017. As for plurilateral agreements by groups of like-minded members, there has been success in updating the Information Technology Agreement (ITA) and the Agreement on Government Procurement (GPA), but negotiations on new agreements such as the Trade in Services Agreement (TiSA) and Environmental Goods Agreement (EGA) have stalled. It has become obvious to everyone that the rule-making function of the WTO has declined.

This situation stems from the fact that its members are increasingly stratified and diversified, resulting in the growing complexity of their respective interests. Today, two-thirds of its members are developing countries. It had already become evident 20 years ago, at the third ministerial meeting in Seattle, that the GATT 1947 decision-making process, still dominated by the developed countries with the Quad – the United States, EEC, Japan, and Canada – in the lead, no longer worked. The turn of the century has seen the rise of the BRICs. China and Russia joined the WTO in 2001 and 2012 respectively. Today, these state capitalism states and emerging economies have a major presence.

A quarter of a century after its entry into force, the WTO agreements have become outdated as a result of the deterioration of the WTO's rule-making function. Agricultural products and natural resources aside, the production lines of most products, from smartphones to jumbo jets, are no longer confined within national borders but are manufactured through the worldwide division of labor that we call the global supply chain (GSC). And goods and services are not the only things that move between the production bases in the GSC. The free, cross-border movement of capital, people, knowhow, and data is essential to this process. But there are no WTO agreements on digital trade or direct investment, and liberalization of the movement of natural persons has only been achieved in a limited manner under the General Agreement on Trade in Services (GATS). The focus of rule-making has shifted to mega-regions under agreements such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), EU-Japan Economic Partnership Agreement (EPA), and the (currently under negotiation) Regional Comprehensive Economic Partnership (RCEP), while the WTO declines in importance.

In addition, WTO rules assume market economies as its players; state intervention in the market is considered the exception. But the rise of state capitalist nations led by China means that this assumption no longer holds in the real world. Some of the US frustration with the WTO's Appellate Body stems from the fact that the unfair trade advantages that China creates through state-owned enterprises (SOEs) cannot be regulated through the interpretation of the rules in force. As the trade dispute between the US and China shows, this has been one of the reasons why the US is having recourse to self-help in the form of unilateralism.

The WTO has been more successful in executing and monitoring the rules in force. WTO members have the treaty obligation to notify the WTO secretariat of the trade measures that they take. This notification is then examined in detail by the committees and councils with jurisdiction as well as by the Trade Policy Review Body (TPRB). This multilateral monitoring has worked to prevent the adoption of protectionist trade policies. The WTO's dispute settlement system has mandatory jurisdiction and juridical procedures. It is held in high esteem as one of the most successful international dispute settlement mechanisms, which is manifested by the 590 cases filed since the establishment of the WTO. The accumulation of precedents under the panels and the Appellate Body has clarified the provisions of the agreements, and enhanced stability and predictability in international trade under the WTO.

However, this enforcement and monitoring system is also showing increasing signs of institutional fatigue. The dispute settlement procedures in particular are in dire straits, with the Appellate Body on the verge of paralysis. The crown jewel of the WTO is losing its luster.

Main Agendas & Discussions Among WTO Members

This situation has given rise to a growing movement for WTO reform ("Modernisation") led by the European Union. In the summer of 2018, the EU reached summit-level agreements with the US and China respectively on the necessity of WTO reform. Meanwhile, it worked to produce a proposal for reform during the spring and early summer of the same year, and published it as a concept paper in

September (http://trade.ec.europa.eu/doclib/press/index.cfm?id=1908). Canada also supported this initiative, hosting a meeting of a small number of the like-minded members (Ottawa Group) in the same year in Ottawa, where it published a discussion paper on WTO reform (WTO doc. JOB/GC/201). The Ottawa Group has met this year during the World Economic Forum's annual meeting in Davos in January and the OECD Ministerial Council Meeting in May. The Trilateral Meeting of the Trade Ministers of the US, EU, and Japan also agreed at its fourth meeting in September 2018 on the necessity for WTO reform.

As for broader venues including developing countries, the APEC summit held in Papua New Guinea in November 2018 failed to produce a joint communique – the first time that such a thing had happened – because of a clash between the US and China over WTO reform. However, an agreement was reached the following month at the G20 Buenos Aires summit to support WTO reform. At the G20 Osaka summit in June this year, the Ministerial Statement on Trade and Digital Economy listed specific issues regarding WTO reform and committed to their resolution, and the Leaders' Declaration endorsed this.

At the WTO, discussions on reform have been moving forward since the autumn of 2018, as members have been submitting specific proposals on the respective issues to the General Council and other WTO bodies. The main items on the agenda and the current state of the discussions are as follows.

