The Dark Side of the Moon: ‘Completing’ the WTO Contract through Adjudication*

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Abstract

The WTO dispute settlement system has a lot to brag about. It is unique in international relations in that its innate feature is compulsory third party adjudication. The WTO has become a busy forum for state-to-state international litigation, attracting record numbers of disputes since 1995. In this paper, we focus on quality of the case law the system ‘produces’. We argue that WTO ‘courts’ have failed to ‘complete’ the contract in important, indeed quintessential, areas of world trade law. Judicial mishaps can occur in any system and in principle new, ‘more complete’, legislation can take care of problems that arise. Unfortunately in the WTO completion of the contract through (re-)negotiation is not a realistic option; the stalled Doha Round illustrates the problem. We point towards a number of institutional improvements that can help WTO adjudicating bodies to better honour their function of clarifying (‘completing’) WTO law.

* The views expressed are personal and should not be attributed to the World Bank.
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Introduction
Following an extended period during which both industrialized and developing countries maintained high barriers to trade, starting in the mid 1980s governments began a process of mostly unilateral liberalization. As of 2010, the average level of import protection was some 10 percent or less in many developing countries, and the average uniform tariff equivalent of merchandise trade policies in OECD countries had fallen to less than 4 percent. Imports of many manufactures are now duty-free. The policy reforms helped generate a boom in world trade. The value of global trade in goods and services passed the US$15 trillion mark in 2006, up from around US$1 trillion in the late 1970s (measured in current dollars). The global value of the stock of foreign direct investment (FDI) rose more than 6-fold between 1990 and 2008, substantially faster than the growth in trade, which increased ‘only’ 3.5 times over the same period.

The change in attitude towards trade policy was reflected in the stances taken by many countries in the Uruguay Round of multilateral trade negotiations, which resulted in major ‘structural change’ of the global trade regime. As is well-known, rules for agricultural policies were greatly strengthened and agreements were reached to discipline the use of a variety of instruments of contingent protection, including antidumping and voluntary export restraints. New rules were negotiated on policies affecting trade in services and measures to protect intellectual property rights. Equally important were the changes that were made to the GATT dispute settlement system, with the shift to a two-level system of adjudication and the removal of the possibility of a party to a dispute blocking the adoption of a dispute settlement ruling.

The WTO is in many ways a unique international organization, but perhaps most distinctly in having a binding dispute settlement mechanism. The institution has proved to be rather effective in sustaining cooperation: as of end August 2012, WTO members had formally raised 445 disputes, most of which were concluded with the losing party bringing its measures into compliance. The dispute settlement system has been used by an increasing number of WTO members, including developing and emerging market economies. Developing nations were defendants in only 8 percent of all the cases brought during the GATT years; in the WTO period this rose to 30 percent.1 Developing countries accounted for about one-third of all complaints during 1995-2011. They increasingly use WTO procedures against each other—44 percent of all complaints were directed at other developing countries. This can be explained in part by proximity – states taking action against a trading partner that is nearby and with which it has more intense trading relationships – but also by the fact that some one-third of all WTO cases pertain to AD/CVD/XIX and most such actions are directed against developing countries.2 The largest emerging markets – Brazil, China, India – account for over one-

1 Horn et al. (2011).
2 This reflects both the increasing use of such instruments by developing countries and the detailed procedural requirements that are laid out in the relevant WTO agreements. In Brazil and China, AD covers around 2 percent of total imports; in India – now the world’s most active user – it is 4 percent (Bown, 2011).
third of all cases brought by developing countries, but smaller middle-income states such as Argentina, Chile, Mexico, and Thailand have also been very active. About one-half of the 15+ cases brought by Argentina are against other Latin American nations; for Chile the figure is 60 percent; for Mexico, 30 percent; and for many Central American states it is 50 percent or more. Conversely, East Asian countries generally do not challenge regional partners before the WTO. It is also striking that to date large emerging markets (Brazil, China, India) have not been challenged very frequently by developing countries. Moreover, Brazil has never contested a measure taken by India or China; India has taken only one case against Brazil; while China has not launched any cases against a developing country.\(^3\)

The advent of the WTO, and the ensuing establishment of a two level-adjudication mechanism, marked the passage to a compulsory third party-adjudication system. This is an oddity in international relations: as per Art. 23 DSU, WTO adjudicating bodies become the exclusive forum for adjudication of all disputes between WTO Members with respect to issues coming under the purview of the covered agreements. This feature (exclusive adjudication), along with the fact that more and more issues have come under the purview of the multilateral trading system as a result of the Uruguay Round, helps explain the substantial increase in the number of WTO disputes and reports compared to the GATT-era.\(^4\)

Views on the operation of the DSU differ widely, in part reflecting the perceptions of observers regarding the ‘legitimacy’ of the institution and the rules of the game that have been negotiated. Some argue that the WTO dispute settlement system gives too much discretion to unelected judges to write law; others take the view that judges have inadequate scope to interpret agreements. In this paper we review certain aspects of the performance of the WTO dispute settlement process, focusing in particular on the extent and effectiveness of WTO adjudicating bodies in ‘completing the contract’. We believe that this is a very important dimension of the dispute settlement process as it has a major bearing on the feasibility of operationalizing many of the proposals that have been put forward in the DSU review to strengthen the dispute settlement mechanism.

