

**Rule making amidst growing diversity:
A club of club approach to WTO Reform and new issue
selection**

By

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Several years ago, Albert Bressand, Taktoshi Ito and I, laid out a Vision for the World Economy.¹ We emphasized the need for international organizations to achieve a balance between openness, diversity and cohesion and argued that these principles should be applied through international organizations and agreements which we called Clubs.

Clubs are voluntary associations of willing members who combine to achieve shared objectives. Clubs establish rights and duties of their members based on shared values and benefits, not coercion. They are generally concerned with collective goods, allowing members to realize scale economies by sharing fixed costs. They reduce free rider-ship by excluding members from club benefits.

In our proposals we suggested that some of these international clubs could be functional and devoted to single or related issues. Examples today include the ILO and the BIS. Other clubs could be regional and might contain several issues – such as APEC or the EU. In addition, however we also advocated “global coordinating clubs” to deal with linkages among issues and regional agreements. These we called the “club-of-clubs.” We pointed out that the United Nations, the WTO and the OECD embodied elements of such an institution. In our proposal these Clubs of Clubs would play a strong role in coordinating functional and regional organizations, initiating new clubs, encouraging

¹ Lawrence, Robert, Albert Bressand and Takatoshi ITO, A Vision for the World Economy, Washington DC: Brookings Institution 1996.

dialogue and interaction among clubs (particularly on cross-cutting issues such as environmental protection measures that affect trade).²

As many of earlier papers in the conference will undoubtedly have observed, the WTO has in its past, actually been closer to a club of clubs by having had separate codes to which its members could subscribe. While the WTO rules continue to contain several plurilateral agreements, because the Uruguay Round was a single undertaking, currently by-and-large, all members adhere to all agreements.

Partly as a result of this feature, in fact, the WTO has become an increasingly controversial institution. On the one hand, the WTO has been assailed for having gone too far. Some critics, typically reflecting the concerns of many developing countries, claim that by making all of its members adopt agreements such as those relating to Trade Related Intellectual Property and Investment Measures (TRIPs and TRIMs), the WTO has strayed beyond its basic trade mission and forced many of its members to accept obligations that are not in their interest, intrusive of their sovereignty and beyond their implementation capacities. On the other hand, the WTO has also been assailed for not going far enough. Other critics, typically reflecting the concerns of developed countries, have sought to broaden and deepen WTO coverage within the context of a single undertaking by negotiating new disciplines on issues such as investment, labor standards, competition and the environment.

At the Cancun ministerial meeting these conflicts came to a head when the meeting ended in an impasse over efforts to launch negotiations on the Singapore Issues.

² There is a need to distinguish between the WTO as a forum for agreements relating to trade versus its role as a body coordinating relationships between trade related and non trade related issues, as the central body undertaking what has sometimes been termed coherence. I will assume, for purposes of this paper that the major issue relates to the former task rather than the latter.

In Geneva, in August 2004, the WTO members reached agreement to drop investment, competition policy and transparency in government procurement from the Doha Round agenda. Moreover these developments were preceded by other unsuccessful efforts such as the negotiations for a Multilateral Agreement on Investment at the OECD, and the US efforts to introduce labor standards into the WTO at Marrakech and Seattle.

One conclusion from the recent experience might be that the WTO rules should not be expanded beyond those currently in place. But this could be costly in terms of opportunities foregone. Although the desirability of adopting rules relating to each of these issues as integral components of the WTO Agreement remains a matter of some controversy, there are strong reasons to believe that additional rules could aid in the integration required for fully exploiting the potential of the global economy. There is considerable evidence that even when tariffs are removed, border effects continue to impede the free flow of goods and services. This was surely the experience of Europeans who concluded in the early 1980s that despite the virtual elimination of internal tariffs their markets remained fragmented. The considerable extent of fragmentation even among developed countries is documented by Bradford and Lawrence as are the large welfare benefits that could be enjoyed from price convergence.³

These controversies at the WTO reflect the tensions that result from the challenge of deeper international economic integration. There are strong political pressures at work for the WTO to expand its mission. There is also evidence that deeper integration could yield significant economic benefits. But there are dangers that such an expansion could

³ Bradford, Scott and Robert Z Lawrence (2003) *Has Globalization Gone Far Enough? The Costs of Fragmented Markets*, Washington DC: Institute for International Economics.

exceed the implementation capacities of both the WTO and its members. In addition, it could lead to growing challenges to the institution's legitimacy.

