Developing Countries and DSU Reform

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There has long been a desire to help developing countries make more of dispute settlement at the WTO. Ever since the subject of Dispute Settlement Understanding (DSU) reform was taken up in the Doha Round, Members have proposed various ways to help developing countries gain more *ex post* compliance. In the Chairman's current text (JOB/DS/14, Art. 22), DSU receives a lot of attention in this regard, the aim being to make retaliation more viable for developing-country complainants as a matter of special and differential (S&D) treatment. Two proposals merit careful attention: Art. 22.3*bis* DSU provides for developing countries to ask for authorisation to cross-retaliate as a first option (contrary to the current text which provides for cross-retaliation only if retaliation in the same agreement is ineffective); and Art. 22.4 DSU changes the way that the level of nullification and impairment is calculated for these complainants (the current standard being equivalence between damage inflicted by the author of the illegal act and the amount of retaliation authorised).

We worry about both proposals, less because of their mechanics than the mindset they create with respect to the efficacy of retaliation as being the key to compliance. We would prefer more S&D provisions focused on *ex ante* settlement.

Ecuador's request for cross-retaliation in *EC-Bananas III* made the idea nearly irresistible, and it is now routine for developing countries to at least weigh this option. *US—Gambling, US—Upland Cotton and US—Clove Cigarettes* have drawn added attention precisely because cross-retaliation by Antigua-Barbuda, Brazil and Indonesia (respectively) looms large. We see the lessons of *EC-Bananas III* differently. First, Ecuador never followed through on its authorisation to cross-retaliate, fearful that the suspension of copyrights on European music would only hurt foreign direct investment

(FDI). Now that cross-retaliation is synonymous with poor countries hitting back against the intellectual property of rich countries, our concern is that it is *not* credible to fast-track cross retaliation, especially in light of the web of north-south bilateral investment treaties (BITs) that cover intellectual property. Indeed, respect for property rights is among the most salient country-risk factors shaping flows of FDI, and threats to undermine intellectual property on an ad hoc basis can only hurt in this regard.

We are not saying that cross-retaliation should be ruled out, but rather that it should not be fast-tracked. On the contrary, the harm done to FDI by cross retaliation might actually be lessened by adhering to a more formal vetting of why other forms of retaliation (as per the hierarchy established in Art. 22 DSU) are not within reach. The current case law has probably gone too far by imposing too much of a constraint when it comes to deciding on cross-retaliation. We are afraid, though, that by going too far in the other direction through the proposed text, developing countries might rush to cross-retaliation without giving adequate thought to negative externalities stemming from similar actions. The risk to do so depends, of course, on inter-agency coordination across national administrations.

Second, more central to *EC-Bananas III* than Ecuador's threat to cross-retaliate was the US's implementation of *carousel* retaliation. By raising uncertainty on the part of EU exporters as to whether they would be named on the US list, carousel retaliation had the effect of prompting widespread lobbying in favour of compliance. True, it may be difficult for some developing countries to retaliate in-kind or under the exact same agreement, but if they can, something modeled on carousel retaliation could be the preferred S&D provision to cross-retaliation. If, on the other hand, cross-retaliation is the only option, it should be shown to be so, not fast-tracked as per Art. 22.3*bis* DSU.

Carousel retaliation is not necessarily DSU-consistent, of course, since there is no guarantee that all lists for retaliation respect the discipline established in Art. 22 DSU (equality between damage inflicted and amount of retaliation), unless if the requesting Member presents various lists for authorisation. In this case, the surprise effect is

somewhat mitigated since all potential addressees will have been ex ante revealed. On the other hand, revelation might induce them to form wide coalitions to address the potential for retaliation through lobbying efforts.