1. The Institutional Role of the WTO Adjudicating Bodies

Dispute settlement in the WTO aims at maintaining the balance of negotiated concessions. Art. 3.2 of the WTO Dispute Settlement Understanding (DSU) reads:

> The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system. The Members recognize that it serves to preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law. Recommendations

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\(^3\) The large developing nations instead rely more of diplomatic processes. An example is a China-India trade remedy working group that was formed to discuss concerns about antidumping investigations and avoid launching of investigations in the first place. China is the target of the majority of Indian AD cases (Krishnan, 2012).

\(^4\) Hudec’s monumental study (1993) reveals that fewer reports were issued between 1947-1993 than in the first 15 years of the WTO. There are of course many mitigating factors.
and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements.

It follows that Panels (the first instance court), and the Appellate Body (AB, the second instance court) cannot extend or reduce the policy space that has been negotiated and agreed by the principals (the WTO Members). However, WTO judges must clarify (interpret) WTO law. As discussed below this will sometimes imply ‘completing the contract’.6

**Who are the WTO ‘Judges’?**

Dispute settlement Panels are overwhelmingly staffed by (former) members of WTO delegations, and, on occasion, by outside experts that are pre-selected (pre-approved) by the membership. The Appellate Body (AB) comprises seven members who have 4-year appointments that are renewable once. Cases are judged by three of the seven members. AB members are required to be ‘...persons of recognized authority, with demonstrated expertise in law, international trade and the subject matter of the covered agreements generally. They shall be unaffiliated with any government’ (Art 17:3 DSU).

AB members are nominated by individual WTO members and appointed by consensus by the DSB. The consensus rule implies that any candidate – or AB member who is up for re-appointment – can be blocked by any dissenting WTO member. Elsig and Pollack (2012) document that over time the process of AB appointments has become more politicized, and that major players increasingly scrutinize and ‘vet’ the nominees they decide to put forward or agree to support in an effort to ensure that their views are consistent with their own. The more careful vetting is a reflection of the increasing importance of dispute settlement activities and concerns by governments regarding the substantive views and philosophical approach of AB members, especially with respect to ‘filling in the gaps’ that are created by ambiguous language in the WTO agreements – perceived by some WTO members as inappropriate judicial activism when decisions imply outcomes that conflict with their preferences. The limited terms for AB members imply relatively rapid turnover and greater control by the principals—the WTO members—over the ‘type’ of persons that sit on the AB. We will return to this matter in the concluding section.

**WTO ‘Judges’ Clarify the Content – Flipping a Coin is not Enough**

Art. 11 DSU, the companion provision to Art. 3.2 DSU, states that, when interpreting a provision, Panels must make an objective assessment of the matter before them: 7

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5 In this paper we will use the terms ‘judge’ and ‘court’ for descriptive convenience although this is of course not WTO parlance. The Appellate Body is a body, not a court; the persons appointed to sit on it are ‘members’ not ‘judges’. This terminology reflects the history of dispute settlement in the GATT, which was more diplomatic in nature than legalistic/judicial, and many WTO members were concerned to circumscribe the role of the AB to ensure that it would not get into the business of writing law or have the stature of a supreme court. Art. 3.2 DSU is a reflection of that concern.

6 This is quite distinct from ‘judicial activism’ or ‘writing law’, which is clearly circumscribed by the DSU.

7 Any assessment by a judge is of course a subjective assessment. However, in light of the negative connotation that the term ‘subjective assessment’ has, by convention reference is not made to it in a provision such as Art. 11 DSU.
The function of Panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, a Panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements. Panels should consult regularly with the parties to the dispute and give them adequate opportunity to develop a mutually satisfactory solution.8

This provision explicitly reserves to WTO ‘judges’ some room for manoeuvre within the limits of the available policy space as explained in Art. 3.2 DSU: clarification is not a simple flip of a coin since the WTO ‘judge’ must follow an intellectual path that ensures that the policy space that WTO members have retained is not circumscribed.

The WTO is, on occasion, a highly incomplete contract, in that the texts of negotiated agreements do not contain all the information necessary for its operation. Take for example, the national treatment provision. For good reasons negotiators refrained from spending time trying to provide a complete list of all domestic instruments that should come under the purview of Art. III GATT:9 had they decided to bind all domestic instruments, the list would have been long as never before, and they would find themselves in a permanent state of negotiations since social preferences change over time and sometimes may do so quite rapidly. Another illustration is offered by the fact that the DSU nowhere regulates the allocation of burden of proof.10

By interpreting the covered agreements, WTO adjudicating bodies will address instances where the contract is incomplete by ‘adding’ the missing information.11 This is necessary in order to be able to apply generic language (as is often found in many WTO provisions) to a transaction-specific context. As Posner (1995) explains, there is tension between the willingness of the legislator to draft laws using all-encompassing language in order to subsume the maximum number of transactions, and the limits inherent in our human nature to predict future events (state-contingencies) on which we have, at the stage of drafting, imperfect information. This tension is particularly prevalent in a contract such as the WTO, which is between sovereign governments in a setting where there is no central enforcement mechanism, and that is not meant to be transaction-specific but instead aims to regulate future trade relations (after the negotiation of an agreement). As a result, negotiators will naturally privilege generic expressions, rather than seek to employ precise definitions. The more we move away from a transaction-specific language, however, the greater the ambiguity that may arise. Take the term ‘like

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8 Although this provision explicitly mentions Panels and not the AB, the latter has consistently held in its case-law that it is bound by it as well.