Since it appears impossible to obtain agreement by all members to accept obligations on these new issue areas, an alternative approach could be a more variable set of commitments. In this paper, therefore, I consider whether a more new clubs under the aegis of the WTO might not serve to make the organization more effective. What I have in mind is supplementing the core WTO commitments as embodied in the Uruguay Round Agreement, to which all WTO members subscribe, with additional agreements – or clubs – to which only some members would subscribe.

Protocol for Club Formation.

Once efforts had been made to make the ill-fated Singapore Issues part of the single undertaking in the Doha Round, it made it difficult to allow them to remain on the agenda as separate pluri-lateral agreements. In particular, opponents of these issues were suspicious that even if they were initially introduced as pluri-lateral agreements, members that did not originally sign these agreements could later be forced to join them. Indeed, they pointed to the precedent of having several of the Tokyo Round codes incorporated into the Uruguay Round Agreement. Accordingly, and partly to allay such fears, it would be important for the WTO to contain an agreement for club formation, a protocol that would define the rules for forming clubs that would make it clear that membership was strictly voluntary and would also make it clear and explicit that absent consensus, these clubs could not be made part of the single undertaking. In addition, it would also be important to lay out a set of rules to apply to all clubs, before considering each in particular. What might these rules be?

Selecting the Issues.

I believe that the WTO should only host clubs that are (a) related to its mission; (b) enforceable by the means available to the organization and the members who join the club and (c) compatible with maintaining and enhancing legitimacy.

Mission. The Preamble of the WTO Agreement indicates that the WTO is an organization which seeks to enhance welfare by (a) reducing barriers to trade. (Such as tariffs); (b) reducing discrimination in trade. (e.g. requirements for MFN and national treatment), and (c) enhancing development through trade. Accordingly, the issues that are chosen should be trade related in at least one of these respects and ideally in all of them. In this context, trade should be interpreted broadly to include international exchanges of goods and services and the movement and location of firms and people designed to accomplish such trade. The coverage should relate either to policies which directly affect market access (e.g. border barriers) or to the aspects of other policies which can materially affect such access. The aim is to facilitate trade in both goods and services while at the same time preserving adequate scope for national policy differentiation. While there are many other issues that may be important subjects for international cooperation (e.g. environmental policies and human rights) and many other policies that could contribute to economic development,(education, health etc) trade-relatedness should be the sine-qua-non for inclusion. In addition, to the maximum extent possible, agreements should provide the maximum space for other functional international clubs to implement non-trade related international agreements and for members to have considerable scope for differentiating their domestic policies to match their conditions

and requirements. The issues contained in clubs should also not overlap with issues that are already part of the WTO's single undertaking.

Means. The WTO itself and members of the clubs must have, or be readily able to acquire, adequate means to carry out the missions. WTO itself must have adequate expertise, resources and authority. For example, a competition policy agreement that envisaged the WTO Club operating to provide consent on international mergers would have to be equipped with the expertise and resources and authority of the US Justice Department or the European Commission. However, a weaker agreement that entailed simply providing an opinion would need similar expertise but less power. In addition, since most clubs would rely heavily on national implementation, members should have, or be readily able to acquire the necessary capacity. Only the able should be encouraged to join.

Legitimacy. The desirability of the issue as an item for inclusion in the WTO club framework should enjoy widespread acceptance by the membership. All Members should view their obligations on each issue (or club) as welfare enhancing. Even if members are themselves not ready to accept binding obligations and club membership there should be a consensus that the WTO is the appropriate institutional setting. Finally, the approach should minimize inhibitions on national autonomy required to achieve any given objective i.e. subsidiarity should be a key element

Operating Rules.

