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THE NEW ISSUES

THE NEXT TRADE NEGOTIATING ROUND:
EXAMINING THE AGENDA FOR SEATTLE

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Chapter 5

On Thinking Clearly about the Linkage Between Trade and the Environment[1]

Jagdish Bhagwati
Arthur Lehman Professor of Economics and Professor of Political Science, Columbia University

I. Introduction

The question of linkage between trade and environmental issues, indeed between trade and labor standards and between trade and human rights, has reached center stage as several NGOs (non-governmental organizations) have demanded that the WTO formally incorporate such a linkage through, for example, a Social Clause on labor standards in WTO and through as yet unspecified mechanisms as far as environmental standards are concerned.

Within the environmental arena, the GATT itself, and now the WTO (GATT's successor), have been the focus of much agitation by environmental groups that see this trade institution as an obsolete obstacle to environmental progress. The anti-GATT feeling materialized first when the celebrated Dolphin-Tuna decision was announced, declaring Mexico the winner in the dispute over the US legislation that sought to proscribe access to Mexican tuna caught in purse seine nets. A throwback to that sentiment occurred recently when the Shrimp-Turtle Panel decision also went against the United States over its legislation that mandated unilaterally a denial of access to shrimp harvested without the use of TEDs (the turtle excluding devices).[2]

These cases reflected one of a number of different ways in which the work of the WTO interfaces today with the environmental questions and agendas. The main and unifying essence of both cases was the question: should suspension of market access be allowed automatically to a nation which objects unilaterally (i.e. without obtaining a multilateral consensus) to other countries exporting products to it when those products are made by using processes that the nation objects to on "values" grounds?

In the Dolphin-Tuna case, the US government objected to the use of purse seine nets in harvesting tuna because these nets kill dolphins (which Americans have voted to protect, presumably because they are "cute" and a great draw at zoos) gratuitously and also cruelly. In the Shrimp-Turtle case, the objection was similar: it related to what are called in GATT jargon PPM objections, i.e. objections to process and production methods.

[1] This paper was prepared for the Conference on Environment and Trade at the Kiel Institute for World Economics in Kiel, Germany, in Summer 1999. It was also discussed at the Columbia University Conference on The Next Trade Negotiating Round: Examining the Agenda for Seattle, July 22 and 23, 1999.

[2] In each of these cases, there have been more than one Panel findings; in the latter case, the new Appellate Court also ruled after the initial Panel finding. The precise grounds on which the United States lost in both the cases have therefore varied.

Similar cases can arise if nations object similarly to the importation of, say, chickens produced in batteries, or hogs produced in crowded pens, or fur harvested from animals caught in leghold traps, and many more instances of what some nations, but not all or most, consider to be "values"-wise unacceptable PPMs.

But while these cases are the subject of high-profile, high-octane attacks on the GATT and the WTO, and they raise questions which necessarily involve an interface between the WTO and the environmental groups, there are other issues which are equally the object of demands by environmental groups on the WTO but, in my view, are not necessarily ones that belong to a WTO or trade-treaty agenda. In particular, I believe this to be true of the demands for harmonization or upgrading of environmental standards in developing countries if they wish to export products, even when the pollution involved is "local" and has no global environmental externalities as with global warming or ozone layer depletion or acid rain.

Unlike in the popular debate, which tends often to blur necessary distinctions among different types of problems, and where the environmentally sensitive lobbies often are unwilling to make the distinctions anyway because they would weaken coalition-building for political action, I propose here (in a brief essay focused on "trade and the environment" linkage) to make these distinctions very sharply (in Section I).

In particular, using these distinctions, I set myself the task in this paper of providing a road map which is aimed at dividing the current "linkage" demands between trade (whether institutions or negotiations) and environmental questions into those that are "necessary" and those that are not. In the latter case, as when trade access is used as a way of pushing environmental agendas abroad on altruistic grounds, I will also propose alternative ways in which such agendas may be pursued outside of the trade context and institutions (e.g. in UNEP rather than WTO): thus raising the question of what I like to call the design of Appropriate Governance (i.e. what agenda to pursue where).

II. A Necessary Taxonomy

I first provide a necessary taxonomy so that the issues concerning linkage of trade and environmental questions can be analyzed with clarity and optimal policy solutions designed with the aid of such analysis. This taxonomy can be built essentially around two sets of distinctions:

(i) whether the environmental damage or pollution is "domestic" or "international"; and

(ii) whether the country addressing it follows egotistical (i.e. its own advantage) or altruistic (i.e. others' advantage) objectives.

The former distinction was introduced principally in the 1992 GATT Report on Trade and the Environment, though it must have been used simultaneously by many researchers, I am sure. If I pollute a lake in India which only (even then just a few) Indians have heard of, the pollution is of concern to Indians at risk. But if I pollute a river that flows into Bangladesh, or produce acid rain in the US which goes across and hurts

Canadians, the problem is clearly international. When global warming and ozone layer depletion are involved, the problem is actually global. The international/global problem is clearly one where externalities are at stake unless a "market" is already in place to internalize these externalities (e.g. by having tradable permits, suitably devised).

The latter distinction is appreciated by few, including economists who write about Globalization, about fixing the World Trading System et.al. without any real understanding of the complexity of the issues at hand.[3] Thus, we must distinguish between, say, objecting to the import of child labor-produced carpets from India because we object to being put at a competitive disadvantage with other nations because we prohibit, and they allow, cheaper child labor, and objecting to such imports instead with a view to reducing or eliminating the use of child labor abroad because we think that our cessation of such imports will help bring that about. In the former case, we are "egotistic": we are simply interested in maintaining our competing industries. In the latter case, we are being "altruistic" in thinking of children's welfare even though they are abroad in other nations and we are using consequentialist ethics, hoping to effect change abroad. The latter is therefore a matter of seeking to advance social agendas abroad; the former is a matter of protecting our industries, for our own benefit. In assessing the demands for prohibiting the imports of products made with child labor, our evaluation of the proposal and the design of appropriate policy instruments will clearly have to be different, depending on which of these two motivations we are confronting.[4]

Once then these two sets of distinctions are made, we have four sets of problems: Domestic Environmental Problems with Egotistic and with Altruistic Objectives by nations; and International Environmental Problems with Egotistic and with Altruistic Objectives again. In this paper, I devote myself to the Domestic Environmental issues: these are among the trickier ones where a great amount of confusion reigns.

[A Digression: The International Environmental Issues are understood much better, including in their interface with the WTO's functioning: and I shall eschew a discussion of them here. Let me just say, in regard to them, that the interface with WTO comes principally insofar as the MEAs (Multilateral Environmental Agreements such as Basle and the Montreal Protocol) seek to use trade sanctions against defectors and against free riders, and that these two sets of nations, when WTO members, could claim WTO-defined rights against the use of such sanctions. These questions are not easy to settle since we must raise questions such as: is the MEA efficiently and equitably designed[5]; if

[3] Here, the culprits include my good friend, Dani Rodrik, and his publisher, the Institute for International Economics in Washington D.C. which has published yet other authors such as the political scientists Mac Destler whose knowledge of the economics of international trade policy questions seems to be exclusively based on reading what the Institute brings out, advocating linkage to facilitate fast track renewal and the start of the Millennium Round.

[4] In this paper, I cannot discuss these distinctions fully. A systematic and deep analysis is provided in my and others' contributions to Bhagwati and Robert Hudec (eds), Fair Trade and Harmonization: Prerequisites for Free Trade?, Vol.1, MIT Press: 1996; and also in 3 chapters in Section VI of my recent book, A Stream of Windows: Unsettling Reflections on Trade, Immigration and Democracy, MIT Press: 1998.

