

## Twin crises in the WTO, and no obvious way out

Bernard Hoekman and Petros C Mavroidis\*

Pause for a moment. Assume that, by magic wand, the Trump Administration changes its attitude, and agrees to new appointments to the Appellate Body (AB). Have the WTO problems disappeared simply because a complete AB is now in place? Even if matters such as Rule 15 are addressed,<sup>1</sup> the distinction between facts and law is clarified and a resolution is found to concerns regarding the AB overstepping of its mandate, we are left with the fact that new trade agreements are being routinely negotiated outside the confines of the WTO, leading enforcement to migrate elsewhere. Is the AB crisis simply a case of missing judges or should it be viewed as symptom of a wider crisis hitting multilateralism, even if the causes for the latter are distinct?

We argue against the commonly held view that the AB crisis would *ipso facto* be over, if the United States (US) were to change its mind, and move to complete the AB membership. This view ignores both the perceptions of many insiders that the operation of the dispute settlement system needs to be improved, as well as, crucially, the broader challenges confronting cooperation in the WTO. The increasing shift to bilateral, regional and plurilateral forms of cooperation will have an impact on WTO dispute settlement even if the AB were to be reconstituted. The

\* Bernard Hoekman is Director of the Global Economics research area at the Robert Schuman Centre for Advanced Studies of the European University Institute. Petros C Mavroidis is the Edwin B Parker Professor of Foreign and Comparative Law at Columbia Law School. This note draws on B Hoekman, PC Mavroidis, *Preventing the Bad from Getting Worse: The End of the World (Trade Organization) As We Know it?* (Mimeo 2020).

<sup>1</sup> Rule 15 of the Working Procedures for Appellate Review reads ‘A person who ceases to be a Member of the Appellate Body may, with the authorization of the Appellate Body and upon notification to the DSB, complete the disposition of any appeal to which that person was assigned while a Member, and that person shall, for that purpose only, be deemed to continue to be a Member of the Appellate Body.’

WTO has not managed to add much to its legislative arsenal since its creation. Besides a few sector-specific agreements in the realm on goods and services negotiated in the late 1990s, the only comprehensive agreement it managed to conclude since 1995 is the Agreement on Trade Facilitation. The legislative function of the multilateral trading system is... well, in crisis.

The wider crisis (malfunction of the legislative branch) is, of course, the next frontier. It should be kept in mind, but it is not the priority for now. For now, the WTO should concentrate on the narrower, and easier to solve crisis: the AB crisis.

The WTO dispute settlement system – compulsory third-party adjudication – long held to be the crown jewel of the multilateral trading system, is in crisis, potentially endangering the future of the organisation. This is the result of the US blocking new appointments to the AB as the terms of sitting members expired. The official justification is that the US is unhappy with the performance of the AB. At the time of writing, the number of AB members stands at one, making the appeals function of the WTO impossible (at least three AB members are needed to consider an appeal of a panel report<sup>2</sup>). As a result, there is no longer a multilateral forum to hear new appeals. For the moment, panels continue to be established, suggesting that WTO Members retain confidence in the dispute settlement system even if this does not include a functioning AB. This silver lining comes with a heavy touch of grey: there is uncertainty regarding the outcome of new disputes submitted to panels, if an appeal is lodged against the issued reports. Some WTO Members are seeking to self-insure against this risk by developing alternative appeal mechanisms. A prominent example is a European Union-Canada-Norway initiative to have panel reports heard by an *ad hoc* appellate process.<sup>3</sup> Such initiatives constitute partial patch-up solutions at best. They risk creating a multi-tier system across WTO Members, as some will participate in an appellate process, and some will not. This is unlikely to result in an internally coherent jurisprudence, the *raison d'être* of any appellate process.

<sup>2</sup> According to art 17(1) of the Dispute Settlement Understanding.

<sup>3</sup> See Joint Statement by the European Union and Canada on an Interim Appeal Arbitration Arrangement (25 July 2019) <<https://trade.ec.europa.eu/doclib/press/index.cfm?id=2053>>.

While most WTO Members oppose the US decision to block new appointments to the AB,<sup>4</sup> a recent survey, undertaken by Fiorini and others,<sup>5</sup> of WTO delegations and practitioners, reveals that the US is not alone in having concerns about the performance of WTO adjudicating bodies.<sup>6</sup> While dispute settlement may be the crown jewel of the WTO, it has imperfections. This is neither surprising nor contested. The problem is that the WTO membership collectively has been unable – more accurately, unwilling – to make timely repairs, and thus, allowed the jewel to crack.