Art. 22.4 DSU is a step in the same direction, adding to the level of concessions that a developing country complainant might suspend. This may well seem enticing. Something like it happened in *Canada—Aircraft*, where the WTO factored in a punitive cost to what it saw as the harm done to Brazil when Canada announced its *ex ante* unwillingness to comply. Art. 22.4 DSU formalises this for developing countries, such that "the level of nullification and impairment shall also include an estimate of the impact of the inconsistent measure on the economy of such Member". We doubt that this "estimate" would be within reach of an Art. 22.6 DSU arbitration. But this is beside the point. Even if it were, this is a highly 'incomplete' provision which could be interpreted in various ways by judges; there is no guarantee that it will be meaningful. More importantly, if developing countries struggle to retaliate, adjusting the level of nullification and impairment higher is not going to help. Small economies, by definition, cannot be much of a threat to recalcitrant big players, even if economy-wide effects enter the calculation for lawful retaliation. Worse still, it may motivate complainants to pursue a big judgement, rather than negotiate a solution to their dispute up front.

Our concern is that both proposals create a mindset that compliance must be pursued through retaliation, Art. 22.3*bis* DSU making it easier and Art. 24 DSU making it bigger. Ideally, we would like to see similar proposals in practice and then 'measure' how much they have contributed to securing compliance. Alas, we do not have this luxury. What is clear to us, though, is that developing countries suffer from procrastinated compliance. In the absence of retroactive remedies (an issue that no one wants to touch upon in the current negotiations), it is in their interest to look for legislative solutions that will promote fast-track solutions, as opposed to *ex post* compliance (which might, if at all, come at the earliest five years down the road, e.g. from the moment that a request for consultations has been submitted).

Developing countries are at a disadvantage in negotiating *ex ante* settlement. The focus of S&D provisions should thus be to help make consultations work these complainants. The DSB Fund proposed in Art. 28 DSU can help in this regard.

Over the years, there have been many proposals to reimburse developing countries' legal fees in the event that they prevail against a developed country. The problem is that this only increases the incentive to go the legal distance, looking for a favourable ruling. Art. 28 DSU explains that those countries that cannot access the DSB Fund, for lack of budget, may nonetheless be reimbursed where the developing country wins as a complainant, or does not lose as a defendant. The spirit of Art. 3 DSU is to settle whenever possible, not prevail in litigation at all costs. In fact, where rich countries do better than poor ones in dispute settlement is in negotiating mutually satisfactory solutions. Importantly, developed country complainants do not win more, nor do they get more compliance with the rulings they win. The DSB Fund should therefore invest in helping developing countries make more of consultations. We would start with the proposed reimbursement rate. First, the amount allocated for consultations should be increased so that developing countries can retain counsel earlier in deciding whether to file, and keep counsel longer should consultations go on for the additional 15 days that are provided for under the proposed Art. 4.10(b) DSU.

The next step is to affirm that all legal expenses for consultations are to be covered by the DSB Fund, *even if the case does not proceed to the panel stage*. This should not be viewed as subsidising 'fishing expeditions' – which is why we know that, as an S&D provision, Members would never go along with the idea that rich countries should underwrite the legal expenses of poor ones in consultations. But in the context of the DSB Fund, we submit that there is already an untapped architecture in place that would guard against fishing expeditions: namely, Art. 27.2 DSU, which is in need of revitalisation, potentially as a precursor to tapping the DSB Fund. And while DSU has never gained much traction, we would submit that this mechanism can do much to improve the experience of developing country complainants in consultations.

In line with these recommendations, we suggest the following work programme:

1. Delete Art. 22.3*bis* DSU and Art. 22.4 DSU in favour of Art. 28 DSU as a more viable S&D provision, focused on consultations, as we outline above.
2. Bridge 27.2 DSU to Art. 28 DSU to ensure that developing countries get an opinion about the legal merits of pursuing a dispute *and* the funding to launch productive consultations. The required text for this recommendation should be drafted for the next ministerial. We are well aware that this will change the nature of Art. 27.2 DSU; one of us (Mavroidis) has provided legal advice under this mechanism. Developing countries have always needed more from Art. 27.2, and we would submit that this is a relatively easy fix.
3. We further propose building a bridge between Art. 27.2 and the Advisory Centre on WTO Law (ACWL). This would facilitate the exchange of information between the two institutions and enable developing countries to tap a wider pool of information in the process. The required text for this recommendation, like the one above, should be drafted for the next Ministerial Conference.

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