[5] Thus, in relation to the NPT and CTBT, India refused to sign them because it did not accept the division of the world into the status quo of those who had nuclear weapons and those that did not, and backed

the scientific evidence in support of it is disputed, can you treat a nation that does not wish to join as a free rider when in fact it may simply be opting out of getting on to the bus? In this context, let me say that, while Kyoto is a useful step forward (though I share some of the misgivings about its design that the economist Richard Cooper expressed in his article in Foreign Affairs last year, and felt that Stuart Eizenstat's reply was lame, to say the least), I have been surprised that none of the models that I have seen seem to do the obvious if you know the domestic environmental scene in the US:

- For the "stock" problem, i.e. the damage done in the past, there must be a clearly defined responsibility for the polluters: this is a principle that has been accepted in the **Superfund** approach and in the torts claims addressed to past polluters for phenomena such as the Love Canal disaster. Why is it not accepted at the international level as well for past damage to the environment on Global warming (principally, of course, by the developed nations)? The question then must be, not whether there is responsibility for past environmental damage, but how to assess it and the specific ways in which the levy can be used to reduce the Global Warming problem, e.g. by financing the creation of new environment-friendly technologies and their subsidized diffusion across the world.
- For the "flow" problem, as to what to charge for emissions, the conceptually clear answer has to be to put all such emissions (net of absorption services through, for instance, your forests) into the pot of world demand for such pollution and then to determine, with a suitable utility function defined positively on goods and services and negatively on pollution, the shadow price of a unit pollution. That would then define the cost which the nation must pay for its contribution to the Global warming problem. Needless to say, that cost would be vastly higher for the rich than for the poor countries. Instead of doing this, the rich countries are opting for an international variant of the principle which we call in the US the "PSD" Principle: i.e. prevention of significant deterioration. In plain English, this means that those who pollute a lot as part of the initial condition can get away with it: burdens are to be prorated to marginal changes in pollution!

So, what we have therefore in the Global warming debate is a cynical and virtual denial by the rich countries of the Superfund principle whose incidence would hurt them, and an adoption of the PSD principle which would help them. Not bad, indeed. As I read the Kyoto arguments and policy papers, it seems to me therefore that the developing countries have an intuitive sense of what I am saying above but no conceptual clarity or

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instead a universal nuclear disarmament plan. The moral incoherence of the nuclear nations is manifest from Britain's condemnation of India's nuclear tests when Britain, an admirable nation in other ways, holds on for no reason whatsoever to its own nuclear stockpile and could instead make an important moral and effective gesture by bringing the great unilateral nuclear disarmament advocate Vanessa Redgrave (leader of the unilateral-British-nuclear-disarmament CND movement) out of the mothballs and putting her in charge of a rapid unilateral destruction of Britain's stockpile! One might also note that the US itself has not ratified CTBT yet. The mere fact that a certain powerful group of nations, and its NGOs with their vast resources compared to those situated in the poor nations, support an MEA is no proof that it is equitable, free from power play that distorts priorities and burdens from an objective point of view, and therefore those who refuse to sign on to it are therefore "free riders" or "rejectionists". At least, we economists need to look at such claims with a cynical eye.

technical work to back it. Instead they talk inchoately about how the flow burden should be far less on them because the stock damage was due to the developed countries and also because they are poor and hence should not be asked to bear any burden. But as soon as they do that, arguing their case on these grounds, they are shot at in the US Congress as countries that are doubly wrong because they wish to be free riders and are also guilty of trying to exploit the "guilt" angle!

Again, one needs to consider whether, given the hostility manifest between the more vociferous environmentalists and free traders on many other fronts, it would not be wise to "grandfather" the existing MEAs and to leave the contentious question of the WT0-compatibility of future MEAs to further consensus-building among the WTO membership: we may prudently decide that this was one major battle we could withdraw from. This is certainly an issue that the WTO must come to immediate grips with, preferably at the Millennium Round to be launched in Seattle in December 1999. **]**

III. Domestic Environmental Issues

So, let me turn to the purely domestic environmental problems, dealing first with the Egotistical Objective and next with the Altruistic one.

Egotistical Objective

Here, I deal with the following distinct aspects of the demands for "greening the WTO":

1. **Contention**: WTO should allow importing countries to countervail "social" dumping, i.e. when a product is produced with differential tax burdens in different countries and the exporting country has a lower tax burden. This is what I & T.N. Srinivasan call in the Bhagwati-Hudec volume 1, Chapter 4, CCII (cross-country-intra-industry) harmonization of tax burdens. Clearly, this is wrong. With different fundamentals, there is no good reason for such harmonization to occur or to be demanded. We may demand that every nation adopt a Polluter Pay Principle; but the pollution tax, for the same carcinogen in the same industry, will generally be different.
2. **Contention:** We nonetheless may object to others having lower tax burdens because that will result in a "race to the bottom" that hurts our standards even if we do not care otherwise what standards others have on CCII basis. Therefore WTO should allow countervailing duties to offset "social dumping".
   Unlike the previous argument, this is theoretically a sound one. But it is an argument for a cooperative solution which will nonetheless not be characterized in general by harmonization. Besides, there can also be a "race towards the top" as John Wilson points out in his paper on the subject in the Bhagwati-Hudec volume. The argument besides depends on capital taxation being sub-optimal. Finally, the empirical evidence for such a race does not seem to be strong: (I) multinationals do not seem to respond to lower environmental burdens (not just because the differences among different locations are small, since these could

rise) for a variety of reasons including reputational ones (see the detailed discussion in Bhagwati-Srinivasan of the reasons why), though a couple of recent papers detect some elasticity of response to differential environmental burdens within the US across states; and (2) the evidence that poor countries lower environmental regulations to attract MNCs is not plausible when democratic countries are involved: the competition for capital/MNCs is really through tax breaks, tax holidays et al & land grants etc. all of which amount to a race to the bottom in taxation that hurts the competing countries, most analysts believe. Few democratic countries are going to offer facilities to pollute freely as a way of attracting MNCs.

So, for both Contentions 1 & 2, the Gephardt-Bonior-Gore type of demand for harmonization and/or legitimation at the WTO of countervailing duties on so-called Social Dumping seems to me to be NOT the way to Green the WTO. We should resist such demands**.**

Instead, I recommend **two Other Solutions:**

(i) I have argued that MNCs must be asked to adopt the environmental standards of their home countries when they go abroad. If they tend to do so anyway, as argued above empirically, then this mandate will not hurt and will buy environmentalists' approbation at very little deadweight loss. (See pp.178-179 in Bhagwati-Hudec, Vol.1). I think now of this as a Mandatory Code, unlike the Voluntary Code approach discussed below which is complementary in my view.

(ii) We can also go ahead with setting Voluntary Labeling Schemes like the SA8000
(whose pioneering originator, Alice Marlin, is at this Columbia University Conference), the world's leading Code today which firms can sign on to and several have indeed recently. This defines conditions of work etc. and includes independent monitoring. This means that all the signatory firms from every country would have to adopt the common, minimum standards whereas the Mandatory Bhagwati-style Code above would permit differences among firms from different countries.

3.) "Values-Related" PPMs: Next, there is the Shrimp-Turtle and Dolphin-Tuna type of problem. US consumers simply feel that the US should be allowed to prohibit imports of such products, using morally objectionable PPMs. This question has also been dealt with in the Bhagwati-Hudec volume.

Evidently, we cannot force such imports down people's throats. Indeed, economists are well aware of the legitimacy of PPMs as something which enter our utility functions: after all, the way you produce something is part of the characteristics of the vector that defines Lancaster-like a product. The problem is not that we free traders have not realized

that PPMs are legitimate and must be dealt with[6], but how do you deal with them when there is no consensus on that "value"? Do you allow automatic unilateral shut-off of such products?

Here again, the 1992 GATT Report, correctly in my view, argued that the grant of automatic market access suspension rights in such ethical or moral or "values"-related cases would be a slippery slope: how would you draw a line? Moreover, we do know that protectionist intent will occasionally underlie environmental legislation, often in the specifics of the design of the environmental regulation (as in the Dolphin-Tuna case and the Ontario-US beer can case). Are we simply to ignore that by saying an environmentally-aimed prohibition on imports cannot be challenged at all?

Again, powerful countries would be able to indulge their "values" but the weaker ones are less likely to be able to do so since legal standing is given only to governments that must take into account the ability of the powerful countries to use punishments and inducements to advance their agendas: so the principle that virtue goes with power would be enshrined into the WTO's working when, in fact, the WTO has been seen so far as a platform for the protection of the weak from the willfulness and self-indulgence of the powerful.

Therefore, again, I would say that the precise way in which the WTO deals with such values-related PPM problems should **not** be along the lines of automaticity or ill-considered and almost hare-brained proposals such as Rodrik's that an administrative procedure like anti-dumping be devised to ensure that the moral preference is genuine and widely shared after which the imports should be shut off (as if the enactment of the Turtle and Dolphin legislation itself was not the expression of such a widely-shared preference and as if an administrative body could sit in judgment over a legislative outcome!).

