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Multilateralism and Regionalism from an American Perspective: Parallels and Contrasts with the Langhammer Vision

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Abstract The paper discusses various milestones in the process of multilateral trade negotiations, pinpoints current challenges facing the world trading order, and proposes possible ways out of the persistent impasse. Hufbauer argues that the success of the multilateral approach is at least partly because the GATT departed from the strictly unconditional definition of the most-favored nation (MFN) rule in the late 1970s already. Regional agreements such as NAFTA complemented, rather than hindered, multilateral trade liberalization in the past. The political economy of further multilateral liberalization has become increasingly complicated since countries such as Brazil, China, and India have emerged as relevant players. Against this backdrop, Hufbauer expects regionalism to become the strongest vehicle for delivering liberalization in the future. This could still leave a bright future for the WTO as a “house of plurilaterals”, i.e., agreements on specific issues such as services liberalization with conditional MFN treatment of varying membership.

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1 Introduction

In June 1973, Rolf J. Langhammer and I were embarking on academic careers amidst storms in the international economy. The world was enduring an oil shock, suffering tremors from the Smithsonian agreement, and Watergate hearings were unfolding on the pages of the *Washington Post*. One bright spot was a foreseeable end to the Vietnam War, a costly adventure for the United States in ways that find echoes in Afghanistan forty years later.

Before resigning in August 1974, Richard Nixon helped launch the Tokyo Round of Multilateral Trade Negotiations (1973–1979), an enterprise that dominated my years at the U.S. Treasury Department (1974–1980), and brought both Rolf and me face-to-face with the policy side of international economics. In retrospect, the Tokyo Round was the high water mark for multilateralism as the defining doctrine of U.S. trade policy. While we were both multilateral enthusiasts, Rolf and I drew different lessons from the Tokyo Round. In the next few sections, I will cite a few extracts from Rolf's extensive writings, placed in boxes, and I will summarize but not cite my own contemporaneous views.

2 Tokyo Round Enabling Clause and Codes

Where Rolf saw considerable promise in the Enabling Clause, adopted in the Tokyo Round (Box 1), at the time I regarded it as a relatively harmless nuisance – a departure from the unconditional MFN rule for tariffs. The Enabling Clause enshrined the unfortunate but politically necessary Generalized System of Preferences (GSP), which resulted from a GATT waiver in 1971. In Rolf's scenario, as a consequence of the Enabling Clause, developing countries would, between themselves, form preferential trade areas without regard to regional boundaries. Memory may fail me, but I cannot recall giving this prospect serious thought back in the 1970s.

However, the Tokyo Round departed from the unconditional MFN rule in a manner that I did welcome: the construction of codes on six frontier subjects, namely Government Procurement, Customs Valuation, Standards, Licensing Procedures, Antidumping, and Subsidies. These codes limited their rights and/or obligations to code members. I was deeply involved in negotiating the Subsidies Code. Early on it became apparent that very few developing countries would accept the code obligations. I concluded that code benefits (procedural rights and the injury test in countervailing duty cases) had to be limited to code members or the Subsidy Code would never be accepted by the U.S. Congress, and possibly not by other legislative bodies. To this day, I believe that the same conditional MFN logic applies to most frontier subjects. Liberalization beyond the elimination of tariffs faces a rocky path if constrained by the unconditional MFN rule.

Box 1. The Enabling Clause

“The new “framework for the conduct of world trade” initiated by some developing countries under the leadership of Brazil and concluded in the Tokyo Round [the Enabling Clause], however, incorporates inter-regional liberalization rounds between developing countries as a permanent legal component into the future GATT and hence may stimulate further attempts [to conclude preferential trade agreements].” See Langhammer (1980).

3 Regionalism in Asia

In the 1980s, after the conclusion of the Tokyo Round, Rolf led Western scholarship on trade developments in Asia. As an expert on ASEAN, he was somewhat skeptical, in the late 1980s, of its trade policy declarations. A decade later, in the late 1990s, his skepticism came to bear on the grandiose rhetoric of APEC leaders, which Rolf contrasted unfavorably with the hard commitments of the European Union (Box 2). Both as to ASEAN and APEC, for many years I have agreed fully with Rolf’s evaluation. In my view, these agreements are essentially geopolitical pacts, disguised as trade deals. ASEAN capped the decision of political leaders in Southeast Asia to desist from supporting guerrillas in each other’s territory, and otherwise to reduce their military antagonisms. APEC should be viewed as a diplomatic effort to head off confrontation between the United States and China, and as a forum for Pacific leaders to meet and exchange views on the critical issues of the day. These are valuable contributions, but they are not the same as trade and investment liberalization.