Dispute Settlement Procedure

It is indisputable that the reform of the dispute settlement process is of the greatest urgency. The US claimed in its 2018 Trade Policy Agenda and 2017 Annual Report that the Appellate Body was adding to or diminishing rights and obligations under the WTO Agreement in violation of the provisions of the Dispute Settlement Understanding (DSU) and criticized this exercise of its powers as "overreach". Specifically, the US questions the Appellate Body's routine disregard for the mandatory 90-day deadline for its final report, its assertion of *stare decisis* for its reports, which has no legal basis in the DSU, and its issue of *obiter dicta* and advisory opinions that are not necessary to resolve the dispute.

Consequently, the US has prevented the nomination of replacements for vacancies since the summer of 2017. The number of Appellate Body members is currently down to three, the minimum necessary to comprise a division to hear an appeal. The terms of two members will elapse on Dec. 10, pushing the Appellate Body to the brink of suspension. DSU reform is truly an urgent challenge.

So far, the EU, Honduras, Taiwan, Thailand and others have submitted amendment proposals in response to US concerns. However, the US has shown almost no interest in these and has merely been repeating its position that they should revert to the DSU agreed to in 1994, leaving the discussion at an impasse. The EU in particular, while sharing US concerns, has also submitted a joint proposal with China and India to enhance the independence of the Appellate Body (WTO doc. WT/GC/W/753). There is a significant gap between the view of the US and the EU regarding the degree of judicialization of the WTO dispute settlement procedure.

Institutional Issues: Regular Work & Transparency

An important role of the WTO as an administrative organization is to secure transparency, serving as a clearing house. It has members submit notifications concerning trade measures according to their obligations under the WTO Agreements, based on which the councils and committees examine on a regular basis the trade measures of the respective countries and their implementation. However, this obligation to notify is not being adequately complied with, making it difficult for the WTO subsidiary bodies to conduct this regular work.

On improving transparency, the EU, Japan and the US submitted a joint proposal on notification procedures in November 2018 (WTO doc. JOB/GC/204/rev.2 (revised version as of June 2019)). According to this proposal, a member that fails to file a notice one year past the deadline would be sanctioned in principle. The member would be ineligible to elect chairpersons of committees and the like, ordered to increase its contribution to the WTO, and suffer other disadvantages. Developing countries oppose securing compliance with notification obligations with sanctions. In June 2019, six developing country members including India and South Africa proposed the implementation of notification obligations based on inclusiveness that take the resource limitations of developing countries into consideration (WTO doc. JOB/GC/218).

As for activating councils and committees and making them more efficient, 11 members including Australia, the EU and China, submitted a joint proposal for procedural guidelines in July this year. This proposal covers preparations for meetings, procedures for discussions on trade issues, and procedures for informal resolutions by chairpersons of issues that are raised (WTO doc. WT/GC/W/777/Rev.1).

Special & Differential (S&D) Treatment & Developing Country Status

In the WTO, there are many provisions that provide "special & differential" (S&D) treatment to developing country members, exempting them from some of the obligations under the respective agreement. In addition, developed countries have adopted preferential tariff systems under which tariffs on imports from developing countries are reduced or eliminated altogether to improve their market access.

However, this developing country status is based on self-designation, and even China, the country with the second-largest GDP in the world, is treated as a developing economy in the WTO. Meanwhile, developing countries include the Democratic Republic of Congo, Liberia, Niger, and Zimbabwe, the poorest countries of the world, some even called "failed states". The developed countries are reluctant to place them in one bundle to be given preferential treatment as developing countries. The US in particular makes no effort to hide its strong dissatisfaction. In February this year, it offered a proposal for an objective standard for receiving S&D treatment. According to the US proposal, OCED member countries, G20 participants, and high-income countries according to World Bank standards, for example, will not receive S&D treatment in ongoing and future negotiations. The main developing countries have reacted harshly against this proposal (WTO doc. WT/GC/W/764).

Because of this, the US suspended preferential tariffs for India in June 2018. India fought back by imposing a tariff increase on US products, a measure of questionable WTO consistency. Finally, US President Donald Trump announced that unless the WTO's current system that uses self-designation for developing country status was amended within 90 days from July 26, the US would no longer treat countries that the USTR determined inappropriate as developing countries in the WTO.

Meanwhile, in October 2018, Taiwan announced that it had renounced its developing economy status on its own initiative. South Korea has also decided to voluntarily abandon its self-designated developing country status in future negotiations.

New Substantive Rules: Digital Trade, Fishery Subsidies & Others

As the Ministerial Declaration from the WTO's Tenth Ministerial Conference (MC10) in Nairobi in December 2015 shows, developing countries support the continuation of the Doha Round because they support its goals, which emphasize development, while developed countries are reluctant because the negotiation agenda, which had been established on the basis of the priorities at the time the round was launched in 2001, is out of date. The substantive rules of the WTO, in the 25 years of its existence, have become outdated. There is an urgent need to create rules that match economic realities. Discussions on the new, post-Doha trade issues of the WTO have begun to gather momentum.