9 There is a positive correlation between the amount of information contained in a contract and what can be achieved through the contract at hand. Adding information gives rise to negotiating costs so that negotiators might reach a point of diminishing returns: negotiations take a long time and might not yield satisfactory results. Thus negotiators will assess the merits of including additional information against the ensuing expected returns.


11 See Horn et al. (2010) for a formal model and analysis of the role of the WTO judge as the entity completing the missing information and thereby making the outcome of adjudication more predictable.
product’, for example, which appears frequently in WTO agreements: depending on the specific comparator used, one can reach different (internally coherent) interpretations. The WTO framers were mindful that the privileged term was sub-optimal and prone to misunderstandings and yet could not come up with a better solution. It is therefore not paradoxical that different Panels, and the AB, have reached different interpretations.

**Recourse to the Vienna Convention on the Law of Treaties: a Curse, not a Blessing**

WTO adjudicating bodies are not free to choose any intellectual route when interpreting the contract. Art. 3.2 DSU imposes on the WTO judge recourse to customary rules of interpretation. Starting with its very first report, the AB has equated customary rules to the general rule of interpretation embedded in the Vienna Convention on the Law of Treaties (VCLT). The VCLT is far from being exact science; it reflects various elements of interpretation, but falls short of establishing with precision the weight to be given to each element. Hence, it is not unheard of that, in the name of the VCLT, courts have reached divergent decisions on more or less identical issues. In other words, formal recourse to the VCLT does not ipso facto yield consistent results.

An illustration is probably appropriate at this point. In the two decisions by the AB on recurring subsidies, US–Lead and Bismouth II and US–Countervailing on Certain EC Products, the AB arrived at diametrically opposite responses to the same question, i.e., to what extent do non-recurring subsidies pass through to a new owner who has paid a market-determined price for a privatized entity? In both instances the AB made recourse, as it always does, to the VCLT. On both occasions, it went through each and every element enshrined in Art. 31 VCLT. A reading of the reports does not suggest that different weights were given to the elements of the VCLT. Yet, the outcome is not the same; the first report stands for the proposition that an arm’s length transaction always exhausts the benefits received by the former owner, whereas the second takes the view that this is not necessarily the case.

Why has this been the case? The WTO judge is called to interpret one incomplete contract through another incomplete contract. This is definitely not an envious position to be in and is a factor that should be considered whenever criticism is voiced against decisions by WTO adjudicating bodies. Errors are thus not excluded. Through commission of errors, WTO ‘judges’ are not only imposing costs on the addressees of decisions, but are also creating institutional damage as well: they might reduce the

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12 Irwin et al. (2008) report that the GATT framers had agreed to renegotiate this term in the context of the wider ITO (international Trade Organization)-negotiation. The collapse of the ITO had as consequence the absence of new negotiation of the term.

13 There is a presumption expressed in Art. 3.2 DSU, that recourse to the VCLT guarantees, in principle at least, that the balance of rights and obligations, as struck by the founding fathers, will not be undone by the judge.

14 Not that consistency is in and of itself a value, for one can be consistently wrong. Assuming correct interpretations however, a court gains in institutional credibility when it can show a consistent pattern of decision-making. In such cases, the presence and demonstration of distinguishing factors from one case to the other will sufficiently justify divergent outcomes.

15 In the view of Grossman and Mavroidis (2007) both reports are wrong.

16 WTO adjudicating bodies pronouncing a false positive (Type I error) will be adding to the obligations of WTO Members, whereas, through a false negative (Type II error), will be diminishing their rights.
faith of trading nations in this form of dispute adjudication, in an era where compulsory third party adjudication is very much a rarity in international relations.

**Redeeming Factors (for Judicial Errors)**

1. **No Stare Decisis**

There is no formal stare decisis (binding precedent) in the WTO. As a result, errors do not have to be repeated. This mitigating factor however, should be taken with a pinch of salt: there is legitimate expectation that Panels will adhere to case law as established by the AB. Indeed, the AB, in its report on *US–Stainless Steel (Mexico)*, re-visited all prior case law, and held that it expected Panels to follow prior AB findings dealing with the same issue (§§158-162):

It is well settled that Appellate Body reports are not binding, except with respect to resolving the particular dispute between the parties. This, however, does not mean that subsequent panels are free to disregard the legal interpretations and the ratio decidendi contained in previous Appellate Body reports that have been adopted by the DSB. In *Japan – Alcoholic Beverages II*, the Appellate Body found that:

> [a]dopted panel reports are an important part of the GATT *acquis*. They are often considered by subsequent panels. They create legitimate expectations among WTO Members, and, therefore, should be taken into account where they are relevant to any dispute.

In *US – Shrimp (Article 21.5 – Malaysia)*, the Appellate Body clarified that this reasoning applies to adopted Appellate Body reports as well. In *US – Oil Country Tubular Goods Sunset Reviews*, the Appellate Body held that "following the Appellate Body’s conclusions in earlier disputes is not only appropriate, but is what would be expected from panels, especially where the issues are the same."

Dispute settlement practice demonstrates that WTO Members attach significance to reasoning provided in previous panel and Appellate Body reports. Adopted panel and Appellate Body reports are often cited by parties in support of legal arguments in dispute settlement proceedings, and are relied upon by panels and the Appellate Body in subsequent disputes. In addition, when enacting or modifying laws and national regulations pertaining to international trade matters, WTO Members take into account the legal interpretation of the covered agreements developed in adopted panel and Appellate Body reports. Thus, the legal interpretation embodied in adopted panel and Appellate Body reports becomes part and parcel of the *acquis* of the WTO dispute settlement system. Ensuring "security and predictability" in the dispute settlement system, as contemplated in Article 3.2 of the DSU, implies that, absent cogent reasons, an adjudicatory body will resolve the same legal question in the same way in a subsequent case.