Box 2. ASEAN and APEC

“The analysis undertaken for consumer goods supplied in four ASEAN countries...finds domestic inflation and exchange rate changes to be more important determinants of changes in tariff redundancy than changes tariff rates.” See Langhammer (1988).

“This article discusses similarities and differences between past EU binding internal liberalization “across the board” in the industrial sector and present so-called voluntary sectoral liberalization of member states of the Asia-Pacific Economic Cooperation (APEC). ...[The] major disadvantage of liberalization APEC style in the industrial sector consists in disparities in timing liberalization under the so-called Bogor target of achieving free trade within APEC in 2010 (2020 for less advanced member states). Reliance on “peer pressure” as the only mechanism to commit member states to liberalization I seen as a weak driving force to make APEC’s concerted unilateralism a stepping stone for the successor round of the Uruguay Round.” See Langhammer (1988).

While Rolf cast a critical eye on trade policy initiatives in ASEAN narrowly and the greater APEC region broadly, he was among the first to remark on the region’s market-led integration through the expansion of global value chains between China and Southeast Asia. This is illustrated by his article referenced in Box 3. Other scholars (Frost 2008) have since picked up on Rolf’s theme that market forces led the integration process in Asia, while trade pacts essentially followed arrangements already concluded between enterprising firms.

Box 3. Asian Value Chain

“Until 1985, intra-PACRIM trade in manufactures was a Japanese domain...China’s beginning outward orientation strengthened the inter-industry component of intra-PACRIM trade... whereas intra-industry trade become more prominent in the rest of intra-PACRIM trade.” See Langhammer (1989).

4 Regionalism in North America

Whereas Rolf’s skepticism towards ASEAN and APEC responded to the hollow content of their trade policy declarations, his skepticism towards NAFTA ran much deeper. It reflected his profound concern that NAFTA posed a threat to the multilateral system, as shown in Box 4.

Why did the United States turn so sharply from strident advocacy of multilateralism in the 1980s to strident defense of NAFTA and other regional initiatives in the 1990s and 2000s? Five central reasons can be cited for the shift. Unlike Rolf, I subscribed to these arguments and espoused them within Washington policy debates.

The foremost reason was the end of the Cold War. Multilateralism was in large part the handmaiden of U.S. foreign policy that sought to assemble the largest possible group of countries to favor market-oriented economics and adopt a friendly posture toward the United States, whatever their internal governance on the spectrum from democracy to autocracy. With the end of the Cold War in 1989, the political impulse towards multilateralism weakened among ruling circles in the United States, while the tendency to scrutinize the internal governance of partner countries increased.

Box 4. NAFTA

“Yet, one might ask whether it makes much difference to have NAFTA or not... North American-based companies will continue to exploit the potential of “natural trading partnership” by furthermore integrating Mexico into their globalization process of worldwide sourcing. So why doing something institutionally what would come naturally through the market, through cultural and economic proximity, and through unilateral policies? There are a number of answers.

“First, the weaker partner Mexico wants to bind the larger partner US because such binding lowers the risk premium to investment in Mexico....

“Second, NAFTA gives the US a leverage to contain the flow of negative cross-border externalities like environmental pollution or migration across the Rio Grande... and better control the protection of intellectual property rights.

“Third, NAFTA could become a centerpiece for...a “hemispheric initiative” of negotiating first hub-and-spoke types of bilateral agreements with other Latin American countries and later on inviting other countries to join NAFTA...”

“Fourth, most important, NAFTA has been motivated by the frustrating lack of progress in the Uruguay Round. In a strategic game with the EC, NAFTA [has] become a bargaining chip to push the Uruguay Round forward. This has triggered the fear that by killing the disease, the patient, that is the multilateral trading order, may be killed too.” See Langhammer (1992).

The second reason was the more intrusive inquiry by American officials into barriers that hinder U.S. exports. This reflected a growing realization that border measures are often the smaller part of barriers that restrict international commerce. Many of us in the Washington debate feared the near impossibility of getting multilateral agreement on the progressive eradication of behind-the-border barriers.