How would the clubs operate? Who would negotiate and determine their rules? When would these negotiations take place? What rights would WTO members that are not club members have? What would be the relationship between the clubs and the WTO

dispute settlement process? These are some of the questions that need to be answered before the approach can be fully evaluated. Fortunately, the WTO rules themselves provide some initial answers. As noted, the WTO already operates as “a club of clubs” because it contains several pluri-lateral agreements. In this respect, the most interesting is the Agreement on Government Procurement Agreement (AGP). It provides useful guidance for how the clubs might operate.

Negotiations. All the contracting parties participated in the negotiations in the AGP (and the other codes in the Tokyo Round.) Even though all members did not sign the agreement and all codes, they all had the ability to craft the agreement in a manner which reflected their interests. Arising as it did in the context of a broader negotiation, cross-issue trades undoubtedly played some part in obtaining the agreement.

Non-Members. Those that do not accept the obligations of the agreement should not enjoy its benefits. India did not sign the AGP. However, its government argued that because of the MFN provisions of the GATT, Indian firms should be treated in the same way as those from countries that had signed the agreement. The case brought by India against the USA clarified, however, that the general MFN provisions of the GATT do not apply to the AGP.

Dispute Settlement. Originally, the AGP and other Tokyo Round codes had their own dispute settlement procedures. However, after the Uruguay Round, these procedures were replaced by those of the Dispute Settlement Understanding. (DSU). By and large disputes under the AGP follow the general procedures laid out in the DSU (such as consultations, panel hearings, appeals etc). One difference, however, is that panelists are only drawn from members who have signed the agreement. “Only members of the WTO

Party to this agreement shall participate in decisions or actions taken with respect to disputes under this agreement. “⁴

Retaliation. If a party to the agreement is found to have violated the agreement and fails to come into compliance, other parties can be authorized to suspend concessions. These authorizations are made by the panel that heard the dispute. *However, only obligations from the GPA itself can be used for these suspensions.* No cross-agreement retaliation is allowed. “Suspensions of concessions or other obligations under the Agreement on Government Procurement cannot result from any dispute arising from other agreements and any dispute arising under the AGP agreement shall not result in the suspension of concessions or other obligations under any other Agreement”⁵

Should these rules of the AGP be emulated by other clubs? Let us consider them in turn:

Participation. Should all members be allowed to participate in the negotiations as they were in the case of the AGP? My answer would be yes. Regardless of whether they currently wish to join, all WTO members have an interest in the nature of the rules determined by the institution. Indeed, the ability to participate in deliberations should be a fundamental feature of membership in the overarching club of clubs. Currently, any sub-group of WTO members could negotiate a pluri-lateral agreement relating to issues not covered by the WTO outside the WTO. (This would have been the case, for example, had the ill-fated Multilateral Agreement on Investment (MAI) actually been negotiated). And forming a club outside the WTO could be the fallback position if recalcitrant

⁴ Agreement on Government Procurement (AGP) Art XXII, 3.

⁵ AGP Art XXII, 7

members that had no intention of joining a club chose nonetheless to use the consensus rule to block other members from forming a club under the aegis of the “club of clubs.” However, important benefits could result from conducting the negotiations under the WTO aegis: namely, the legitimacy conferred by the stamp of approval of the organization, access to WTO resources and dispute settlement facilities, the ability for other members in the future to join a club with rules that they had previously endorsed and the ability to integrate club formation into other negotiations to allow for cross-issue trades.

This approach would represent a noteworthy contrast with MAI approach in which one group negotiating an agreement and presenting it to new possible members as a *fait accompli*. To be sure, some might object to having members who have no intention of every joining a club from having a say in its rules, but it would be problematic to identify such members before the club is actually formed. After all, even those intending to join would not commit themselves unconditionally before the specifics of the agreement had been laid.⁶ Instead, it is more appropriate for an organization of sovereign nation states to assume that all those who participate in a negotiation are acting in good faith.

