

“The WTO: Is it Really at Risk?”

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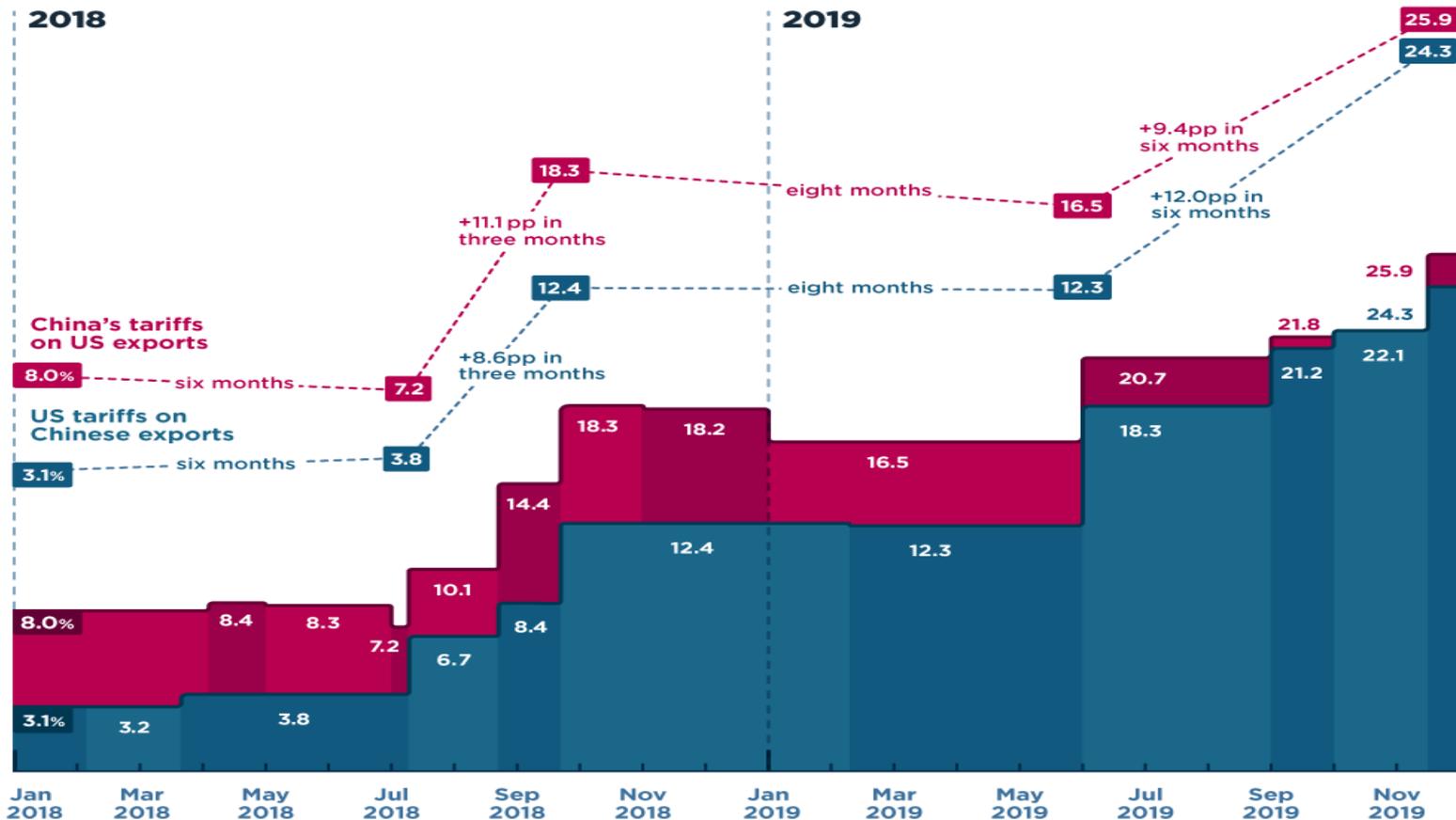
Key issues

- **US shift to “power-based” tariff bargaining**
- **Why the shift?**
- **US-China trade war and failure of WTO dispute resolution: which came first?**