A third and related reason for the tilt towards regionalism responded to U.S. political dynamics. The dwindling U.S. labor movement retained its political clout in Washington through alliances with the left-wing of the Democratic party. Trade unions understood that they could not veto outright every trade agreement to appear on the horizon. But by adding labor rights and environmental protection to the list of U.S. “offensive” demands, the unions could prolong negotiations. Since the WTO would not touch labor and environmental issues with a barge pole, this tactic served to reinforce the tilt toward regional agreements.

Fourth was the plain fact that, by the time of the run-up to the Uruguay Round (1986–1994), in contrast to the Tokyo Round, the Quad countries – Canada, the European Union, Japan and the United States – had lost their dominance of the multilateral agenda. During the Tokyo Round, little was asked of developing countries: they could choose or not to join the various codes and they were not asked to bind their tariffs at applied levels, much less to reduce applied tariffs. But in the Uruguay Round, much was asked of developing countries: they had to agree on a framework for services liberalization (the GATS), and even though the content was sparse, this was regarded as a major undertaking. Moreover, they had to accept the agreement on Trade Related Intellectual Property Rights (TRIPS) and sign the Tokyo Round codes. These were difficult negotiations, and the prolonged agony of completing the Uruguay Round persuaded me that FTAs and RTAs offered greater prospects for future liberalization, once the ink was dry at Marrakech. Rolf probably came away from the Uruguay Round with different conclusions. His multilateral spirits may have been bolstered by post-Uruguay successes in negotiating the Basic Telecommunications Agreement (1997), the Information Technology Agreement (1997), and the Financial Services Agreement (1999) – with rights extended unconditionally to all WTO members, even those which did not agree to the respective obligations.

5 The Prospect of a Trans-Atlantic Free Trade Area

Whether or not he regarded the Uruguay Round as a triumph, Rolf was decidedly cool to one of the post-Uruguay flavors, a Trans-Atlantic Free Trade Agreement (TAFTA), as the excerpt in Box 5 shows. Though I haven’t found a Langhammer article on point, I would be surprised if he wasn’t even more skeptical of the ill-fated Free Trade Agreement of the Americas (FTAA), an enterprise that was launched in Miami in 1994 and died in the same city in 2003. Looking back on the mid 1990s and early 2000s, I counted myself among the FTAA enthusiasts, and if TAFTA talks had moved beyond the low-key Trans-Atlantic Dialogue, I certainly would have been a supporter. Rolf’s crystal ball was better than mine.

However, Rolf and I do agree on one critical dimension of a Trans-Atlantic Partnership: if embraced before 2020, this could be the last great opportunity for the United States and the European Union to play a decisive role in shaping the rules

governing global commerce. But where my tactical preference calls for Trans-Atlantic rules that open European and American markets for goods, services and people, and harmonize our regulations on a conditional MFN basis, Rolf adheres to the unconditional approach. He argues that the United States and the European Union can best lead by example, eschewing discrimination against emerging countries – even when they keep their own markets closed, even when they favor state supported enterprises (SSEs), and even when they have scant regard for intellectual property rights (Box 6). He holds this view despite the fact that the lead emerging economy, China, has played a disappointing and unconstructive role in the Doha Round, absolutely at odds with Rolf’s advice proffered in 2005 (Box 7).

Box 5. The Questionable Wisdom of TAFTA

“There are cases shining favourably on the idea, but the implementation of TAFTA will imply substantial costs due to the internal and external consequences. The problem of a free trade area between the two most important economic blocs is the impact on the multilateral approach of trade liberalisation.

“The authors suggest a Transatlantic Liberalisation Initiative (TALI) as an alternative to TAFTA. Under TALI, the EU and the US should accelerate their implementation of their Uruguay Round commitments and liberalise in areas that are not yet covered by WTO agreements. This should be done under the Most-Favoured-Nation clause and would be a strong motivating force for multilateral liberalisation.” See Siebert et al. (1996).

Box 6. TAFTA Revisited

“Transatlantic leadership in global trade policies is badly needed but the way via TAFTA – regardless of whether or not it is a dead horse – is an impasse... [The right] response could be labeled transatlantic liberalisation initiative (TALI) intended to facilitate global trade by multilateralizing rules for transaction procedures concluded between the EU and the US and extended to third parties...” See Langhammer (2008).

Box 7. China’s Role in the Doha Round

“Seen from Europe, China plays an important role in giving a new momentum to the [Doha Round] and to save the WTO from a post-Cancun stalemate trauma. Yet, to play this role, it is crucial for China that it does not join any ‘South’ coalition in controversy against the ‘North’.” See Langhammer (2005a).