Because the WTO Dispute Settlement Understanding (DSU) was a major innovation for the trading system – key features included the creation of an appellate function and removal of the ability of losing parties to block adoption of rulings – the Uruguay Round negotiators built in a formal review of the operation of the DSU. The DSU Review was duly initiated in 1998. Over the years, many suggestions to improve the operation of WTO dispute settlement were made by WTO Members. A core substantive concern of the US regarding the operation of the AB – that the AB has at times gone beyond its mandate – was raised in the DSU Review almost two decades ago. A 2002 proposal put forward by the US and Chile<sup>7</sup> on ‘improving flexibility and member control in WTO dispute settlement’ aimed to address US concerns regarding AB rulings on anti-dumping (zeroing) and more generally to create ‘some form of additional guidance to WTO adjudicative bodies.’<sup>8</sup> Whether engagement with this proposal would have helped avoid the current AB crisis is unknown, but other WTO Members rejected the suggestion. Other proposals made in

<sup>4</sup> This is clearly reflected in the proposal supported by 119 Members, which calls for launching the selection processes for the six vacancies in the AB.

<sup>5</sup> M Fiorini, BM Hoekman, PC Mavroidis, M Saluste, R Wolfe, ‘WTO Dispute Settlement and the Appellate Body Crisis: Insider Perceptions and Members’ Revealed Preferences’ (Bertelsmann Stiftung 2019) <[www.bertelsmann-stiftung.de/fileadmin/files/BSt/Publikationen/GrauePublikationen/MT\\_WTO\\_Dispute\\_Settlement\\_and\\_the\\_Appellate\\_Body\\_Crisis\\_Survey.pdf](http://www.bertelsmann-stiftung.de/fileadmin/files/BSt/Publikationen/GrauePublikationen/MT_WTO_Dispute_Settlement_and_the_Appellate_Body_Crisis_Survey.pdf)>.

<sup>6</sup> R McDougal, ‘The Crisis in WTO Dispute Settlement: Fixing Birth Defects to Restore Balance’ (2018) 52 *J World Trade* 867-96, and T Payosova, G Hufbauer, J Schott, ‘The Dispute Settlement Crisis in the World Trade Organization: Causes and Cures’, Peterson Institute for International Economics Policy Brief 18-5 (2018), provide excellent discussions of US concerns and options to address them.

<sup>7</sup> WTO Doc TN/DS/W/28 (23 December 2002).

<sup>8</sup> H Hauser, T Zimmerman, ‘The Challenge of Reforming the WTO Dispute Settlement Understanding’ (2003) 38 *Intereconomics* 241-45.

the DSU Review – eg, a suggestion by the European Union to establish a permanent panel body (ie, a true first instance court, which could have reduced the need for appeal) – might also have helped prevent the current AB crisis, if adopted.

Many reform proposals were made during the DSU Review. None were ever adopted. The proximate reason is WTO working practice, notably consensus-based decision-making. Consensus also permitted the US to block AB appointments. Although some WTO Members sought to discuss matters raised by the US during the Review, the need for consensus impeded the ability to respond flexibly to changed circumstances and priorities. Insistence to stick to an agenda established in the early 2000s essentially made the DSU Review an exercise in futility.

The specific issues raised by the US regarding the functioning of the AB eventually became the focus of a separate process launched by the General Council in December 2018. Ambassador David Walker (New Zealand) was appointed as ‘facilitator,’ with a mandate to explore resolution of a number of issues raised by the US, which arguably should have been addressed well before the crisis erupted, during the DSU Review. The consultative process proved to be too little too late, as by that time the key protagonists were deeply entrenched in their positions. These consultations were forced to address the relatively insignificant procedural issues raised by the US, diverting attention from the core issues falling under the broad heading of ‘WTO Member control’ in the DSU Review discussions.

The quintessential US criticism concerns the alleged overstepping of its mandate by the AB, most notably exemplified in the haphazard treatment of the idiosyncratic standard of review embedded in the WTO Agreement on Antidumping (Article 17(6)). This provision, introduced at the insistence of the US delegation in the Uruguay round, was meant to act as a deferential standard in favour of interpretations adopted by investigating authorities, if panels find that more than one permissible interpretation was possible in any given dispute. The US delegation’s understanding was that Article 17(6) served as a green light for ‘zeroing,’ a practice designed to inflate dumping margins. The AB was required to give meaning to Article 17(6). The US critique is that it only paid lip service to it. This critique is well founded. Panels and the AB have routinely repeated a statement to the effect that the Article 17(6) standard of review is not at odds with the generic standard of review, and, as a result,

have not seriously engaged with Article 17(6). Arguably nothing would have changed with respect to zeroing case law had the AB approached the interpretative issue from the angle of Article 17(6) and it is unfortunate this was not done.<sup>9</sup>

Re-negotiation of the zeroing issue is probably the wisest path forward, as case law continues to be erratic on this matter.<sup>10</sup> Where they are not clear, rules should be clarified by the WTO membership.