In the hierarchical structure contemplated in the DSU, panels and the Appellate Body have distinct roles to play. In order to strengthen dispute settlement in the
multilateral trading system, the Uruguay Round established the Appellate Body as a standing body. Pursuant to Article 17.6 of the DSU, the Appellate Body is vested with the authority to review "issues of law covered in the panel report and legal interpretations developed by the panel". Accordingly, Article 17.13 provides that the Appellate Body may "uphold, modify or reverse" the legal findings and conclusions of panels. The creation of the Appellate Body by WTO Members to review legal interpretations developed by panels shows that Members recognized the importance of consistency and stability in the interpretation of their rights and obligations under the covered agreements. This is essential to promote "security and predictability" in the dispute settlement system, and to ensure the "prompt settlement" of disputes.

The Panel's failure to follow previously adopted Appellate Body reports addressing the same issues undermines the development of a coherent and predictable body of jurisprudence clarifying Members' rights and obligations under the covered agreements as contemplated under the DSU. Clarification, as envisaged in Article 3.2 of the DSU, elucidates the scope and meaning of the provisions of the covered agreements in accordance with customary rules of interpretation of public international law. While the application of a provision may be regarded as confined to the context in which it takes place, the relevance of clarification contained in adopted Appellate Body reports is not limited to the application of a particular provision in a specific case.

We are deeply concerned about the Panel's decision to depart from well-established Appellate Body jurisprudence clarifying the interpretation of the same legal issues. The Panel's approach has serious implications for the proper functioning of the WTO dispute settlement system, as explained above. Nevertheless, we consider that the Panel's failure flowed, in essence, from its misguided understanding of the legal provisions at issue. Since we have corrected the Panel's erroneous legal interpretation and have reversed all of the Panel's findings and conclusions that have been appealed, we do not, in this case, make an additional finding that the Panel also failed to discharge its duties under Article 11 of the DSU.

In *US-Continued Zeroing* the Appellate Body expounded this approach (§362):

Following the Appellate Body's conclusions in earlier disputes is not only appropriate, it is what would be expected from panels, especially where the issues are the same. This is also in line with a key objective of the dispute settlement system to provide security and predictability to the multilateral trading system. The Appellate Body has further explained that adopted panel and Appellate Body reports become part and parcel of the *acquis* of the WTO dispute settlement system and that "ensuring 'security and predictability' in the dispute settlement system, as contemplated in Article 3.2 of the DSU, implies that, absent cogent reasons, an adjudicatory body will resolve the same legal question in the same way in a subsequent case." Moreover, referring to the hierarchical structure contemplated in the DSU, the Appellate Body reasoned in *US – Stainless Steel (Mexico)* that the "creation of the Appellate Body by WTO Members to review legal interpretations developed by panels shows that Members recognized the importance of consistency and stability in the interpretation of their rights and obligations under the covered agreements." The Appellate Body
found that failure by the panel in that case to follow previously adopted Appellate Body reports addressing the same issues undermined the development of a coherent and predictable body of jurisprudence clarifying Members’ rights and obligations under the covered agreements as contemplated under the DSU.

There are few instances where Panels did not follow rulings by the AB: in EC–Commercial Vessels, for example, the Panel refused to adhere to the AB’s understanding of Art. 18.1 AD, as expressed in its US–Offset Act (Byrd Amendment) report. A series of Panels have distanced themselves from the AB’s outlawing of the zeroing practice in antidumping investigations. The AB itself has consistently referred in its own prior reports. There are of course, cases where the AB has departed from prior case law, like the pass through-jurisprudence referred to above. But from a quantitative perspective they represent exceptions rather than the rule.

2. ‘Soft’ Remedies are a Mitigating Factor

If a member is found to have violated a commitment, the remedy is prospective: the offending member is simply called upon to bring its measures into compliance. How this should be done is left to the WTO member to determine. There is no requirement to compensate for losses imposed while a violation occurred. In cases where a member does not comply with the DSB, a member may be authorized to retaliate in an amount that is equal in effect to the action that was taken by the country that violated a commitment. Ethier (2009) notes that, due to the uncertainty as to the identity of the defendant (and the soundness of the judgment), WTO Members have agreed to ‘softer’ remedies than they otherwise might have done. Governments do not want to subject themselves to a process where they may be subject to penalties that they deem inappropriate given the absence of ex ante specificity on the rules that will apply. This may be so in particular for countries that expect to be both complainants and respondents over time. Ethier (2009) argues that this gives countries an incentive to agree to remedies that are limited in scope, i.e., that is constrained to maintaining the original balance of concessions.