6 Steady Rise of Globalization

Perhaps a major reason why Rolf takes a sanguine view of multilateralism is the steady growth of globalization since the mid 1990s. Rolf used the Frankel Index to calculate the extent of globalization over a fifteen year period, and whatever the country grouping he found a rising trend (Box 8). I agree with Rolf that unilateral liberalization, added to the implementation of the Uruguay Round accords and combined with rapidly falling communications costs, have spurred the pace of global integration in recent decades.

The difference is that I attribute more importance to regional agreements, and I am less sanguine about the continuation of recent trends in the absence of major new policy initiatives in the next decade.

Why am I less sanguine? Common sense suggests that trade liberalization is a much easier to sell politically when national economies are operating near their production frontiers, unemployment is low, and inflationary winds are in the air. In such periods, displaced workers can readily find alternative employment and imports are welcomed as a curb against inflation. To be sure, short-term troubles may spur statesmen to launch new trade agreements (as happened in the early 1970s and early 2000s), but long term sub-par growth, high unemployment, and threatened deflation do not seem like a promising environment for trade liberalization. In this context, the main selling point for new trade deals is more jobs in the export industries. The problem with that line of political salesmanship is that trade liberalization is a two-way street: trade bargains increase both imports and exports, and in approximately equal amounts. The “inconvenient truth” is that, as a first approximation, trade is about raising productivity not about reducing unemployment. To be sure, by boosting economic potential in all countries, trade opens the opportunity for new productive investment, and the new investment can, over time, create jobs.

But the jobs argument should not be oversold. A simple thought experiment as to the link between higher investment and more jobs is instructive. Appendix A in Hufbauer et al. (2010) reports an average “dollar ratio” of 0.46, derived from several regression analyses and computable general equilibrium (CGE) models. The “dollar ratio” is the ratio between the estimated GDP gain, expressed in dollars, from liberalization scenarios and the estimated two-way increase in trade, again expressed in dollars. A robust trade agreement, such as an ambitious Doha Round, might deliver an increase in two-way trade for the United States, Europe and Japan of around \$140 billion (the CEPII-CIREM estimate). The implied dollar increase in the potential GDP level, based on the average “dollar ratio” would be \$64 billion. This would probably be achieved over a five-year period, or an additional \$12 billion per year. Assuming that new investment of the same magnitude is created (a capital-output ratio of 1.0), the investment stimulus would be about \$12 billion. Using current U.S. coefficients, around 7,000 jobs per billion dollars of investment, the additional employment in the three countries would be about 84,000 jobs – a small figure, considering the combined labor force of the three countries (near 400 million) and their current unemployment levels (near 10 percent, including discouraged workers). This simple calculation reinforces the common sense of economics that the real gains from trade derive from pushing out the production frontier, not from pumping up aggregate demand and creating a massive number of new jobs.

Box 8. Globalization Track Record.

“Measuring the FI [Frankel Index] over many countries and over a 15-year period shows three clear results. First, the degree of globalization has been rising from different levels in different income groups of countries. Second, this rise holds for less globalized large countries as well as for more globalized small countries. Third, the distinction FI in large and small economies has been vanishing. Large economies have gradually caught up with smaller economies in terms of their degree of globalization.” See Langhammer (2011).

7 Liberalization through Regionalism

Today, in 2012, the year 2030 seems distant. But when we consider that 18 years is the same span since the conclusion of the Uruguay Round at Marrakech in 1994, the year 2030 does not seem so far away. The past 18 years saw multilateralism on the defense, and regionalism on the offense. In fact, the score became so lopsided that two distinguished economists, with close ties to the WTO, edited a volume with the awkward title *Multilateralizing Regionalism*, suggesting that hitching a ride was the best chance to keep the multilateral train moving (Baldwin and Low 2009). This section argues that regionalism will prove the strongest vehicle for delivering liberalization over the next 18 years. The concluding section expounds a new approach that could secure the WTO's role and foster a robust multilateral contribution.