> (1) Rather, they should proceed along the lines of <u>labeling</u> **(**which itself raises a number of questions that UNCTAD has been particularly considering and which we know somewhat from US experience as well: e.g. who determines the label, how "alarmist" or "realistic" should it be, etc.: thus, in the hormone-fed beef case, the USTR Ambassador Barshefsky has suggested that it would be sufficient to label the US hormone-fed beef as "Made in USA" since everyone knows that much of US beef used hormones!), what are the problems for small producers in developing countries that have few facilities for such labeling etc. But it is still the way to explore and go, giving consumers information and choice.
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> **(2)** Equally, I think it is necessary to ensure that, if the WTO continues to object to automaticity of such suspensions of access as I believe it should, then the remedy when a country has lost such a case and still wishes to maintain the import suspension and is unwilling to accept a labeling solution, should not be to slap on retaliatory measures (as the US favors if recent examples in the hormone-beef and the bananas cases reveal a trend) but rather to go for a cash compensation that

[6] Rodrik, in his IIE pamphlet on Globalization, argues as if we are so unmindful. But this is to betray ignorance of the extensive debate over the problem, including in the 1991 GATT Report on Trade and the Environment.

reflects the gains from trade lost. There is no point in disrupting trade yet further: it is time that the economists weighed in on this aspect of the Dispute Settlement Procedures and Remedies.

4.) Other Forms of Linkage: I believe that the main ("egotistical") linkage questions of importance are the three I have listed & discussed above. But, in the classroom, we can certainly discuss other forms of "linkage" (in the sense of an interrelationship) which have little policy salience in my view. Two can be cited.

1. Say, I cannot use tariffs to exploit monopoly power. Then, I certainly can use other instruments (including pollution tax rates) to have a second-best improvement of my income through "inefficient" but still welfare-improving exploitation of monopoly power. This was at the heart of the Bhagwati-Ramaswami-Srinivasan, Kemp-Negishi and related discussions in the early and mid-1960s. Frankly, I do not think this sort of insight is particularly important in the trade and environmental interface discussion, any more than we want to get tied up worrying about dozens of possible policy instruments that may bear on trade indirectly. Cost-benefit analysis should suffice to say: think of other things! But I could be wrong; or perhaps, I should say: persuade me otherwise. [In fact, I should be personally happy as a scholar if I was wrong: after all, my own work in the 1960s helped define this linkage rigorously!]
2. Along the same line, scholars such as Brian Copeland have extended this type of argument to strategic interplay of environmental policies and to a demonstration as to how environmental negotiations that complement trade negotiations can improve welfare outcomes.[7] In a fine paper done for CIEL/Barrett, he takes egotistical governments maximizing utility. If tariffs are bound to zero, though each country has monopoly power in trade, each government then has an incentive to distort its environmental policy to manipulate the terms of trade in its favor. The country that imports the (only) environmentally dirty good in this model has then an incentive to stimulate the production of that good a little bit, in order to lower its world prices, and thus to relax its environmental regulation a bit (relative to the first-best, where the tax would just equal the environmental harm). The country exporting the dirty good has an incentive to restrict the production a bit to raise its world price, and hence to tighten its environmental regulation a bit (relative to its first-best). Therefore, without a free trade agreement, each country would set its environmental tax equal to the marginal environmental harm in that country; but with the free trade agreement, neither does.

Hence, we can have further gains from negotiation, over environmental policy once the free trade negotiation is done. Both countries can change their regulation in the direction

[7] Without detracting from the importance of Copeland's analysis, I might mention that one of our Columbia students, in a dissertation that was awarded "distinction", Waseem Noor, developed precisely the Copeland-type argument, in the context of labor standards. I must confess that my reaction then was the same as now: that the argument is analytically beautiful but has no empirical salience in my judgment. Cf. Waseem Noor, Labor Standards & International Trade: Four Essays, Ph.D. Dissertation, Submitted to Columbia University, 1997.

of the first-best simultaneously, so that the terms of trade effects cancel out and both countries therefore are better off because both have moved to giving individual polluters the right incentives.

But frankly, few developing countries have terms of trade to manipulate: they tend to be price takers in world markets (as empirical-cum-econometric analyses by Reidel and Panagariya have plausibly argued). More important, I doubt if the Copeland type argumentation really captures the spirit in which environmental regulations are set: I have seen no plausible evidence that the low environmental standards have been set by reference to trade-competitiveness considerations --- the most extreme example being the case of abysmally low standards set by the former communist countries which hardly traded at all. My view rather is that the low environmental standards, set for trade-unrelated reasons, are in fact being used to advance protectionist agendas by the high-standard countries: the Copeland-type argument is, in that view, turning the reality on its head!

(B). Altruistic Argument for Linkage

But suppose that we seek linkage because of altruistic reasons, treating trade treaties and/or institutions as mere instrumentalities via which we hope to effect change in morally offensive practices abroad.

My main objection to the inclusion of such social agendas in trade institutions and treaties is that this amounts to trying to kill two birds with one stone: a recipe for missing both birds except in the fluke event where the two birds happen to lie on a common trajectory and Wonder Woman is hurling the stone into the sky with deadly force and accuracy.

We already know how the linkage proposed by President Clinton when he asked the Congress for fast-track authority divided the Republicans and the Democrats and was a factor in his loss of the Congressional support for fast-track renewal. And, even if it had cleared Congress, you can be sure that it would have been a divisive North-South issue, as indeed it is. All this, of course, slows down trade liberalization, thus missing that bird. But I would contend that linkage makes you miss the other bird as well: the social agendas themselves get compromised. For, remember that when you take your moral agendas to the trade arena, the dominant players there are trade lobbies; and this context inevitably taints your program with the stench of competitiveness considerations. In fact, this distortion is very real: as many of us have observed, the objectionable PPMs that are currently specified in the Social Clause being proposed by the US, France and some other countries at the WTO are, unsurprisingly, those where the competitive developing countries are expected to be the defendants, not the developed countries that fear the competition. Thus, you have child labor in the Clause. But there is nothing there about sweatshops or the treatment of migrant labor: the former would affect almost half of the US garment industry while the latter would hurt deeply US agriculture if the occasional documentation of quasi-slavery on several farms using migrant labor is to be believed.

So, the very choice of what you put into the Social Clause and what you leave out of it reveals the cynical reality that the moral face of this Clause is a mask hiding the fear of competition. So, you devalue the morality of your social agenda and hurt the cause, thus missing the other bird as well.

Linkage thus undermines both the freeing of trade and the advancing of our social agendas. We need another stone, or a number of pellets to aim at a number of birds. Of course, this is the economists' **theory of economic policy**: generally speaking, we have to match the number of instruments with the number of targets. And we do have the possibility of fashioning new stones, as required. Thus, it is perfectly possible for us to pursue freer trade through WTO-led trade negotiations and treaties, while pursuing children's rights (including freedom from juvenile capital punishment) quite universally through UNICEF, child labor questions jointly between UNICEF and ILO, environmental improvement through UNEP, humane treatment of refugees through UNHCR, and so on. I have long proposed also the creation of a World Migration Organization to oversee the ethical and economic dimensions of immigration flows quite generally, repairing this great lacuna in the international superstructure today. By bringing impartial, symmetric and systematic reviews of national policies in these areas, these agencies can bring to bear moral suasion to bear in desirable directions, prodding nations into better behavior, thus spreading morally attractive agendas with universal appeal.

Moral and financial support of NGOs, in turn, can be important aids in mounting pressures for change, based on these impeccable and impartial reviews (as distinct from the biased and witless national reviews which, as with the State Department on Human Rights, and USTR on unfair trade, concentrate on others while turning a blind eye to our own failings). I am often told that the ILO, for instance, is toothless, its research incompetent and its structure unproductive. Even if this were true, surely the answer for a superpower such as the US is to open the jaws and put in the missing teeth by, if I may mix metaphors, putting our shoulders to the wheel.

Nor should we forget instruments such as **aid and technology transfer**. Thus,
consider the recent WTO "shrimp-turtle" case to see how aid could well have solved a gratuitous conflict. When the WTO Appeals Court recently found against our legislation because it had, without prior efforts at negotiations, unilaterally excluded shrimps from countries which did not mandate the use of narrow-necked nets that would prevent turtles from being caught in them, the US environmentalist groups went ballistic against the WTO. But surely, this is ridiculous. The fishermen in the plaintiff countries (India, Pakistan and Malaysia, with Thailand joining the case but having no shrimp fishing in dispute) could have been outfitted with the desired nets by the United States, which valued turtles, at something like $50.00 a net at Wal-Mart. The issue would have been off the front pages and the evening news and the objectives of both freer trade and the turtle-protecting environmental groups would have been creatively reconciled at no social cost if only a half dozen aid-financed boondoggle economics conferences in Bangkok and New Delhi had been cancelled and the moneys diverted to such a program.