In the WTO-era (the post-1995 period) all Panels have, with one exception, recommended prospective rather than retroactive remedies. Implementation of adverse WTO decisions is less costly (than in case retroactive remedies had been recommended), since only prospective implementation is required; although formally there is no efficient breach of contract in WTO law, parties that can afford to, can always opt to be subjected to countermeasures, rather than implement a decision.\footnote{The Panel on US-Shrimp and Sawblades discussed this issue extensively underscoring the caution expressed by the AB against Panels that refuse to adhere to its decision. China, in this Panel’s view, had adduced prima facie evidence simply by invoking the case law condemning zeroing (§§7.25ff.).}

\footnote{WTO members have been unwilling to go down the compensation track, due to uncertainty regarding the possible repercussions (potential liability). Some countries have also argued that their legal systems prohibit compensation. Historically, developing countries have favored the introduction of rules that would allow for claims for monetary damages to be paid to them in instances where illegal measures are imposed against them by industrialized nations. Not surprisingly, GATT contracting parties always rejected this. ‘Money damages, said the developed countries, were simply outside the realm of the possible. In effect, they were saying, GATT was never meant to be taken seriously’ (Hudec, 2002).}

\footnote{See Bagwell et al. (2006) for an account of such cases. We do not suggest here that all implementation is non-costly. We further do not mean to say that performing the contract and being subjected to
Strong enforcement is of course, more of a threat to ensure compliance, but can have the perverse effect of inducing countries to make fewer commitments in the first place, resulting in an outcome that is inferior to one where there is weaker enforcement – in that the expected benefits of cooperation are higher (Lawrence, 2003). It also mitigates the impact of judicial error. To be sure, the use of ‘soft’ remedies in the WTO context does not make judicial errors mundane: a wrong judgment is almost never limited to the transaction it addresses as it raises the expectation that similar treatment will apply to similar transactions in the future.  

3. Potential to Address Problems by Re-negotiating the Contract

An obvious solution in principle to problems arising from an incomplete contract is to pursue re-negotiation. Renegotiation in the WTO setting is costly and uncertain, both in terms of the time it takes and the prospects of a successful outcome. Kennedy (2010) discusses the only example to date of an amendment to the WTO—the resort to compulsory licensing of medicines protected by patents. Although eventually there was unanimity across WTO Members as to the conditions under which developing countries could use compulsory licensing to this effect, the negotiation to get such agreement took years, and as of the time of writing it has yet to formally enter into force for lack of adequate number of ratifications. The only realistic option is therefore adjudication.

2. Assessing the Performance of the WTO Judges

The operation of the WTO dispute settlement system has been the subject of a huge literature as well as a review process mandated by a Uruguay Round Ministerial Decision that became part of the Doha Round agenda (although not formally part of the single undertaking). The DSU review generated numerous proposals to strengthen the DSU. Many of the proposals put forward in the review (and more generally in the academic literature) involve a significant strengthening of the system – e.g., moving to a permanent Panel body (a true first instance court); additional rights for third parties in disputes; converting AB appointments into full-time, dedicated positions; mandating greater use of economic analysis in cases. Others aim at making the process more transparent – e.g., multilateral review of bilateral settlements; public access to the dispute settlement process.

countermeasures are of equal value. Legally, they are not. Art. 22 DSU clearly proscribes that suspension of concessions (countermeasures) is a temporary measure until compliance has occurred. In practice, however, the opposite could very well be true. However, a property rule is established only in name, and the transitional liability rule could de facto become a permanent solution.

20 We can also note that remedies are not that soft for those with weak bargaining power, although in theory at least, they can profit from ‘cheap’ exit from contractual obligations from the moment of the commission of the illegal act until the end of the compliance period to implement an adverse DSB ruling. This raises issues that are beyond the scope of this paper.

21 We do not refer here to renegotiations of tariff duties. These do not deal with the text of the agreement but only with the level of bound tariffs. On this score, see Hoda (2001).

On occasion there have been voices raised by institutional players against the reasoning adopted and/or the final decision itself. Reports will be adopted by negative consensus, and the defendant might find it appropriate to signal, at the DSB meeting, its disagreement with the report. Mexico, for example, expressed in very explicit terms, its disagreement with the rationale and the findings of the report on Mexico–Telecoms when it was presented for adoption (WTO Doc. M/170 of July 6, 2004). Similar voices are not that frequent though. It is probably the inevitability of the whole endeavour that explains the passivity of WTO members in this respect: AB reports cannot be appealed, and recourse to countermeasures cannot be blocked either. The mitigating factors noted above (‘soft’ remedies) also help in understanding the prevailing situation.

(Some) Academics Beg to Differ

Starting in 1999, the American Law Institute (ALI) has undertaken a project that analyzes all the case law of the WTO (i.e., Panel reports that have not been challenged and AB reports). Each case report is written jointly by a lawyer and an economist, who are asked to assess whether the outcome of the case is satisfactory, and if not, whether the source of dissatisfaction lies in the interpretation of the law by the Panel/AB, or the law itself. This, to our knowledge, is the only consistent mechanism for detailed monitoring of the ‘quality’ of the output produced by Panels and the AB. It is particularly useful for the purpose of this paper as authors are requested to pronounce on the reasonableness of the approach taken by an individual Panel and/or the AB looking into the law as ‘completed’ through case law, and then, if unhappy with the final outcome, ask the additional question whether the source of their unhappiness lies with the case law understanding of the law, or the law itself.

Erroneous Outcomes as Opposed to Methodological Errors

Through 2011, ALI authors have completed 69 reports. In a quarter of these the authors have disagreed with the outcome (18/69). In almost 70 percent of cases (48/69) they have voiced concerns regarding the methodology used to reach the outcome. The latter is important in light of the previous discussion: the role of the WTO judge is to complete the original law and make the outcome of future similar cases predictable, thus reducing the number of cases in the future.