Launching. New clubs and amendments to club rules could certainly be formed as part of new Rounds as were the plurilateral codes, such as the AGP that were the result of the Tokyo Round. Under these circumstances, if combined with the consensus requirement for establishing a club, there could be some cross-issue trading. However, one of the benefits of a club of club approach is that it could also allow for agreements to be negotiated outside the confines of Rounds. The Club of Club approach would thereby

⁶ It would be possible to limit the ability to amend all or some parts of the agreement to members that had signed it.

facilitate early harvests and could help to make future rounds more focused and less complex and time-consuming.

Treatment of non-members. Provision of benefits to non club members signatories should not be required, as was the case with the AGP but they could be allowed. Doing otherwise would clearly reduce the incentives to join. For example, as part of a competition-policy club, members might agree to extend “comity” to each other i.e. more extensive cooperation in anti-trust enforcement. They might be willing to do the same for less developed WTO members but not for developed members that refused to reciprocate. Thus developed country WTO members might not be allowed to free-ride but the least developed WTO members might enjoy some benefits without assuming obligations. In addition, even when they are not part of the club, outsiders may derive benefits. For example, if a group of countries agree to implement a set of standards all who compete with them may benefit, regardless of whether or not they are part of the agreement.

Dispute Settlement. Clubs should be required to use the WTO system for settling disputes. In particular, using a common Appellate Body would help assure cross-club consistency in the interpretation of the rules. This would represent an improvement over the approach adopted in the Tokyo Round in which each code had a separate dispute settlement system and there was no overall Appellate Body. However, there is some logic to the AGP provision that panels should be drawn from neutral members of the Club and not more broadly from the WTO. Again this might create a small additional incentive to join the club and it could be argued that countries actually implementing codes could have a better understanding of their operation.

Cross-Retaliation. The great attraction of the WTO for many proponents of new issues is the ability to use the enforcement mechanism and in particular the suspension of tariff concessions for enforcement. For example, advocates of TRIPs were particularly eager to have it made part of the single undertaking and enforced via the DSU. To be sure the DSU has provisions which call for retaliation to take place under the same sector and agreement in which the violations occur,⁷ but adherence to these provisions are not obligatory and countries are given considerable scope to engage in cross-sectoral retaliation. Countries committing TRIPs violations could therefore face trade retaliation. This phenomenon, which Steve Charnovitz has aptly termed “sanctions envy”, runs the risk of attracting new issues to the WTO not because they are highly germane to its mission, but rather because of the desire to have them enforced through the DSU. Among other reasons, to avoid this development, it seems appropriate to confine the ability to suspend concessions only in the same club where the violations have occurred, as is done with the AGP. For example, only suspensions of concessions in competition policy could be used to respond to violations by members of the competition club. In addition, club concessions should not be used for cross-retaliation. For example, members should not be allowed to withdraw competition club concessions in response to violations under TRIPs, GATT or GATs.

To be sure this approach might mean that club rules would be enforced by a somewhat weaker process than in the core WTO agreements. But this is not necessarily a bad development. It could help to encourage members to join since there would be fewer risks associated with default. It would also re-enforce the idea of reciprocity that is

⁷ WTO Dispute Settlement Understanding, Art 22,3

fundamental to the retaliation process.⁸ Since they represent independent agreements, in principle, countries made concessions *in a particular club* to obtain the adherence of other members to that club's rules. Thus suspension would entail restoring the status quo ante the agreement until compliance is obtained. Members would not feel that by joining a club they could lose benefits they currently enjoy from the core agreements and trade retaliation in particular would not proliferate if the number of clubs expanded. This provision could also help deal with the disquiet felt by many countries, particular the LDCs that difficulties with adherence to particular rules (such as labor or environment) could be used as an excuse for protectionist retaliation

An additional option, particularly in response to frequent violations, could be the temporary suspension of membership until compliance was achieved. Suppose for example, there was a separate agreement on labor standards in which parties agreed not to weaken their labor laws to gain an advantage in trade. Assume a developing country was found to have done this recurrently. It could then lose the right to claim membership of the club. This might result in consumer disapproval.