The same might be said of technological assistance. We all know how the Global Warming treaty has been facilitated by the use of technological transfer to the developing countries by the US and other OECD countries. But let me tell you how the Save the Tiger campaign might also be aided by ingenious use of technology to effectively supplement, if not substitute for, the use of trade sanctions. The danger to the tiger comes from the CITES-illegal demand for it Chinese communities on the mainland and overseas because its organs are considered as an aphrodisiac by them. But take Viagra now. It has of course swept America, which is no surprise. But if only this potent drug, which is surely more effective as an aphrodisiac and far cheaper than smuggled tiger parts, were made even more cheaply available by our EPA and USAID in South East Asia, we would help reduce the demand for tiger organs and thus help save the tiger from extinction.

So, to return to my main theme, we need to recognize and proactively pursue the numerous possibilities of fashioning alternative policies that are more cost-effective than burdening trade treaties and negotiations with social agendas as preconditions for the freeing of trade. We need to develop, and bring our citizens to its embrace, a clear conception of what I like to call Appropriate Governance, i.e. how to accommodate creatively, while preserving the efficient pursuit of free trade, the different social or values-related agendas on the stage today. I submit that, instead of the intellectually lazy option of accepting the demands to pile everything on to the WTO and thus trying in a futile fashion to kill two birds with one stone, our politicians should be providing the leadership to argue forcefully and unequivocally that it is best to pursue (except when unavoidable interface exists) free trade and social agendas in different fora, with equal fervor.

Indeed, if I may end on a general observation of central importance, the pursuit of free trade, and indeed of economic reforms everywhere, is a moral agenda as well. For, without the prosperity that free trade and other reforms will engender, we can only carry our liberalism on the lapels of our jackets, not translate it into the reality that alone matters. So, free trade is not an evil force that must be contained by social agendas; it is itself part of our overall moral agenda. And, the pursuit of these different moral agendas, including better environment and respect for human rights, must be pursued appropriately, without sacrificing any one of them (except when this is totally unavoidable) by designing the tools of appropriate governance.

Chapter 6

Addressing Environment and Labor in the WTO

Steve Charnovitz
Associate, Wilmer, Cutler & Pickering, Washington DC

The linkages between trade, environment, and labor should be addressed by the World Trade Organization (WTO) both to increase public support for freer trade and to achieve more coherent international governance. This presentation will suggest that there are many useful steps that the WTO could take in Seattle. For those who follow environment and labor issues, my proposals may look minimalist. But in working on these issues for many years, I have seen how hard it is to make any progress.

Let me start with a few recent news items that can help in framing the debate. In early July, the Secretary-General of the United Nations issued a Joint Statement with the International Chamber of Commerce (ICC) reporting on the continuing dialogue between the two organizations. Among many interesting points, the Statement said:

> The rules-based multilateral trading system was not designed to address these non-trade issues [meaning labor rights, human rights, and environmental protection]. To call on it to do so would expose the trading system to great strain and the risk of increasing protectionism while failing to produce the desired results.[1]

Around the same time a Thai government official said that Thailand will reject any proposal that labor issues be included in the new trade round.[2] Another news item said that The Philippines will call on the WTO to defer inclusion of labor and environment issues in its new agenda.[3]

How should one appraise these statements and similar ones coming from many developing countries? It depends on what they mean. If Kofi Annan and the ICC are saying "Don't try to negotiate labor and environment policy in the upcoming WTO round; keep these issues in the international institutions where they belong," then this would be good advice. If Mr. Annan and the ICC are saying that the rule-based trading system has no jurisdiction over national measures used for environmental protection, then this would be welcome news to many non-governmental organizations (NGOs) who were disappointed with WTO Clean Air and Shrimp-Turtle cases. (But the news would be untrue.) If Mr. Annan and the ICC are saying that there are no economic and ecological

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[1]Joint Statement on the Global Compact proposed by the Secretary-General of the United Nations, July 5, 1999.

[2]"Thailand Will Reject Inclusion of Issues Connected to Labor in WTO Trade Round," *Daily Report for Executives,* July 8, 1999, at A59.

[3]"Philippines to Urge WTO Deferral of Links to Labor, Environment Issues," *Daily Report for Executives,* July 8, 1999, at A5.

links between trade and non-trade issues, then the Joint Statement would surely be wrong.

That salient links exist between trade flows and environmental protection cannot seriously be questioned. In the absence of proper environmental regulation and resource management, increased trade might cause so much adverse damage that the gains from trade would be less than the environmental costs. Years of analytical work in the OECD have shown that the scale, structure, and physical effects of trade can potentially harm the environment. While it is probably true that most trade causes little adverse impact, the fact is that when trade does cause harm (even outside the territory of the exporting nation), the WTO does nothing about it.

In view of the inattention to these linkages, it may not be surprising that over 500 environmental NGOs in 60 countries have teamed up to fight the new round. Similarly, some environmental groups are opposing an "early harvest" in forest products liberalization out of a fear that it would accelerate deforestation. These NGOs are surely overreacting. But can anyone honestly assure them that their fears are wholly unfounded?

Links also exist between trade and labor, but of a different kind. While exploitative labor conditions can be bad for workers (leaving aside the question of whether they get compensated by higher wages), such conditions exert no physical effect on the consumer in the importing country. There is nothing analogous in labor policy to transborder spillovers of environmental "bads," or to global challenges like climate change. The trade-labor effects are purely economic, and largely distributional. Trade can cause job loss, but is unlikely to do so for a country as a whole. While there have been many episodes where export imperatives have led governments to violate core labor rights, these episodes have typically occurred in non-democratic countries. Thus, at least among democratic countries, greater trade is unlikely to be bad for workers in aggregate.

The different way in which trade affects the environment from how it affects workers points to the need to separate "trade and environment" from "trade and labor" as policy issues. Prescriptions for environment may be inappropriate for labor. Moreover, labor is less compelling as an issue that requires international cooperation. Of course, the world community acknowledged in 1919 when establishing the International Labor Organization (ILO) that labor policy cooperation among governments was desirable and that labor rights were to be part of international law.

Appropriate Policy Assignment

I doubt that Mr. Annan and the ICC are denying that trade, environment, employment, and development are all linked. They are making a point about appropriate policy assignment in the international community. What I think they are saying is "Don't put environment and labor on the agenda for the next WTO round." Thailand and The Philippines are probably saying the same thing.

Undertaking trade negotiations on environment and labor measures would be a bad idea.[4] To start with, it would be fruitless. The issues are far too polarized within the WTO to achieve a consensus, especially at a time when new protectionist measures are being taken. But the more important reason to avoid such negotiations is that international environment and labor issues deserve continuous attention by governments rather than episodic attention in Rounds held years apart. Furthermore, environment and labor do not fit well into a negotiation where nations horsetrade their perceived commercial interests.

It would make no sense to condition further trade liberalization upon progress on labor and environmental issues.[5] That would be like the ILO refusing to approve a treaty addressing the worst forms of child labor unless governments agreed to reform antidumping laws that thwart developing country exports. In general, progress on one goal should not be held up to await progress on another (especially when complementary).[6] The sooner we can achieve more trade liberalization, the better.

In counseling against such negotiations, I do not mean to suggest that environment or labor should be absent from the new round. There are environmental reasons to liberalize trade and reduce distortions and it is appropriate to talk about that in the WTO. Negotiations on services -- such as energy and tourism -- might be given a boost by pointing to the environment as a reason to conclude the talks quickly. Negotiations on subsidies could benefit from greater attention to the environmental harms of fishery, agriculture, forest, energy, and mining subsidies.

That's why the idea of conducting an environmental impact assessment of the new round is so valuable.[7] Environmental factors should be considered by government trade negotiators. If a trade initiative will help the environment, then it should be given a high priority. If a trade initiative will hurt the environment, then governments should think twice about going ahead with it. Having a process of environmental assessment should lead to a more nature-friendly trade round and will also give the public greater assurance that the WTO does not look at its mandate too narrowly.