Over the next decade, the big frontier – the great opportunity for trade growth – will very likely be services. Many services will be delivered across borders through foreign direct investment. Wal-Mart, UBS and SAP are today's exemplars. In the future, universities (perhaps Kiel University as well as MIT, Yale and Oxford) will open foreign campuses; and world-class medical centers will open clinics abroad (Mayo, Johns Hopkins). Tourism continues to grow at a steady pace. Global airlines are coalescing into a few huge networks. Many services will be delivered electronically. As Rolf and others have shown, the advanced countries enjoy a decided comparative advantage in business and professional services (Box 9). And, as J. Bradford Jensen has suggested, the scope for expansion of services trade could be multiples of the magnitudes calculated using standard economic techniques (Hufbauer et al. 2012).

One testing ground between regionalism and multilateralism will be their respective results in lowering multiple barriers that confront services trade. Contrasting the ambitious commitments in the Korea-U.S. and Korea-EU Free Trade Agreements with the limited progress in the Doha Round, it appears that regional pacts are winning this race. The European Union has come a long way in its internal liberalization (Box 10), and the Trans-Pacific Partnership promises major strides. Even so, recent services talks in Geneva, between self-selected WTO members, could put the multilateral system back in competition (Hufbauer et al. 2012).

Another testing ground will be agreements that achieve convergence in industrial, sanitary and phytosanitary standards. Differing standards are among the most effective means of separating markets, enabling firms to enjoy significant market advantages within their respective national territories. Standards fall within the purview of the WTO, through the Agreement on Technical Barriers to Trade and the Agreement on Sanitary and Phytosanitary Standards. They are also addressed by regional agreements. But apart from the European Union, with its Cassis du Dijon decision on mutual recognition (the product of an exceptionally strong judicial system), the convergence of standards remains a distant goal (Box 10).

A third challenge is trade facilitation. This sounds boring, but at a March 2012 meeting of the ICC in Geneva, this was the one deliverable from the Doha Round that CEOs most wanted, as a break out item from the Doha Round. The pleas of business firms were repeated at the B20 meeting in Mexico in April 2012. If trade facilitation cannot be achieved by the WTO in Geneva, separated from the rest of the Doha package which is now wrapped together by the "single understanding", trade facilitation might be achieved in regional agreements. As for most of Africa and parts of Latin America,

trade facilitation is about cutting petty border corruption, slashing paper work, and upgrading ports, airports and roads. In advanced countries, the challenge is to lessen the burden of security and food safety controls, and to adopt uniform electronic customs procedures, together with upgrading ports and the inter-modal connections between ports, roads and railroads.

Box 9. Comparative Advantage in Services

“RCA [revealed comparative advantage] estimates for the US, EU and Japan confirm the leading role of the US in most business services (except for insurances) while Japan has not established itself as a leading supplier of services.” See Langhammer (2004).

Box 10. Behind the Border Barriers in Services

“As a result [of EU offers in the Doha Round], by February 2003, the EU has already come closer to the status of a customs union in services than before. This process will continue as the EU Commission urges Member States to comply the commitments to remove any trade barriers within the EU. Opening access for German consumers to internet pharmacies located in the Netherlands in early 2004 has been part of this process.” See Langhammer (2005b).

8 Breathing Life into Multilateralism

“Will the WTO Enjoy a Bright Future” – that’s the title Jeffrey Schott and I chose for a report to the International Chamber of Commerce – and the opening sentence reads, “Our answer is a resounding “yes”,” (Hufbauer and Schott 2012). But the report goes on to explain that the “yes” depends on radical changes in the architecture of multilateralism. I do not know whether Rolf would agree with the prescriptions that follow, but we are in accord that the WTO should enjoy a bright future for the world economy to flourish in the twenty-first century.

Resurrecting the WTO must begin with an acknowledgement that the GATT system was a multi-speed affair, even in its heyday at the end of the Tokyo Round in 1979. As early as 1970, the eminent Harry Johnson sealed the end of unconditional MFN for tariff barriers when he endorsed the Generalized System of Preferences. The Tokyo Round, of course, created plurilateral codes and the Enabling Clause. “Special and differential treatment” has since become a watchword in practically every WTO agreement. However grand the rhetoric may sound, “special and differential treatment” is the polar opposite of “unconditional MFN”.

To revive multilateralism as an agenda and the WTO as an institution, the reality of multi-speed agreements must be embraced, not regretted. The frontiers of liberalization are standards, services, trade facilitation, and investment. The objective of the “new multilateralism” should be measured progress towards deeper integration at different speeds, not “one size fits all”. This will create policy “cliffs” – different rights and obligations for different WTO members – but cliffs should be seen as the motive for future reciprocal bargains.