As part of the overall WTO agreement a set of common provisions should be required of all clubs. In addition to the rules already mentioned, these could include provisions for:

Capacity-Building. Clubs should be required to explore possibilities of providing special and differential treatment and to make provisions for capacity building. One approach would be to unilateral provision of benefits ala GSP in which members could provide non-members from developing countries with benefits and rights but not require

⁸ See Robert Z Lawrence *Crimes and Punishments? Retaliation Under the WTO*. Institute for International Economics Washington DC 2003.

reciprocity. A second could entail a basic set of commitments for the least developed members and more extensive obligations by full members. In addition, clubs should be required to offer non-members with technical assistance and capacity building opportunities to allow them to become fully-fledged members.

Binding Obligations A central purpose of the WTO is to establish the rule of law in the trading system. This is not going to be achieved if agreements are not mandatory. Thus in all cases, adherence to club rules should be binding on all members, and all clubs should be required to use the enforcement provisions described above. In addition, clubs should be open to all WTO members that are willing accept their rules. Clubs should have discretion over whether to admit non-WTO members.

Pluses and Minuses.

The Club of Clubs approach has much to recommend it. It could facilitate the expansion of trade-related issues that the WTO could cover yet also accommodate countries that felt their interests were not served by a particular set of rules. Those members that wish to pursue deeper international integration through a multilateral route could do so within the framework and under the aegis of the WTO while others who viewed such obligations as ill-suited to their needs or capabilities would not be obliged to join. In some cases, non-members would automatically benefit if countries make their domestic markets more contestable, or improve their environments or raise their labor standards.

The club of clubs could help ensure a better alignment between mission and means since it would reduce implementation burdens that might otherwise arise. It is far better to exercise caution in extending obligations to countries that are both ill-equipped

to assume them and ill-equipped to refuse than to have countries resent being forced to accept obligations they believe to be burdensome. Increased differentiation among members is surely compatible with the notion of special and differential treatment. Indeed the club of clubs approach embodies differential treatment.

All of these features could bolster the institution's legitimacy. No country could be forced to join a club it did not feel served its interest. At the same time, the WTO would provide a framework in which those interested in implementing an agenda of deeper international integration would be able to do so. Simultaneously the Club of Club would address the concerns of those who believe the organization should do more to promote such integration and those who believe that countries should not all be subject to the same rules and obligations.

Having the clubs as part of the WTO would provide advantages. It could allow all members to participate in drafting the club rules and thus increase the likelihood that provisions commanding universal support would be adopted. This would also reduce the danger that a group of members would try to set the bar so high that others would be precluded from joining. Although clearly to a lesser degree than would be the case with a single undertaking, having the clubs formed during WTO rounds would also facilitate cross-club concessions. Members not yet ready to join, could also be assured that once they became ready they could not be excluded from membership.

In sum, as the experience of the European Union illustrates, it is highly problematic to apply a one size fits all approach to deeper economic integration. The diverse nature of WTO membership makes it highly unlikely that members will all be willing and able to sign on to the full range of agreements that many members might find

desirable. The club of clubs approach seems to offer an avenue for compromise in which diversity can co-exist with a more extensive set of commitments.

This club of clubs approach could however give rise to some concerns. One is that it might create a WTO with two classes of citizens, the first class nations that are members of the clubs, and the second class nations that are not. However, one of the great strengths of the WTO is that there are already distinctions among the obligations assumed by members. These range from different tariff rates, different proportions of bindings, special and differential treatment and different speeds with which agreements have to be phased in. Moreover the upside of a two-tier system is that it will be more difficult to compel countries to accept obligations.

A second concern is that a few developed country club members will establish a template and setting the bar too high and later force others to join. Here the fact that the Uruguay Round induced many members to accept and implement most of the Tokyo Round Codes is seen by some as a troubling precedent. But if clubs are made an intrinsic part of the WTO architecture, this would be less likely. Indeed, the lesson of Cancun is that many developing countries have learnt from their experiences in the Uruguay Round about the pitfalls of accepting obligations that they would have difficulties in implementing. They are unlikely to repeat the same mistakes again. Moreover, the rule that permits all members to engage in the negotiations over the club rules should limit the possibilities of agreements which do not command widespread support among the members.