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[4]Of course, there is a counterargument: Since international environmental decisionmaking affects countries differently and requires some attention to national commercial interests (e.g., climate change), some issues might be brought into the WTO so that there will be broader issue sets among which mutually beneficial deals could be made. But any attempt to link trade liberalization with higher environmental standards is sure to give both the North and the South excuses to avoid further market opening.

[5]See, e.g., *Fair Trade and Harmonization. Prerequisites for Free Trade?* (Jagdish N. Bhagwati & Robert E. Hudec eds., 1996).

[6]For an analysis of when linkage might be appropriate, see Steve Charnovitz, "Linking Topics in Treaties," 19 *University of Pennsylvania Journal of International Economic Law* 329 (1998).

[7]At least four governments – the European Union, the United States, Canada, and Norway – have announced that they will be doing such assessments. It would be good if an international process could be devised to examine such nationally-produced assessments.

To assure that the environmental impact of trade agreements is given adequate consideration, it would be helpful for the U.N. Environment Program to create a group of environment ministers to monitor the new round. Such a parallel group could also give advice to trade negotiators regarding any new WTO rules being considered.

So far I have identified with Mr. Annan, the ICC, and the ASEAN countries, but in the remainder of my presentation I am not sure whether we agree. While labor and environment as such should not be negotiated in the new round, there are several useful steps that trade ministers can take in Seattle regarding these two issues. Before discussing this, let me point out that it is important for the WTO to grow out of the "GATT mindset" of a negotiation marked by rounds. The WTO is now a cutting-edge international organization with institutional capacity to interpret its rules, propose WTO amendments, cooperate with other international organizations, and work with civil society.[8] It must not hesitate to make new policy outside of the context of trade rounds.

Next Steps on Environment

The Ministerial Council should take the following actions on trade and the environment:[9]

1. **Subsidies**– Analytical work in the Organization for Economic Co-operation and Development (OECD) and the WTO Committee on Trade and Environment have shown that some subsidies – for example, agriculture and fisheries – can be bad for the environment as well as trade-distortive. It is time for the WTO to address this problem in cooperation with other international organizations. One option is to get governments to agree to phase out such harmful subsidies. Another is to prohibit such subsidies, just as export subsidies are prohibited. Another is for the WTO to publicize these subsidies in order to inform citizens in the country using them. The WTO might assign this issue to its Committee on Subsidies and Countervailing Measures and ask for a report and recommendations within a year. It should be noted that earlier this year, several governments proposed that the WTO work to reduce or eliminate fishery subsidies that contribute to overfishing.[10]

2. **International Standards**– The WTO Agreement on Technical Barriers to Trade (TBT) calls on governments to use international standards as a basis for their technical regulations (unless such standards would be ineffective or inappropriate).[11] The preeminent standardizing organization, the ISO, has several environmental management standards (e.g., ISO 14000). The Seattle Ministerial should direct the TBT Committee to

[8]Agreement Establishing the World Trade Organization, arts. IX:2, X:1, V:1, V:2.

[9]In proposing that the Ministerial Council take these steps, I am aware that some of them could be acted upon by the WTO Council or WTO Committees. But no such action has occurred at the lower levels since 1995.

[10]The countries are Australia, Iceland, New Zealand, The Philippines, and the United States.

[11]TBT art. 2.4. Some international standards might fall outside the purview of this article because they deal with processes and production methods that are unrelated to the product.

promote the use of ISO environmental standards and to assist developing countries in acquiring the technical assistance that they need.[12]

3. **Dispute Settlement**– The WTO should try to avoid becoming embroiled in trade and environment disputes. The WTO dispute settlement provisions (art. 5) authorize the Director-General to offer good offices, conciliation, and mediation, but these procedures have not been utilized. The Seattle Ministerial Conference should issue a declaration calling on WTO members to try to resolve environment-related conflicts without invoking dispute settlement. Such a declaration should also call for the Director-General to appoint a high-level conciliator when new disputes arise. For example, in the Shrimp-Turtle case, a conciliator might have helped both sides work out an international agreement.

Many other actions by the WTO are needed – for example, clarifying that trade measures taken pursuant to multilateral environmental agreements will not be adjudged a WTO violation.[13] While no such measure has been challenged in the WTO, environmental negotiators are under increased pressure not to use trade measures in new environmental treaties. A solution to this problem is long overdue. But in the present political climate, it is difficult to imagine any progress being made.[14] None of the governmental proposals comes close to resolving the issue in a balanced way.

Next Steps on Labor

As noted above, labor is different than the environment. With one historical exception, there are no multilateral labor treaties that use trade measures as an instrument of employment policy. Nor are there expected to be many labor-related disputes going to the WTO. Nevertheless, there is much that the Seattle Ministerial can do to reposition the WTO to promote higher labor rights. The Ministerial Council should take the following actions on trade and workers:

1. **Forced Labor**- GATT Article XX(e) permits governments to ban products made by prison labor. Yet the WTO provides no assistance to governments in knowing when forced or prison labor is being used in exported products. Some might argue that this is none of the WTO's business. Yet the WTO could lift its esteem with the public if it were to work with other organizations to foster more information-gathering about the "forced labor content" of exports. Not many countries currently ban imports made by forced labor. Yet more would do so if better information were available. It is interesting

[12]TBT arts. 11, 13.

[13]The National Wildlife Federation has proposed an explicit deference to MEAs. "Trade Policy Lacking Environmental Content Cannot Win Public Support Needed to Succeed," NWF Press Release, May 20, 1999.

[14]According to India's Centre for International Trade, Economics & Environment, "developing countries continue to view attempts to accommodate MEAs in the WTO as a Northern agenda." *Ratchetting Market Access*, CUTS, 1998, at 34.

to note that in June 1999, the ILO passed a resolution deploring the widespread use of forced labor in Myanmar.[15]

2. **Social Labels**– There is pressure within some countries to use trade measures to prevent imports of products made under labor conditions violative of fundamental labor rights. A less coercive approach would promote new labeling systems to certify that the production process did not violate any core international labor standards. The Seattle Ministerial might establish a working group to examine social labels that could work with the ILO in any future consideration of a Convention on private labeling and certification. It is important that labels be truthful and not be designed in a way that disadvantages imports.

New Institutional Steps

Although the 20th century has shown the advantage of functional international organization, it is apparent that the lack of coordination among organizations is a major deficiency. As Renato Ruggiero stated a few months ago, "We can no longer treat human rights, the environment, development, trade, health, or finance as separate sectoral issues, to be addressed through separate policies and institutions."[16] The WTO needs to do a much better job of coordinating its work with the World Bank, the OECD, the U.N. Conference on Trade and Development, the World Health Organization (WHO), the Food and Agriculture Organization (FAO), UNEP, the ILO, and others. The Seattle Ministerial should call for improved coordination and provide that the WHO, UNEP, and the ILO be given opportunities to participate in WTO Committees and to observe Council meetings.[17]

For high profile issues, the WTO should consider establishing more extensive cooperative procedures. For example on food safety, there should be closer cooperation with the Codex Alimentarius Commission. On emissions trading, there should be cooperation with the Parties to the Climate Change Convention. On fishery subsidies, there should be cooperation with the FAO. On trade and employment, there should be cooperation with the ILO Working Party on the Social Dimensions of the Liberalization of International Trade.[18] On access to medicine in poor countries, there should be

[15]Resolution on the Widespread Use of Forced Labor in Myanmar, International Labor Conference, June 1999.

[16]Renato Ruggiero, "Beyond the Multilateral Trading System," April 12, 1999.

[17]Norway proposed this recently (leaving out the ILO). See Norway, "Preparations for the 1999 Ministerial Conference," WT/GC/W/176, April 30, 1999.

[18]In June 1999, the G-8 Summit Communiqué stressed the importance of effective cooperation between the WTO and the ILO on the social dimensions of globalization and trade liberalization. Final Communiqué of Cologne Summit, para. 26, *Daily Report for Executives*, June 22, 1999, at T11. In July 1999, the European Commission proposed a joint WTO/ILO high level meeting on trade, globalization, and labor issues. See "The EU Approach to the Millennium Round," July 8, 1999. This might be a good idea if sufficient lower-level work preceded the high-level meeting.

cooperation with WHO.[19] On the patenting of life forms, there should be cooperation with the parties to the Convention on Biological Diversity.