Contemporary regionalism is organized around two principles: geographical and historical ties between countries (the EU model), and political alliances built on geostrategic concerns (America's FTAs with Bahrain; China's FTAs with ASEAN) or on similar political systems (U.S. insistence that its FTA partners be functioning democracies). By contrast, plurilateral deals within the WTO should *not* be based on geography or political systems. Within the WTO, new arrangements should steer clear of such litmus tests.

Our ICCF Report examines five potential plurilateral agreements: services liberalization, currency undervaluation, climate and energy, zero-for-zero tariffs coupled with disciplines on non-tariff barriers, and rules of the road for state-owned enterprises. If the WTO becomes a "house of plurilaterals", each of these potential deals will have its own peculiar features. However, four common challenges will confront any plurilateral and these challenges are worth mentioning.

Inside or Outside the WTO?

The first common challenge is inside or outside the WTO framework. Our report advocates the "inside" approach, but we recognize that "outside" may prove to be the only way forward for some agreements. Indeed, the Anti-Counterfeiting Trade Agreement (ACTA), recently concluded in Kyoto with 31 signatories, points the way to other "outside" agreements. Many WTO members were unwilling to subscribe to tighter enforcement obligations, within their territories and at their borders. Consequently countries that have sustained large losses owing to counterfeit products – led by the European Union, Japan and the United States – forged an agreement outside the WTO framework.¹

Despite the ACTA precedent, there are strong reasons for both members and non-members to prefer the "inside" approach. For members, an agreement within the WTO framework ensures access to a well-functioning dispute settlement system and a highly competent research staff. For non-members, the WTO framework smoothes the way to their own future participation. For the multilateral system as whole, agreements within the WTO framework are more likely to become universal practice, as happened with several Tokyo Round codes when the Uruguay Round was concluded. Meanwhile, the care and maintenance of agreements within the WTO framework will impart vitality to the organization itself.

Conditional or Unconditional MFN?

The unconditional MFN principle, articulated in GATT Article I, served as a foundation stone of the original GATT (1947). Unconditional MFN thwarts discrimination between alternative foreign suppliers and thereby promotes both economic efficiency and harmonious relations between states. Moreover, the principle ensures that the benefits enjoyed by country A from a trade bargain with country B are not later undercut when B negotiates a still better bargain with country C.² Despite these advantages, over the course of ensuing decades it became increasingly hard to reconcile

¹ It must be noted that, for the moment, the EU Parliament has rejected ACTA. In the larger context of a Trans-Atlantic Partnership, the ACTA would very likely be approved.

² Unless, of course, countries B and C join together in a free trade area or customs union – exceptions to GATT Article I allowed by GATT Article XXIV.

the unconditional MFN principle with forward progress in dismantling barriers and assuming new obligations.

Whenever trade barriers are lowered, or other obligations undertaken, some domestic constituency inevitably protests that its livelihood and values are endangered. In democratic countries, the way to overcome these claims is neither to argue that the losers exaggerate their woes nor to sing the benefits of foreign competition, but rather to show that the bargain ensures reciprocal obligations abroad which pay off for domestic exporters. The simple yet powerful logic of reciprocity goes far to explain the explosion of bilateral and regional free trade agreements since 1990, now numbering nearly 400.³

Whatever its virtues, the unconditional MFN principle creates an open door for free riders and an exit path from reciprocity, especially when concessions agreed among a few countries are extended without cost to all WTO members. If free riders are small developing countries, with little commercial clout, that's not a big problem, and these were long tolerated in the GATT system. But the prospect of free riders the size of Brazil, India or China is enough to suffocate most plurilateral agreements in the crib.

These realities mean that conditional MFN will likely serve as a cornerstone for plurilateral agreements. In turn, that means (per Article IX(3) of the Marrakesh Agreement) that if a plurilateral agreement is to be established within the WTO framework, three-fourths of WTO members must agree to a waiver – fully realizing that the agreement will discriminate against many of them at the outset. Strange as it may seem, many precedents exist for such acceptance. In 1966, most GATT members adopted Part IV, which ultimately paved the way for preferences in favor of developing countries.⁴ In both the Tokyo Round and the Uruguay Round, all GATT members permitted the Government Procurement Agreement (GPA), which opens government procurement only to GPA members. In these and a few other cases, conditional MFN was accepted as the price of fresh liberalization or new obligations.

“Critical Mass” or “Substantial Coverage”?