A third worry would be the weakening of the ability to engage in cross-issue trades. Several members have argued for example that the inclusion of agreements on

investment and competition were vital to obtain the support necessary for their making meaningful concessions on agriculture. It is an open question whether or not the launching of an investment club or a competition club could serve a similar purpose. Much would surely depend on whether sufficiently large numbers of countries were prepared to join the club. Nonetheless, the ability to condition concessions on the acceptance by others of club membership would still exist.

A fourth concern is that the approach might reduce the possibilities of agreements with universal coverage. It is certainly true that if most major countries could be persuaded to accept a particular agreement, in a system based on a single undertaking, it would be likely that all WTO members would agree to join. By contrast, if the agreement was part of a separate club, it would be more likely that some members might decide not to join. But the requirement of a single undertaking also has the effect of making other agreements less likely, whereas the club of clubs could make progress with a pluri-lateral agreement when the single undertaking would fail to obtain any agreement at all.

A fifth concern is that enforcement and thus compliance would be weaker in the clubs if the procedures outlined above were to be followed – in particular confining retaliation to the suspending obligations within the same club. This could imply that compliance with agreements might be weaker. This might well be the case, but it is important not to exaggerate the role that retaliation actually plays in enforcement – the record of compliance under GATT was good despite the absence of actual retaliation.⁹

⁹ See Robert E. Hudec, 1991 *Enforcing International Trade Law: The Evolution of the Modern GATT Legal System* (Austin Texas: Butterworth Legal Publishers)

By and large, it appears that in any case, the role of reputation is probably more important than retaliation in obtaining compliance.

A sixth is that the approach could limit the ability of members to obtain agreements that they are particularly interested in. A similar logic applies to legislation that can pass when measures are combined (or log-rolled) into a package when each could not pass if there were individual votes. Each party supports the package because it comes out ahead on balance but many parties would prefer to drop some items from the package. Thus a single undertaking could achieve some results which could not be attained through the club-of-clubs. But this approach will mean that members will accept obligations not because they view them as beneficial but simply because they are willing to trade them for something else. In the long run, however, both the institution and its members will be better off if members subscribe to rules they believe are all in their interest. At the end of the day there may be fewer universal rules, but those that are applied will command more support.

Conclusions.

For all the talk of globalization, the world economy remains highly fragmented as the economic effects of borders inhibit the realization of more global economic integration. The WTO has a key role to play in helping nations reap the full benefits of deeper integration but as its mission and means have expanded it has become more controversial. The organization's legitimacy has been attacked from many quarters and efforts to add new issues to the rules have foundered, as many members have refused to accept new obligations on a variety of grounds that include problems in implementation,

fears these could result in trade retaliation, and views that they will constrain the scope for differentiated domestic policies.

Supplementing the core WTO obligations with a club of club approach could help to promote deeper global integration while at the same time alleviate some of the WTO's institutional problems. The club of clubs offers a compromise in which diversity can co-exist with a more extensive set of commitments for willing members. Clubs would be chosen were they could help promote the central missions: lowering barriers to trade; reducing the discriminatory effects of domestic policies and enhancing economic development through trade. All WTO members would participate in negotiating club rules, but members would be free not to join. Clubs would use the DSU to deal with disputes but suspension of concessions in the event of violations would be confined to the provisions of the same club in which the violation occurred.

The club of clubs approach might reduce the ability of some members to obtain agreements by packaging them in a single undertaking. It could also reduce the power of retaliation as an enforcement mechanism for certain obligations. But the approach could also enhance the legitimacy of the WTO by helping members to avoid undertaking obligations they did not view as in their interest. It would thereby ensure a better alignment between mission, means and legitimacy, the keys to a more effective international organization.