Another vital institutional step would be for the WTO to improve its interface with civil society. Although some governments argued last March at the WTO Symposia that NGOs should provide input through "their own government," this is inadequate in at least three ways. First, transnational NGOs, such as Consumers International, are established to influence all governments. Second, some NGOs operate in countries that have not been allowed to join the WTO (e.g., China). Third, many NGOs in protectionist countries have lost political battles at home and hope to use the WTO to put pressure on their governments to follow WTO rules. Thus, no normative reasons exist for the WTO to continue resisting NGO involvement.

It would be good for the WTO to hear a broader range of views than are put forward in Geneva by government officials. Consultation and cooperation with NGOs can make the WTO more effective and has the potential of generating public support for a rule-based trading system.[20] There are many modalities for achieving greater NGO involvement. For example, the U.S. Business Roundtable recently proposed that once a year, the WTO convene a meeting of various groups such as consumers, business, environment, and labor.[21] The WTO could also ask two NGOs headquartered in or near Geneva – the World Conservation Union/IUCN and the International Centre for Trade and Sustainable Development – to help manage the process of NGO input. It should also be noted that if the WTO confers cooperative status on the ILO, it could send observers from labor unions and employer organizations.

[19] "WHO to Address Trade and Pharmaceuticals," WHO Press Release, May 22, 1999.

[20]In May 1999, the OECD Communiqué of Trade and Finance Ministers stated that "Active and constructive communication and consultation with civil society are essential for public understanding of the benefits and challenges of liberalization."

[21]The Business Roundtable, "Preparing for New WTO Trade Negotiations to Boost the Economy," May 1999, at 26.

Conclusion

The debate on environment, labor and the WTO remains polarized among governments as well as interest groups. There is a danger that mismanagement of these issues in Seattle could undermine support for the new round even before it begins. The WTO should not negotiate environment and labor as such.[22] But the WTO can take steps in Seattle that would promote greater harmony between free trade and other social objectives.

[22]See the section on "Limiting the WTO's Role" in WWF Position Statement, March 1999.

Chapter 7

A Comment on Attempted Linkages Between Trade and Non-Trade Issues in the WTO

Martin Khor
Director, Third World Network

Introduction

There is a distinct trend, starting with the Uruguay Round, to introduce and inject "new issues" and yet another round of more "new issues" into the GATT and the WTO system.

This was initially done through the argument that the particular issue is "trade related." Thus, in the Uruguay Round, negotiations were undertaken and later Agreements were completed on "trade related intellectual property rights" and "trade related investment measures." The prefix "trade related" was carefully attached to the new issue to symbolize that it was somehow legitimate to bring under the ambit of the WTO and its principles and rules.

This need of justification by proponents of linking more new issues to the WTO has even recently been reduced, as evidenced by the dropping of the "trade related" prefix to the issues. Thus, we now have only the simple word "and" that is used in attempts to link one new issue after another in the WTO: "trade and environment", "trade and labor standards", "trade and investment", "trade and competition policy". In the case of government procurement, it is simply "government procurement."

Of course a justification can always be made that this or that issue is linked in some way to "trade." But that does not mean that it is justified to link the issue to the WTO and its system. For an issue to be linked to the WTO system in an integral way, it must be made to meet a strict test with clear criteria, and moreover there should be a framework that helps specify in which way the particular issue should be integrated in the WTO. Issues chosen should be for the benefit of Members, especially the developing countries that form the majority, and should be treated in a manner that leads to equitable results.

At present there is no such framework determining whether and how "new issues" should enter the WTO system, nor a way to determine the likely benefits and costs and their distribution among the WTO membership.

Yet there are very strong pressures, emanating from the developed countries, to add more and more items onto the WTO agenda. There is now a clear danger that this could lead to very negative consequences: (a) an overload of the WTO system, making it impossible for developing countries to cope with negotiations and implementation; (b) a distortion of the WTO system, where fairness in the process of trade operations is replaced by protectionism; (c) a failure of credibility as citizens in developing countries perceive the WTO as an instrument by the developed countries to impose unfair and inappropriate rules and policies that are disadvantageous to the developing countries. Moreover it is also unlikely that the intended objectives of the proponents of the new issues will be met.

In the light of the already onerous obligations undertaken by developing countries in the existing WTO Agreements, the immense problems of implementation, and the possible serious economic and social dislocation that will result in many countries, it is most inappropriate for the continuing and intensifying pressures to place more new issues onto the WTO.

Why the Pressures for Linkages to the WTO?

Despite the oft-repeated claim that the WTO is a democratic organization that caters to the interests of all Members who have equitable participation in decision-making, in reality the WTO is essentially a power-based organization where countries with trade strength and greater economic and political power have an overwhelming influence.

This does not mean that developing countries do not have bargaining power; but most of them are understaffed, as a result they lack the capacity to be adequately prepared in negotiations. Even though many (or even most) of the developing countries may be opposed to the entry of certain new issues, they find it difficult to resist. Eventually even if they agree, it is not because all of them fully understand, appreciate or are in favor of negotiations or Agreements in new areas. Many of them were, and are, just unable to withstand the tremendous pressures exerted on them not to stand in the way of negotiations or Agreements on new issues.

Such was the case with the negotiations and Agreement on TRIPS. Intellectual property rights is not about trade liberalization, but has the reverse effect in that TRIPS will hinder technology transfer and is likely to maintain and increase monopolization of technology.

It is in fact a protectionist device that hinders technological development Yet it entered the WTO system, even though many developing countries tried to resist its introduction into the GATT system, and tried for many years of the Uruguay Round to limit its scope.

On investment, another "new issue", there were strong pressures during the Uruguay Round by developed countries to have an investment agreement with a wide scope covering investment per se (right to establishment, national treatment, etc). Developing countries were able to narrow the scope of TRIMS to the trade-related measures. But the door called "investment" had been opened, and as could be predicted there are now very strong pressures to pull the whole investment issue per se back onto the WTO agenda. This time the "trade related" prefix has been dropped for the simple (and more wide-ranging) "trade and investment." As a result of strong opposition from several developing countries, the developed countries were unable to get the Singapore Ministerial 1996 to endorse negotiations for an investment agreement. The Ministerial decided only on establishing a working group to study the trade and investment relationship. But now there are pressures again to have the Seattle Ministerial launch negotiations for an investment agreement.

Some developed country Members are also strongly pushing for trade and competition policy, and for government procurement (firstly an interim agreement on transparency and eventually a full agreement incorporating national treatment).

The pressures for the linkages between WTO and IPRs, investment, competition policy and procurement are generated by the large corporations of the developed countries, whose governments then push for Agreements in the WTO to open up market and investment access for these corporations to the developing world. In the case of IPRs, the WTO was used as a means to protect the technology monopoly of the companies, and to make it difficult for local companies in developing countries to emerge with the technology to rival the established big corporations.

I believe that the WTO was chosen as the venue or forum for the introduction and injection of the above new issues for these reasons:

(a) The dispute settlement system (especially since it is "integrated" to facilitate cross-sectoral retaliation) makes the WTO an institution that can effectively enforce rules (through the mechanism of trade sanctions) and thus the WTO is an ideal institution for creating binding and enforceable rules that can disciplining countries in a certain framework of global governance;

(b) It is argued by the proponents of the new issues that the core principles of the WTO are trade liberalization, national treatment and MFN. Thus, issues like investment, competition and procurement are likely to be treated in a certain way, that favors market access for the big corporations, should these issues be discussed or negotiated within the WTO. In contrast, should the issues be the subject of discussion or agreements or codes in for a such as the United Nations, the issues are likely to be treated differently, in a more balanced way, in which the development dimension and interests of developing countries are given higher priority and where the perspective will be more balanced in incorporating the social and development dimensions.

(c) The proponents of the above linkages are developed countries which by and large have overwhelming influence in the WTO, particularly in negotiations on new issues and in formulating of legal texts. As stated above, developing countries as a whole and individually still lack the capacity to match the developed countries in negotiations. It can thus be predicted that the manner in which a new issue is interpreted and integrated or absorbed into the WTO will be determined by the stronger developed countries. Thus, in the battle of interpretations, the developed countries' perspective is likely to win out. This is why the WTO is a better venue than for example the United Nations, from the viewpoint of the proponents of linkages.