There are numerous cases where ALI authors have disagreed with the methodology used and it is impossible to reproduce them all here in light of the space constraints. For example, in 2011 three Panels dealt with the same issue in three cases involving the same issues (more or less) under the WTO Agreement on Technical Barriers to Trade (TBT) and reached irreconcilable positions. By definition the methodology cannot be correct across all three cases. The AB attempt to provide a methodology fell far short of expectations. As a result, at this stage, we are simply in the dark as to whether, when

23 All WTO reports are posted on the home page of the WTO (www.wto.org) as opposed to being printed in an obscure print publication as was the case in the GATT days (an annual publication, Basic Instruments and Selected Documents) that was difficult to access. Moreover, since all reports are adopted (via the negative consensus rule, where the will of the winning party suffices for a report to be adopted), they all become public. This was not the case in the GATT-years where only adopted reports, that is reports that both the winning as well as the losing party would concede to adopt, would become public. There is therefore undeniably much more transparency regarding WTO judicial reports than it ever was in the history of the multilateral trading system.
dealing with TBT disputes, the starting point should be the regulatory intervention because of the dissatisfaction with the market outcome, or the market itself.\footnote{See the critique by Howse and Levy (2012).}

We focus in what follows on non-discrimination, the most basic GATT obligation. Key elements in determining whether this rule has been violated are the definition of ‘like products’ and ‘less favourable treatment’, the two quintessential components of the obligation. WTO case law has become a nightmare, making it impossible to predict how the next case will be resolved. According to the law, once imported goods have paid their ‘entry ticket’ (whatever import duties and fees apply), they must be treated in the same manner as domestic goods. In order not to cast the net too wide, this obligation is relevant for like products only: WTO Members cannot afford less favourable treatment to imported goods than that granted to domestic like goods.\footnote{The terminology changes depending on whether the measures are fiscal or non-fiscal in nature, but the essence is the same.}

**Like products:** the AB insists that the test to define likeness is in the marketplace but has applied the test in such drastically different ways that it is impossible to understand how its test can be applied. In *Japan-Alcoholic Beverages II*, the AB accepted that sochu (a drink produced predominantly in Japan) and vodka were like products based on econometric evidence submitted by the complainants on cross-price elasticities to determine the degree of substitutability across the two products in the Japanese market. In *Korea-Alcoholic Beverages*, the AB held that soju (a drink produced predominately in Korea, but very similar to the Japanese sochu) and vodka were also like products, but this time made recourse to non-econometric indicators, looking at criteria such as consumer preferences, physical characteristics, end use of the products etc. In *Korea-Alcoholic Beverages*, the Panel and the AB looked at the Japanese market to see if sochu and vodka are like goods. They confirmed that this was the case indeed. Then, in light of the resemblance between soju and sochu they concluded that vodka and soju should be like as well. It did not respond to the Korean argument that soju’s price was a fraction of vodka’s price (the price ratio was about 1 to 14) and that for this reason alone, Korean consumers would never substitute soju (in its diluted form) for vodka. But if the second report is right, the first is wrong, or at best, partially right since arguably many goods beyond those examined in *Japan-Alcoholic Beverages II* are like goods to sochu even though they may be substantially cheaper or more expensive.

These cases were followed by *EC-Asbestos*, where the AB held that two goods are like or unlike depending on how a ‘reasonable consumer’ perceives them. This suggests no need to analyze market data or consumer surveys to determine the degree of substitutability of two goods, since all that matters is the opinion of reasonable people and arguably AB members are part of this class. How will the next case be adjudicated? With what we know so far, three reasonable people will decide on likeness. But these three people will have quite different backgrounds, education, religious beliefs etc. Thus, there is absolutely no guarantee regarding the outcome. Leaving it to three reasonable people to decide on likeness implies the absence of any methodology, with all the associated implications for uncertainty and predictability.
**Less favourable treatment (LFT):** in *Korea-Various Measures on Beef*, the AB held that modification of competition to the detriment of imported goods confers LFT. Koreans must still wonder how this could be the case: they had in place a legal quota on US beef. US beef was sold at prices substantially lower than that of Korean beef and traders were selling the former as Korean pocketing in the mark up. So Korea imposed a dual retail system whereby US- and Korean beef would be sold through separate distribution channels. Korea absorbed all of the imported beef every year its quota was in place except for one, in 1997, when the financial crisis hit all South East Asian economies and drove consumption down by 40 to 50 percent (the decline for US beef was much lower). The only evidence produced by complainants was that fewer outlets were selling imported beef than domestic beef. This was to be expected, since the quota corresponded to roughly 10 percent of annual total consumption of beef (it begs repetition that it was all sold in every year but one). And yet Korea lost.

Four years later, in *Dominican Republic-Import and Sale of Cigarettes*, the AB took a different view and held that a detrimental effect on imports is not necessarily LFT: if the reason for making regulatory distinctions is not the origin of the good, then it is irrelevant that imported goods suffer more as a result of any such distinction. In this case, the AB exonerated a measure whereby the imposed fine on sellers was function of their market share, and it so happened that imported goods enjoyed a larger market share and were hence paying a heftier sum. Then comes *Thailand-Cigarettes*, where the AB goes back to the Korea-standard without quoting even once the Dominican Republic report. Confusion reigns on, aggravated by the fact that two subsequent Panel reports ([US-Clove Cigarettes and US-Tuna II(Mexico)]) explicitly refer to *Dominican Republic-Import and Sale of Cigarettes* and do not stop their analysis when finding detrimental effect – they move to discuss the reason for it. In light of the above, how can it be possible for anyone to predict how the next LFT case will be decided?