Rules for digital trade in particular are a topmost priority for WTO members, given their indispensability to the movement of big data in the GSC. Some 71 willing and able members issued a joint declaration on digital trade rules at MC11 in Buenos Aires in December 2017. Following so-called "exploratory work" for serious discussions to identify elements that could be included in an agreement and issues that could arise in the negotiations, a meeting of the like-minded members on the occasion of the annual meeting of the World Economic Forum in Davos in January 2019 confirmed their intent to begin negotiations, effectively launching the process for a new agreement. At the G20 Osaka summit in June this year, a Leaders' Special Event on Digital Economy was held, where the "Osaka Declaration on Digital Economy" was issued, and the 27 participating states including the G20 members signed on to the Osaka Track, an initiative to promote efforts on rule-making on digital trade in the WTO. Since the commencement of negotiations in the WTO, Japan and other important players such as the US, the EU, Canada, Brazil, and Singapore have introduced draft texts, leading to intensive discussions.

However, the key players are wide apart in their positions. The US places importance on the free cross-border movement of data and seeks to achieve the "Three Freedoms" including a ban on source code disclosure demands and a ban on demanding data localization. These principles have already been incorporated in all agreements initiated by the US including the CPTPP, the US-Mexico-Canada Agreement (USMCA), and the newly agreed US-Japan Digital Trade Agreement. China, on the other hand, demonstrated a cautious position regarding free movement of cross-border data movement in the position paper that it submitted to the WTO in April this year. China regulates the outbound transmission from China of personal information and important information designated by law. Its fundamental orientation is incompatible with that of the US. Meanwhile, the EU places absolute priority on protecting personal information through general data protection rules (GDPR) and regards the freedom of data movement as a secondary concern.

India has a significant presence in information technology but is not one of the willing and able.

The G20 Leaders' declaration in Osaka took up "Data Free Flow with Trust (DFFT)" and gained the support of the participants including the US, China, and the EU. However, this apparent consensus on data free flow hides many differences. "Trust", in particular, means that from the government perspective for China, and that from the individual's perspective for the EU, while it is an empty word without substance for the US.

Negotiations on a fisheries subsidies agreement continues as an agenda item from the Doha Round. Negotiated as part of the Rule Negotiations in the Doha Round, the talks had stopped as the overall round stalled. However, the UN Sustainable Development Goals (SDGs) were adopted in 2015, in which agreeing on regulating subsidies that lead to illegal, unreported and unregulated (IUU) fishing as well as overcapacity and overfishing was set as a target. This gave new life to negotiations, and an agreement was reached at the MC11 in Buenos Aires in 2017 to aim at adopting an agreement by the next ministerial conference. However, the key participants have not been able to agree on the most important issue, which is how to regulate IUU fisheries subsidies. Moreover, views have not moved towards consensus on the introduction of S&D treatment provisions for developing countries. The US and China in particular are at odds as to whether China should be able to invoke this exception by self-designation. India has also been a tough and outspoken defender of S&D treatment, and claimed a broad range of exemptions from subsidy restrictions for developing countries.

Efforts also continue at the Trilateral Meeting of the Trade Ministers of the US, EU and Japan, which was launched in December 2017, to strengthen regulation of industrial subsidies and to create new rules on forced technology transfer with China in mind. Specifically, at the third meeting in May 2018, a Scoping Paper on Industrial Subsidies and a Joint Statement on Technology Transfer Policies and Practices were adopted. The scoping paper is an agreement on the necessity of developing more effective rules on subsidies to improve transparency, strengthen regulation of public bodies and state-owned enterprises (SOEs), and set a new list on prohibited ("red") subsidies. The Third Meeting also reached agreement on a Joint Statement on Technology Transfer Policies and Practices, which expressed concern over forced technology transfer to host countries through such means as joint ventures, foreign investment regulation, technology license contracts, and support for cybertheft through improper access. In light of this development, China expressed its concern over the discriminatory treatment of SOEs in subsidies regulation and investment examination for security purposes in its May 2019 proposal for WTO reform (WTO doc. WT/GC/W/773).

From Osaka to Nursultan: a Way Forward

The negotiations concerning these agendas touched upon above clearly and implicitly target agreement or substantial progress at the MC12 in Nursultan, Kazakhstan, in June 2020. Reform of the dispute settlement procedures is of even greater urgency, since the Appellate Body will be unable to operate as early as December 2019. But the prospects are grim.

No WTO member disputes the need for reform and the revival of the multilateral free trade system. For example, the Osaka G20 Communiqué committed all the participating countries to such goals as "keep[ing] our markets open", "a free, fair, [and] non-discriminatory ... trade and investment environment", and "a level playing field". However, to China, which enjoys the fruits of the free trade system under the current WTO regime, the word "free" must shine red and bright, but to the US the words "fair" and "level" must loom in bold, capital letters.

This state of affairs indicates that although no one disagrees that meaningful reform of the WTO is an urgent challenge, countries have different interests in mind. There are no prospects for an end to the heated conflict between the US and China. More generally, the gulf between developed countries and developing countries remains stark, leaving little likelihood that a high-level multilateral consensus will be created in the WTO, at least any time soon. JS

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