One way to encourage this would be for the WTO membership to require the AB to remand cases where the rules are unclear to the WTO bodies that are responsible for the implementation of the agreements that are invoked in a dispute. Even if this could be agreed, it must be recognised that panels and the AB unavoidably will have substantial discretion, as they must interpret one incomplete contract (the WTO) by using another incomplete contract (the Vienna Convention on the Law of Treaties, which does not assign specific weights to its various elements). If it were possible to write a more complete contract, that would have happened. Against this background, what is needed is to select better those entrusted with adjudication, and to pay more attention to the organisational aspects of adjudication. In our view, the following elements could/should usefully find their way into a future negotiation on reforming WTO dispute settlement procedures:

- A roster of 15-20 permanent panellists
  - Panellists should serve for one term of 8-10 years;
  - They should be divided in chambers of 3, and 7;
  - Depending on criteria to be defined (new issues; value of disputes; etc), disputes should be heard by divisions of 3 (relatively less important), or divisions of 7 (relatively more important);
  - Decisions should be taken by majority;
  - Dissenting opinions should be published;

<sup>9</sup> PC Mavroidis, TJ Prusa, ‘Die Another Day: Zeroing in on Targeted Dumping – Did the AB Hit the Mark in *US–Washing Machines*?’ (2018) 17 World Trade Rev 239–64.

<sup>10</sup> In April 2019, the panel on *US–Price Differential Methodology* (DS534) went head on against 25 years of AB case law and found that zeroing can be WTO-consistent.

- An AB consisting of 9 members
  - Its members should serve one term of 8-10 years;
  - It will decide cases in divisions of 3 members;
  - It will decide by majority voting;
  - Dissenting decisions will be published;
  - The collegiality requirement will persist;
- The members will decide on the establishment of a commission of eminent experts well-versed in GATT/WTO dispute settlement, entrusted with the task to screen both panellists, as well as AB members proposed by the Members of the WTO
  - The members of the commission will be decided by consensus, but they should be allowed to decide on panellists/AB members on qualified majority;
- Both the AB members, as well as panellists, will have the right to appoint their clerks
  - The number of clerks serving each judge will be decided *ex ante*;
  - AB members may select only one clerk of their own nationality.

There is, of course, much more to think about when determining how to regulate the WTO adjudicating bodies more comprehensively. The above could serve as basic axes to help address some important dimensions, such as the quality of judges, the incentives of adjudicators to please their nominating party, and the confusion of functions of the WTO Secretariat. Our suggestions complement the principles proposed by Ambassador David Walker to address US concerns with the operation of the AB,<sup>11</sup> which include ensuring that appeals are completed within 90 days; that AB members do not serve beyond their terms; that precedent (case law) is not binding; facts cannot be the subject of appeals; the AB be prohibited from issuing advisory opinions; and that its findings cannot add obligations or take away rights provided by the WTO Agreements.

<sup>11</sup> WTO, ‘Informal Process on Matters Related to the Functioning of the Appellate Body – Report by the Facilitator, H.E. Dr. David Walker’ JOB/GC/222 (15 October 2019).

All of these are fully consistent with – and indeed often echo – what is already in the DSU. For this reason, they should be amenable to all WTO Members and serve as the basis for the substantive agreement needed to address the core US concern – credible measures to ensure the AB will stick to its mandate.

Some type of advisory review body, as proposed by the US business community, with a mandate to assess and report on compliance by the AB with the ‘Walker Principles’ may help provide greater assurance that matters relating to the performance of the AB can be given greater attention in the DSB. However, at the end of the day, if WTO Members believe the AB is exceeding its mandate (eg, in filling gaps), this will need to be addressed by re-negotiating the substantive provisions of specific agreements. As suggested by Payosova and others,<sup>12</sup> this could in part be facilitated by giving the AB the mandate to remand cases to the relevant WTO bodies for them to clarify the applicable substantive rules in instances where there are gaps or rules are unclear.

One lesson from recent events is that more political oversight and interaction between WTO Members and a reconstituted AB is needed. In doing so, it is useful to distinguish between substantive and procedural rules. A step forward would be to agree that changes to the latter can be decided with majority voting. Given the differences in intensity of use of the DSU and the concerns that large players will have in regard of voting, the membership should be prepared to adopt weighted voting for such procedural changes *à la* International Monetary Fund or World Bank, based, for example, on shares of world trade. As things stand, no one will want to fix the DSU by deviating from the consensus rule. If the membership is bold enough to adopt a proposal along the lines indicated here, we might start seeing some light at the end of the tunnel.

<sup>12</sup> Payosova, Hufbauer, Schott (n 6).