**False Positives**

We limit ourselves here to what are in our view some egregious cases. In general, WTO adjudicating bodies do not overstep their authority in the sense they do not add new obligations beyond those agreed. Both Davey (2001), and Howse (2003), coming from different perspectives, conclude so when asking this question. There are however, a few instances where this has happened. These are instances of arguably secondary importance, yet they exist. In all cases where the AB has completed the analysis, it has ipso facto deprived parties of their right to a two stage-adjudication. True, this did facilitate speedy resolution of the dispute. But facilitating resolution should not take precedence over the legislative imperative to abide by the balance of rights and obligations as struck by the WTO Membership. The *amicus curiae*-saga provides another illustration: first came the truly innovative manner in which the AB interpreted in *US-Shrimp* the term ‘seek’ in Art. 13 DSU. Under this provision Panels remain free to disregard un-solicited information, but the AB provided an unwarranted interpretation of the term, holding that ‘seek’ does not exclude the possibility for someone to send an opinion. True. But the Panel had simply stated was that it was disregarding an opinion it had not sought. At the same time, it did not contribute to a solution to the issue either: it held that Panels must decide if they accept or not similar submissions (which is what the Panel had decided anyway). Then came the AB initiative to allow for submission of amicus curiae briefs in *EC-Asbestos*. The WTO Membership convened a special session of the Council and, with very few notable exceptions, by and large condemned the AB
initiative stating that its actions were beyond its legal powers. To date this has been the only collective reaction by the membership against WTO adjudicating bodies. There have, of course, been individual positive reactions (from the prevailing party), and individual negative reactions (from the losing party). But this remains a specific case where the overwhelming majority of the WTO Membership felt that the AB was overstepping its mandate.

There are other examples of false positives: extending the term ‘exhaustible natural resources’ in US-Shrimp to cover living organisms is contrary to the negotiating intent of Members and, thus, against the letter and the spirit of Art. 3.2 DSU. It was also largely unwarranted, since the US should have prevailed irrespective of the legal basis chosen, in light of the minimal cost that its policies imposed on international trade and its, eventually, non-discriminatory character.

In US-Softwood Lumber IV, the Panel faced an awkward situation: there was no prevailing market price in Canada for the products in question; Art. 14 SCM, which deals with the calculation of benefit, pre-supposes the existence of such a price. The US (for good reasons) had used a benchmark other than those referred to in Art. 14 SCM, and Canada challenged the US practice arguing that they should have used one of the benchmarks exhaustively reflected in Art. 14 SCM. This is, arguably, a case of legislative failure. The Panel wisely signalled the issue but refused to play legislator, and found against the defendant. The AB reversed the Panel in principle, arguing that one could legitimately use other benchmarks. By doing that, however, it added to the original bargain. This is not its role, notwithstanding the solidity of arguments in favour of amending Art. 14 SCM.

In US-Upland Cotton, the AB majority opinion offers a reading of Arts. 10.1, and 10.2 of the Agreement on Agriculture (AG) which is difficult to reconcile with the wording but also the overall economy of the provision and its negotiating history: if export credits came under the purview of Art. 10.1 AG, why would negotiators spend negotiating effort to introduce Art. 10.2 AG? Did they want to signal that they were prepared to exclude export credits from the disciplines of the Agreement through future action? This is a highly unlikely outcome, since the whole negotiation was meant to discipline instruments and not the opposite. A contextual reading of the two provisions amply

26 For a detailed narrative on this score, see Mavroidis (2004). Unfortunately, the collective action problem was overcome on the one issue where collective action was the least recommendable: there now seems to be acceptance of the fact that there is nothing wrong with amici curiae participation if it is contingent on the Panel/AB-approval.

27 See Irwin et al. (2008) who document the negotiating history in this respect.

28 SCM stands for the WTO Agreement on Subsidies on Countervailing Measures.

29 And it is almost impossible to establish how the Agreement would have looked like had such a right been included in the original balance. Arguably, the demandeurs of this right would have to pay a price for its inclusion.

30 The AB did not identify another appropriate benchmark and did not even establish the criteria that would help WTO Members in future practice use such alternative benchmarks.

31 This term needs some extra clarification in this particular context. We do not simply mean a look into the remaining provisions of the agreement, but also a look into the circumstances surrounding the negotiation. The Agreement on Agriculture was meant to impose disciplines on instruments affecting farm trade. If Art. 10.1 AG covers all instruments then, for the AB to be correct, Art. 10.2 AG can be understood as some sort of agreement to exclude, eventually, export credits from its coverage. But if there was
supports the minority view, that is, that there was agreement as to the disciplining of many instruments, but no agreement on export credits, an issue left, as per Art. 10.2 AG, to future negotiations.\textsuperscript{32}

3. Conclusion: Improvements Needed

Opinions about the quality of the WTO adjudicating bodies often seem to be impressionistic. The many observers who conclude that ‘the system works’ can also be interpreted as saying ‘so far so good’ in that to date there have not been major disasters. But does the system work in the sense of completing the original contract? Here a more nuanced response is necessary in light of the discussion above. The WTO judge behaves more as a ‘settler’ of disputes, as an honest broker as opposed to an agent who provides the additional information needed for the original contract to be applied in a specific situation. The next question then is what should be done to change this. The disagreements regarding the quality of the output of the dispute settlement process should not detract from the fact that the WTO is the only genuine system of compulsory third party adjudication in the field of international relations. It is precisely for this reason we believe that the process needs to be further strengthened.