Trade war has intensified

The Trade War Is Suddenly Getting Worse

Average tariff rate, percent

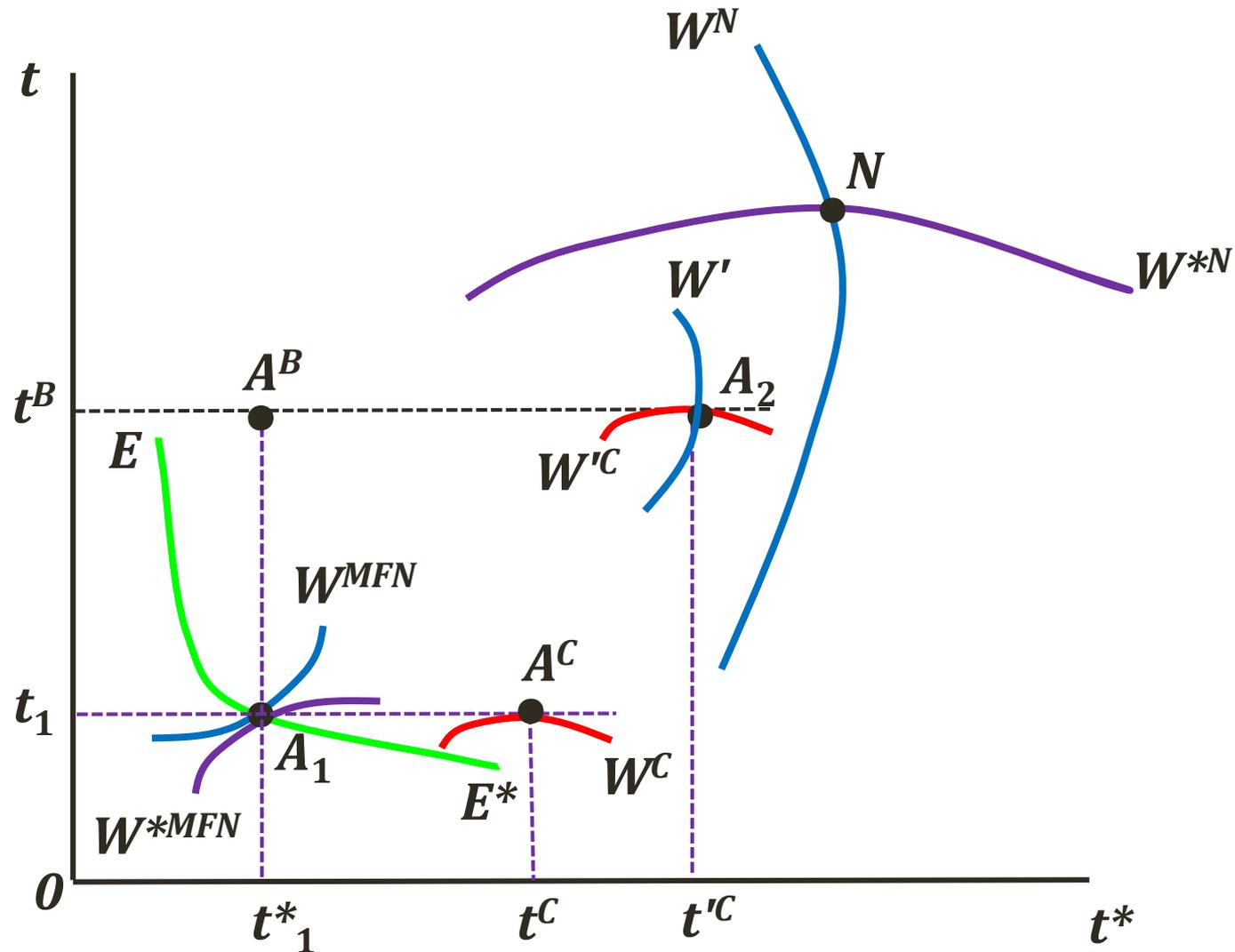


2018

2019

Source: Bown, PIIE, 8/29/19

US “rules-based” vs. “power-based” bargaining



Source: Mattoo and Staiger (2019)