There is another set of "new issues" that are knocking on the door to enter the WTO system. These are issues that are advocated not so much by the corporations of the developed countries for market-access reasons, but by social organizations (mainly of the North but also including some in the South) that are seeking (in their view) ways to protect or promote their interests. The environment and labor are presently the key issues in this category of linkages. There may be attempts in future to introduce other issues, such as human rights, gender equity, etc. Indeed, if environment and labor were

to enter the WTO system as subjects for agreements, it would be conceptually difficult to argue why other social and cultural issues should also not enter.

The objectives of the social organizations in linking their particular causes to trade measures are different from the aims of corporations who seek linkages (in investment, procurement) to gain greater market access and market share, or (in IPRs) to protect their domination and hinder potential new rivals. The social organizations are looking for more effective ways to protect their interests and believe that the instruments of trade measures or trade sanctions can be very effective. They believe that their causes (to defend animal rights and life and conserve the environment, or to protect jobs and promote higher social standards) can be most effectively promoted if governments of countries that have "low environment and social standards" are faced with the potential threat of trade measures and sanctions on products that are produced using the low standards.

In this, the social organizations concerned are seeking methods similar to the corporations, in that they are pressuring their governments and negotiators to make use of a strong enforcement mechanism (unilateral trade measures, or the dispute settlement mechanism of the WTO backed up with the possibility of trade sanctions).

Thus, trade measures have become methods of choice, and the WTO has become a vehicle of choice, for big corporations and some social organizations in promoting their interests.

Trade and Environment

That there are links between trade and environment cannot and should not be denied. Trade can contribute to environmentally harmful activities. Ecological damage, by making production unsustainable, can also have negative effects on longterm production and trade prospects. In some circumstances trade (for example, trade in environmentally sound technology products) can assist in improving the environment.

What is of concern or relevance in looking at "linkages" is the advocacy of the use of trade measures and sanctions on environmental grounds. Some environment groups and animal rights groups believe that national governments should be given the right to unilaterally impose import bans on products on the grounds that the process of production is destructive to animal life, and that WTO rules should be amended to enable these unilateral actions.

Some groups, and some developed country Members of WTO, go further and have advocated the a set of concepts linking trade measures in the WTO to the environment. These concepts are processes and production methods (PPMs), internalization of environmental costs, and eco-dumping. The three concepts are inter-related. When discussed in the WTO context, the implication is that if a country has lower environmental standards in an industry or sector, the cost of that country's product is not

internalized and the prices are thus too low (being unfairly subsidized by the low standard) and thus that country is practicing "eco-dumping." As a result, an importing country would have the right to impose trade penalties, such as levying countervailing duties, on the goods.

This set of ideas poses complex questions relating to concepts, estimations and practical application, particularly as they relate to the international setting and to the WTO. Developing countries are likely to find themselves as a great disadvantage within the negotiating context of the WTO should the subject (which has already been discussed in the Committee on Trade and Environment) come up for negotiations. One of the main issues is whether all countries should be expected to adhere to the same standard, or whether standards should be allowed to correspond to the different levels of development. The application of a single standard would be inequitable as poorer countries that can ill afford high standards would have their products made uncompetitive. The global burden of adjustment to a more ecological world would be skewed inequitably towards the developing countries. This is counter to the principle of "common but differentiated responsibility" of the UNCED or Earth Summit in which it was agreed that the developed countries, which take the greater share of blame for the ecological crisis and have more means to counter it, should correspondingly bear the greater responsibility for the global costs of adjustment. Given the unequal bargaining strengths of North and South in the WTO, the complex issues relating to PPMs, cost internalization, trade related environment measures etc. should not be negotiated within the WTO but if at all discussed, the venue should be the United Nations (for example in the framework of the Commission on Sustainable Development) in which the broader perspective of environment and development and of the UNCED can be brought to bear.

Unilateral trade measures taken by an importing country against a product on grounds of its production method or process are also fraught with dangers of protectionism and the penalizing of developing countries. However tempting the route of unilateral import bans may be for the environmental cause, it is an inappropriate route as it will lead to many consequences and could eventually even be counter-productive.

Policies and measures to resolve environmental problems (and there are many genuine such problems that have reached the crisis stage) should be negotiated in international environmental fora and agreements. These measures can include (and have included) trade measures.
The relationship between the WTO and its rules and the MEAs is the subject of debate in the WTO. On one hand there is the fear (of developing countries) that a system of blanket and automatic approval by the WTO of trade measures adopted by a "MEA" (for example by an amendment to Article XX to enable ex-ante approval of MEA measures) could lead to abuse and protectionism. A sticking point here is what constitutes a "multilateral environment agreement" as it may be include not only truly international agreements convened by the UN and open to all members and enjoying near-universal consensus, but also agreements drafted by a few countries which then invite others to join (and would then also enjoy exemption under the proposed amended WTO rules).

The fear of protectionist abuse explains the reluctance of developing countries to amend Article XX, which in their opinion is already flexible enough to enable exceptions to accommodate environmental objectives.

On the other hand there is the genuine fear of environmental groups (and also developing country and some developed country Members of WTO) that negotiations in new MEAs can be (and are being) undermined by the proposition of some countries that WTO rules prohibit trade measures for environmental purposes, or that WTO "free-trade principles" must take precedence over environmental objectives. Such arguments were for example used by a few countries in the so-far failed negotiations for an International Biosafety Protocol. Such arguments are false, as the WTO allows for trade measures agreed to in MEAs through the present Article XX (although not in the ex-ante manner proposed by some countries). The use of the WTO name by a few countries to turn away the proposals by the overwhelming majority of delegations to establish checks on the trade in genetically modified organisms and products (through a prior informed consent procedure) gave the impression that commercial interests were placed before global ecological and safety concerns and understandably generated outrage among most delegations as well as environmental and social organizations. Negative actions like this that blatantly use the slogan of "free trade" to undermine vital health and environmental concerns are the reasons for the erosion of public confidence in "free trade" and the WTO system. Thus governments must be careful not to wrongly make use of "free trade" or "WTO rules" to counter international agreements that deal with genuine environmental problems, otherwise the credibility of the trading system itself will be eroded even further.

For many NGOs (especially of the South) as well as developing country WTO members, an important "trade and environment" issue is the effect of the TRIPS Agreement in hindering access to environmentally sound technologies and products. There can be "synergy" between liberalization, environment and development objectives if TRIPS is amended to enable exemptions for environmentally sound technology. Also, Article 27.3b of TRIPS opens the road to patenting of life forms. Adverse effects include facilitation of the appropriation of traditional knowledge on the use of biological resources by corporations who claim to meet the patent test; promotion of environmentally harmful technologies; and promotion of technologies that are against the interests of small farmers (such as the "terminator technology" or "suicide seeds" or seeds engineered not to reproduce themselves so that farmers are prevented from saving seeds). These are examples of some issues that can and should be taken up in trade and environment reviews of various Agreements.

In short, discussions within the WTO entailing the environmental effects of WTO rules can be beneficial, provided the environment is viewed within the context of sustainable development and the critical component of development is given adequate weightage.
The Committee on Trade and Environment should orientate its work to the more complex but appropriate concept and principles of sustainable development. But there should not be any move to initiate an "environment agreement" in the WTO that involves concepts such as PPMs and eco-dumping.

Trade and Labor Standards

The push for incorporating labor standards with trade measures in the WTO has come from labor unions in the North and international trade unions which also have affiliations in developing countries. Some trade unions in some developing countries are however opposed to including labor standards in WTO. The issue of labor standards is also linked to the concept of "social clause" (which is broader than labor standards and could include the rights of various groups in society) and supported by some political parties in developed countries.

There may be various strands in the objectives of the advocates. Many trade unions believe that transnational corporations are relocating from countries with higher labor standards to those with lower standards, and that this trend acts to depress labor standards by reducing bargaining power of workers. They also believe that by linking the threat of trade sanctions to labor standards, there will be pressure to upgrade the level of standards in developing countries. They are careful to include only internationally-recognized core labor standards and to exclude the issue of wage levels in the demands for linkage to trade and WTO.

Other advocates believe that the linking of social issues (including but not exclusively labor standards) to the WTO and its sanctions system of enforcement is an effective way of countering the adverse social effects of free-trade free-investment globalization, by forcing corporations and governments to observe socially responsible policies.