Plurilateral sector-specific agreements negotiated within the WTO during the past two decades have usually, but not always, covered a “critical mass” of trading partners. “Critical mass” has typically been defined to include countries accounting for 90 percent or more of world trade in the particular sector. In four instances, this was the touchstone for including the plurilateral agreement within the WTO framework. Examples are the Civil Aircraft Agreement of 1994 which covered the only two producers of large civil aircraft, the United States (Boeing) and the European Union (Airbus);⁵ the Basic Telecommunications Agreement of 1996 which covered roughly 91 percent of the world's basic telecom lines when signed; the Information Technology Agreement of 1996, which covered more than 90 percent of trade in computers and

³ This figure includes many RTAs of limited commercial importance, as well as RTAs notified to the WTO but not yet concluded.

⁴ Preferences took the form of the Generalized System of Preferences (GSP), specifically authorized in 1971, and the so-called Enabling Clause, calling for “differential and more favorable treatment” of developing countries, adopted in 1979.

⁵ The Civil Aircraft Agreement was suspended in 2002 when the United States (on behalf of Boeing) and the European Union (on behalf of Airbus) launched WTO cases against each other complaining about excessive subsidies.

telecommunications equipment;⁶ and the Financial Services Agreement of 1999, which covered roughly 95 percent of the world's basic banking services. In these instances, 90 percent or higher coverage at the outset meant that free riders did not create a serious problem; hence the benefits of the agreement could be extended on an unconditional MFN basis to all WTO members.

Yet, while the “critical mass” test has become part of negotiating lore in Geneva, it is not a requirement articulated in the Marrakesh Agreement for a waiver from the unconditional MFN rule. The important contrary precedent to the 90 percent test and the unconditional MFN rule is the Agreement on Government Procurement of 1994.⁷ Negotiated as part of the Uruguay Round, the GPA covered 28 countries and perhaps 50 percent of government procurement worldwide.⁸ GPA market access benefits are available only to members of the GPA club – in other words, the conditional MFN rule. The GPA is the precedent most relevant to future plurilateral agreements.

“Critical mass”, interpreted as 90 percent or more of world trade in the relevant sector, would be a show-stopper for launching most plurilateral talks within the WTO framework. In our view, the threshold test for inclusion in the WTO framework should be “substantial coverage” of world trade or production in the affected sector – meaning, perhaps, more than 50 percent.

Enhancing the DSM.

In addition to becoming the “house of plurilaterals”, the WTO can add to its institutional presence by improving the operation of its eminently successful dispute settlement mechanism. As a first step, the WTO should appoint a roster of permanent panelists available to hear cases on two weeks' notice. In commercial matters, justice delayed is justice denied, and too many cases drag into a second or third year simply because it's difficult to coordinate the schedules of panelists who must attend to their own professional lives and travel from distant countries.

Additionally, and more important, the WTO should “clone” its DSM to handle new types of cases. First, with appropriate financial support, and upon the request of RTA parties, the WTO clone could hear disputes over the terms of regional arrangements. Regional agreements, with the exception of the European Union, are characterized by weak dispute settlement systems. Some RTAs might like to add a meaningful dispute system to their agreements. Second, the WTO clone could hear trader-state cases, akin to investor-state cases that are regularly brought before arbitration panels under Bilateral Investment Treaties (BITs) and most often decided by the International Center for the Settlement of Investment Disputes (ICSID). WTO agreements spell out hundreds of pages of rights and obligations (*Legal Texts* published by the WTO number 500 pages), and these texts are complemented by thousands of pages of Council decisions, decided cases and other supplementary documents. However, for want of “legal standing” the rules are a dead letter to many companies. Under current practice,

⁶ The ITA agreement now numbers 73 countries and accounts for 97 percent of world trade.

⁷ The Uruguay Round Agreement on Government Procurement superseded the Tokyo Round Government Procurement Code, which had excluded services. The Uruguay Round Agreement achieved a 10-fold expansion in coverage by including both national and local government entities; moreover, it extended coverage to selected services and public utilities.

⁸ The 27 European Union countries are counted here as one member of the GPA.

a company must first persuade its own government to espouse an action in the WTO. Every government has multiple priorities, and these are carefully balanced in deciding whether or not to bring a case. Consequently many meritorious cases simply languish. World commerce not only needs a World Trade Organization between governments; it also needs a World Trade Court to resolve disputes between governments and business. The WTO is ideally suited to fill that need.

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