Impact of “China shock” on US political economy

- Effect of China import shock well-documented, Autor *et al.* (2013), and Pierce and Schott (2016)
- Trade exposure contributed to growth of *populism* (Grossman and Helpman, 2018) and *polarization* in US politics (Autor *et al.*, 2017)
- Populism reflected in *anti-elitism* (Eichengreen, 2018) and shift to *economic nationalism* (Colantone and Stanig, 2018) – i.e., opposition to free trade
- China targeted over trade policies: (i) level of tariffs, (ii) bilateral trade surplus, (iii) exchange rate manipulation, and (iv) violation of WTO rules

Chinese market distortion and WTO

- **US concerns about China's trade practices well-documented (USTR, 2018; Morrison, 2018):**
 - **Forced technology transfer**
 - **Discriminatory licensing restrictions**
 - **Theft of intellectual property**
 - **Investment restrictions**
 - **Subsidies to state-owned enterprises (SOEs)**
- **WTO case could be built against China that one or more Chinese government measures “nullify or impair” benefits of US and other WTO members (GATT Article XXIII:1(a)) (Hillman, 2018)**

Chinese market distortion and WTO

- **WTO case could also be made against China under “non-violation nullification or impairment” (NVNI) clause of GATT (Article XXIII:1(b)) (Hillman, 2018)**
- **Argued only way to approach this is through “grand coalition” of countries (Hillman, 2018; Lawrence, 2018)**
- **Problem with US unilateral approach:**
 - **“Shallow” deal (Hillman, 2018)**
 - **“Free-riding” (Bown, 2018)**
 - **Potential to undermine WTO (Mattoo and Staiger, 2019)**

“China, Inc.”

- **China’s economy structured in ways not anticipated by WTO negotiators (Wu, 2016; 2019):**
 - **Party controls “commanding heights” of economy**
 - **Party controls and directs largest banks**
 - **Party coordinates government agencies and firms**
 - **Party-set performance metrics of SOEs, banks etc.**
 - **Informal linkages between Party and private firms**
- **Party controls economy while still taking advantage of benefits of market mechanism, i.e., control is not necessarily via state**

“China, Inc.”

- **Foreign firms perceive Party-state can reshape terms of trade to their disadvantage – especially where SOEs play key role**
- **Why is WTO ill-suited to deal with “China, Inc.”?**
 - **Incompleteness of rules – no major update since 1994 when “China, Inc.” was unknown**
 - **WTO rules designed to discipline state actors as opposed to type of informal networks operating in China**
 - **Under current rules, China gets “free pass” prior to conclusion of dispute, i.e., policy that breaks rules often achieves objective before WTO ruling**