WTO judges are agents that occasionally have substantial discretion. This implies risks for the system as the result may be to overstep. While there are WTO agreements with procedural provisions that are very detailed and therefore much less subject to problems of interpretation,\textsuperscript{33} when it comes to core basic concepts such as non-discrimination the contract is much less complete. It is there that WTO Members should focus attention. There are no magic solutions in the sense of developing a mechanism that will always guarantee a certain outcome; indeed, good faith disputes will inevitably arise in the context of incomplete contracts. But the current situation in which there is substantial uncertainty regarding how terms will be defined and what methodology should be used in determining whether products are ‘like’ and if foreign products have been treated less favourably should not be acceptable.

There are several steps that could be taken that would make a difference. The first is to make greater recourse to basic economic insights and concepts and to apply these more consistently. It is remarkable that although the WTO contract pursues economic objectives, and Panels are often flooded with econometric evidence, especially in antidumping/countervail cases, the clerks are all lawyers. The conditions under which the WTO Economics Division participates in dispute adjudication are unknown. A

\textsuperscript{32}This is by no means an exhaustive list. Korea might still be wondering why it lost its argument in Korea—Various Measures on Beef, where the AB accepted that its measures genuinely pursued a legitimate objective (consumer protection), but were found to be unnecessary – with no additional explanation. Chile, by the same token, might ask why only its regime, among dozens of examples around the world of progressive taxation schemes (whereby taxation increases in light of the increase in alcohol) has been found to be GATT-inconsistent (Chile—Alcoholic Beverages). And there are other cases as well.

\textsuperscript{33}Antidumping is an example, although even in that case there has been a need for the AB to interpret the rules in ways that proved to be very objectionable to at least one WTO member – viz. the repeated zeroing cases.
change in this respect is very much needed and urgently so. But a precondition for addressing some of the weaknesses of the AB reports discussed in this paper is that economic concepts be applied consistently in areas where they can be. An obvious place to start is in the determination of like products (degree of competition and substitutability of products; definition of the relevant market) but there are many other areas where the consistent use of specific economic concepts and frameworks by dispute settlement bodies would make the process more predictable by generating greater clarity on the methodological approach that will be followed by WTO adjudicating bodies in arriving at determinations.34

It is equally remarkable that less than 10 percent of Panellists have participated in more than five disputes and that in 50 percent of all cases to date Panellists are 'kings for one day', with just one appearance as judges (Horn et al. 2011). The burden of drafting Panel reports inevitably falls on the WTO Secretariat, which can result in greater consistency over time but also can generate perverse incentive effects (Nordström, 2005). Proposals have been made for a permanent body of panellists (Davey, 2003)—or a standing body of Panel chairpersons (Busch and Pelc, 2009)—on the basis that this would improve the quality and consistency of reports and reduce the discretion of (reliance on) the secretariat in the selection of panellists and drafting of findings.

By the same token, AB judges should become full-timers. They often deal with very complex issues and are the last resort. Their focus needs to be in Geneva and not divided between their WTO tasks and other activities. Rather than a 4-year appointment plus a one-time reappointment that is conditional on consensus in the DSB, a shift towards full-time status should be accompanied with greater certainty of tenure, e.g., through agreement that appointments are for 8-10 years. Rather than the current mid-term re-appointment process that does not have clear criteria and that therefore can become politicized, consideration should be given to at least reversing the 'burden of proof' – requiring WTO members to provide arguments to justify a refusal to support extension (along the lines of what was proposed in the Sutherland Report on the use of consensus in WTO decision-making). More generally, greater attention should be given to the appointment process of AB members and the governance of dispute settlement. Mechanisms are needed to ensure that AB members perform the functions effectively and competently and can be held accountable by the WTO membership for their performance without opening AB members to 'hold up' problems and pressure from specific WTO members. Here, as in other areas of the trading system, agreement on the rules of the road (performance criteria) and transparent monitoring of whether they are attained could help to increase the quality of the process.

As has been stressed by Patrick Messerlin in his writings – and put in practice by him as the director of the Groupe d’Economie Mondiale at SciencesPo – transparency is a key input into better policy-making by holding governments accountable for what they do. In the WTO context both negotiation of new agreements (policy disciplines) and implementation of what has been negotiated depends importantly on the ability of those with an interest in more liberal trade policies and enforcement to know how they are being affected by policy measures and whether their government and trading partner

34 Examples include the determination of injury and the impact/incidence of a trade policy action. In the latter area the WTO is increasingly making use of economic analysis to establish the magnitude of permitted retaliation when a member does not implement a DSB finding (Bown, 2010; Bown and Ruta, 2010).
governments are in compliance with their obligations. Transparency of policy is therefore also a key input into dispute settlement (Hoekman and Mavroidis, 2000; Bown and Hoekman, 2005). Information on nontariff policies is often bad, especially for subsidy-type measures (Messerlin, 1993; 2001; 2002; Hoekman and Messerlin, 2006; Collins-Williams and Wolfe 2010). Improving this situation is important from a public policy perspective. But the rate of return on investments in transparency in terms of more effective enforcement of rights and commitments depends also on the effectiveness and predictability of the WTO adjudicating bodies.

References