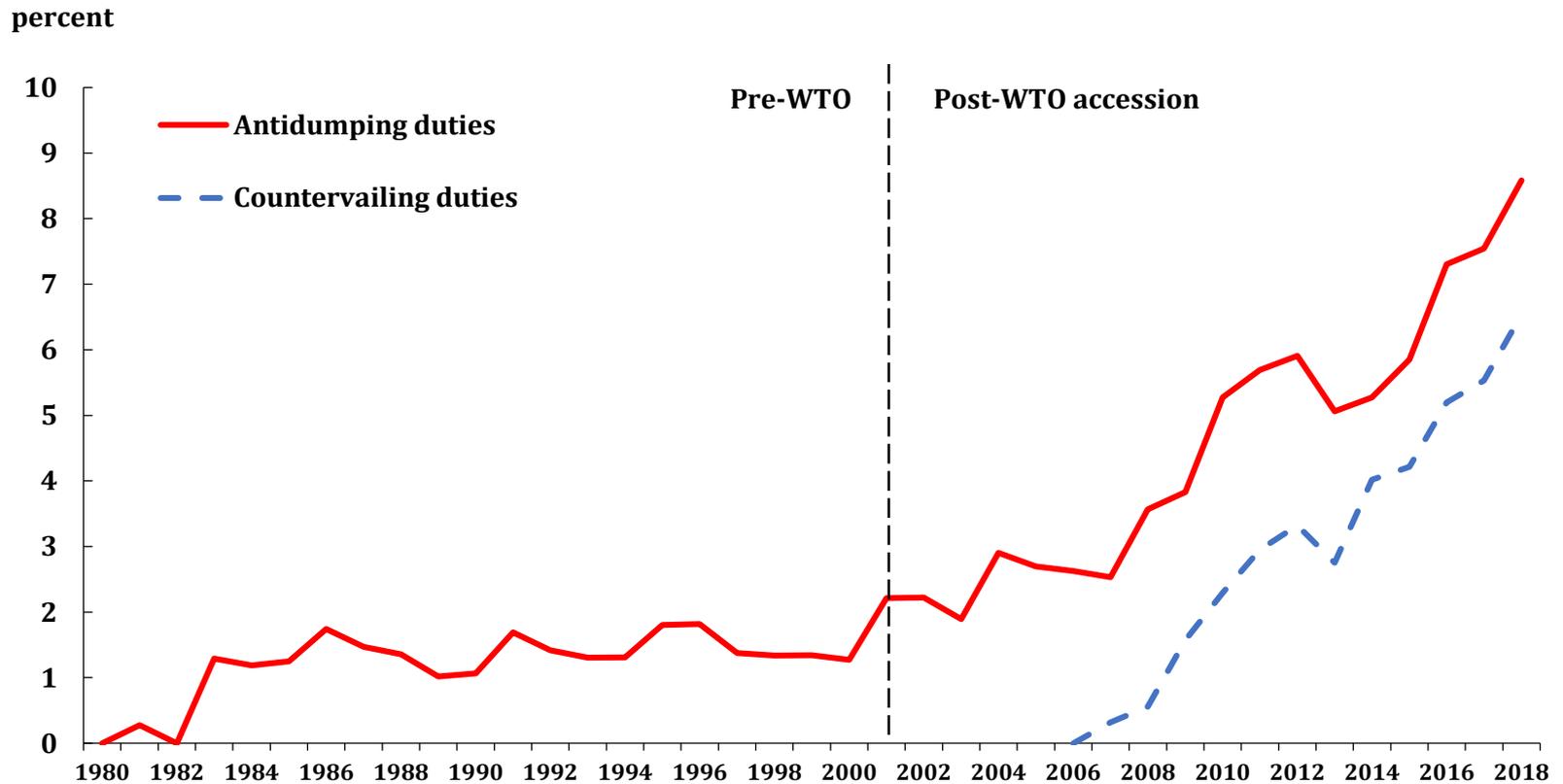
Provoking a trade war

- **Conventional wisdom - US has deliberately poked holes in weakest spots of WTO (Bown, 2019):**
 - **Imposed tariffs on steel and aluminum in 2018 on grounds of national security - US argued these would be “non-justiciable”, i.e., cannot be questioned as with anti-dumping duties**
 - **US unilaterally implemented tariffs on \$250 billion of Chinese imports after internal investigation by USTR (2018) - based on Section 301 of US Trade Act**
 - **US chose to block judicial appointments to WTO Appellate Body (AB)**

Trade war and WTO dispute settlement

- **US imposed national security tariffs in part because of Chinese economic model (Bown, 2019):**
 - **Chinese trade practices had to be countered**
 - **Anti-dumping duties had not worked**
 - **Safeguard tariffs would have been stopped by WTO**
 - **US would not win case at WTO due to “China, Inc.”**
- **Counter-argument – US gave up on formal dispute settlement too soon, i.e., specifically, it should have appealed to NVNI clause**
- **However, requires AB to deal with complex interactions in non-market economy**

US anti-dumping duties and China



Source: Bown (April, 2019)

Failure of WTO dispute settlement

- Concerns over “judicial over-reach” in AB, and emergence of principle of *stare decisis* in WTO case law (Payosova *et al.*, 2018)
- Possibly due to excessive influence of WTO Secretariat in writing panel and AB rulings (Pauwelyn and Pelc (2019)
- Dispute settlement will break down by end of 2019, i.e., any member will be able to block panel rulings
- Members should agree on procedures for AB to submit uncertain legal issues arising on appeal to respective WTO committees – *legislative remand*
- Emphasizes need for permanent negotiations in WTO

Avoiding risk to WTO

- **Requires modality for updating trade rules**
- **Current remedies against repeat rules violations are too weak – go to system of judicial relief?**
- **Too much leeway for countries to hide behind arguments such as “national security”**
- **Hillman’s (2018) call for coalition will not work for large-scale NVNI case against China – burden of proof too complex (Wu, 2019)**
- **Before case can be brought to WTO – need to find way out of AB crisis, allowing judicial arm of WTO to operate**