Developing countries fear that the objectives of the Northern and international trade unions, and of developed country governments that back the social clause demand, are mainly protectionist in nature, i.e. to protect jobs in the North by reducing the low-cost incentive that attracts TNCs to developing countries. They argue that low labor costs in their countries are a function not of deliberate exploitation of workers but of the general low standard of living and the lower level of development, and that the low cost is a legitimate comparative advantage. They therefore have opposed the inclusion of labor standards in the WTO, and argued successfully (as reference the Singapore Ministerial Declaration) that the issue belongs in the ILO.

There is of course justification for public interest groups to be concerned about the social consequences of globalization and liberalization and to campaign to change the nature and effects of the present globalization trends. However the issue is whether labor standards and social clauses in trade agreements is the or even an appropriate route. There is merit in the argument that labor standards or the "social clause" should not be introduced in the WTO. This is because:

(a) Such an issue when placed in the WTO context would be linked to the dispute settlement system and the remedy of trade penalties and sanctions. In other venues, there is the option (which many would argue is more appropriate) of linking the improving of labor standards to positive incentives rather than punitive measures.

(b) Even though most advocates only demand minimum labor standards such as the right of association for workers, there is no certainty that the issue will be so confined in the future. Once the concept of social issues and rights enters the WTO system, it can in future be expanded within the particular issue (eg an extension to social security and wage levels within the issue of labor standards) and extended to other issues (such as the rights of children, women, disabled, human rights in general, the right to education, health, nutrition, etc).

(c) It is possible or even likely that once rights and social issues enters WTO, the GATT concepts of dumping and subsidies, and the relief of countervailing duties, will sought to be applied. Thus, countries with low social standards would be deemed to be practicing "social dumping" (or unfairly subsidizing its products by avoiding to meet social costs) and importing countries could be enabled to impose countervailing duties.

(d) Developing countries are likely to bear the costs of loss of competitiveness. The low social conditions in the poorer countries are largely related to the low level of development and the lack of resources (although the wastage and mismanagement of resources also do contribute significantly). Lower social standards are thus linked to (though not entirely caused by) lower levels of development. It is very possible that the operationalizing of linkage between social standards and trade measures in the WTO system would lead to additional pressures being placed on developing countries and that many of their products would become higher cost and uncompetitive or face trade penalties or both.

(e) It is possible that the firms and products eventually affected are not confined to those involving trade and exports but also the firms (most of them small and locally owned) that cater to the local market. By not being able to remain competitive, some may close.

(f) It is also possible that the erosion of competitiveness and the higher costs (perhaps beyond what would normally prevail in countries at the existing stage of development) would cause loss of jobs, closure of firms and farms and reduced investment; or movement of some workers to more poorly paid jobs.

(g) The inclusion of labor standards would open the door to a much wider range of issues relating to social standards, social rights and human rights. Many new "conditionalities" would be introduced not only on trade at the border but production, investment, etc within the domestic economy. The issues will be so complex and complicated that they will tie the WTO system up in knots, and occupy the time and energy of diplomats and policy makers, not to mention the NGOs and social organizations, in an enterprise that is fraught with controversies, dangers and with no clear benefits guaranteed.

(h) Finally, the efforts of NGOs and social organizations could be directed towards the sources of the social problems within and outside the WTO. For example, to offset problems caused by the WTO, those concerned about human rights and the right of ordinary people to livelihoods and adequate incomes could examine and campaign for changes to aspects of the existing agreements (such as Agriculture, TRIPs, TRIMS, services) that affect farmers' rights and livelihoods, the viability of small farms, food security, the cost of medicines caused by drug patenting, etc. They could also try to prevent new agreements (such as investment, procurement, industrial

tariffs) that would affect the viability of local firms, the livelihood of workers and the people's right to development. And to counter problems whose sources are beyond the WTO, there can be intensified campaigns for debt relief, reforms to the IMF and structural adjustmeht programs, a pro-employment macroeconomic policy (rather than priority to restrictive monetary policy), improved human rights and against exploitative child labor and poor working conditions, etc. But the notion that linking social rights to a trade sanctions regime, though tempting at first sight, is likely to be counterproductive in results.

Conclusion

At present the WTO does not have a systematic way of enabling the assessment, introduction (or rejection), and the appropriate incorporation of new issues. As a result, several new issues have been absorbed during the transition from GATT to the WTO through the Uruguay Round. And many more new issues are in various stages of brewing, with advocates in governments (mainly of developed countries) and in social organizations pushing hard to gain entry for their favorite issues.

A system or procedure for assessing potential or proposed new issues should be established. The criterion should not only be whether an issue is "trade related", because a case can always be made that almost any issue is related in some way with trade. The criterion should be whether the entry of a particular issue would add advantage and benefit to the Members of WTO (especially the majority, i.e. the developing countries, and to the majority of people in these countries) and to the WTO system, with the ultimate goal of equitable and sustainable development (rather than liberalization, which is only a means). And given the fact that the WTO is mainly a negotiating body, with the mandate and task of formulating and monitoring the implementation of Agreements, issues should not be allowed to easily enter the system, even for a "study process" in a working group. Discussions on potential new issues should take place in appropriate for a outside the WTO, in a setting more conducive to perspectives broader than the more narrow framework of trade relations. In such discussions the role of trade relations can be placed in the broader context of equitable and sustainable development, and the specific role of the WTO (if any) can be demarcated. Until the discussion is sufficiently "brewed" or "matured" in the appropriate fora, the issue should not be brought into the WTO system, either for discussion in working groups and certainly not for negotiations for new Agreements.

Unless the trend for putting more and more issues into the WTO basket is reversed, the trade system will become overloaded and over-bloated. It will not be able to carry out the tasks which it was originally intended to do, because it would have taken on other tasks it is ill suited to perform, as well as grappling with a host of new and complicated issues which will tie up its Members, diplomats and policy makers with knots too difficult to disentangle from.

The Seattle Ministerial Conference can either decide to limit the WTO to the tasks it is supposed to do, and to review its rules and system to put it back on the right track, or it can decide to throw more issues and complications into the system, with unknown and probably dire consequences.

Chapter 8

Poor Environmental Policy: the Fundamental Problem in the "Trade and Environment" Debate

Alan Oxley
Chairman, National APEC Study Centre of Australia, Monash University Melbourne

Summary

Trade and environment is represented in North America and Europe as a major issue for the forthcoming Round of the WTO. Environmentalists want changes made to the WTO to enable it to better support measures to protect the environment. Greenpeace wants the WTO to recognize "the equal status of …..MEAs with its rules".[1] The World Wild Life Fund wants environmental concerns "mainstreamed into WTO Agreements".[2]

The dominant focus of discussion about trade and environment issues is the contention, as the World Wildlife Fund puts it, that "application of WTO rules continue to have unintended negative environmental and social consequences".[3] Two issues are used to support this contention. The first is that there is a conflict of obligations between Multilateral Environment Agreements (MEAs) and the Agreements of the World Trade Organization, principally the General Agreement on Tariffs and Trade (GATT). The second is that the rules of the WTO do not permit restrictions on products which have been made in a way that is injurious to the environment.

The preoccupation in discussion therefore is how to adjust the rules of the WTO to meet these two circumstances - first to accommodate the trade provisions of the MEAs and second to widen the grounds upon which trade can be restricted. There has been a long-standing proposal to widen the exceptions provisions in Article XX of the WTO to tolerate restrictions to meet these two cases.

The representation of "trade and environment" as an international problem in this way is perpetuating a situation which is producing poor public policy results. First, public instruments for environmental management are being developed which are at best ineffective and in some cases counterproductive; and they are being replicated. Second, proposals to buttress these measures are being put forward which would undermine the authority of the WTO trading system. This is creating a "lose/lose" paradigm.
Attention needs to focus on what actions will secure a superior result for the environment. How effective are these trade measures at improving the environment? If this question were addressed, the so-called "trade and environment" problem would be seen in a different light. Trade controls, particularly the provisions in MEAs, are ineffective instruments for environmental management and, in some cases, are

[1] Greenpeace International Statement "WTO against Sustainable Development", circulated at the WTO HLG seminar on trade and environment, Geneva May 1999.
[2] WWF International Position Statement, March 1999
[3] Ibid

counterproductive to the environmental objectives of the agreements. Removal of them would make the MEAs more effective instruments for environmental management. This would solve the conundrum of the conflict of obligations between the MEAs and the WTO since it is the trade provisions in the MEAs which create the conflict.

The Trade Provisions of MEAs

There is only a handful of MEAs with discriminatory trade provisions. They put members of the WTO which are parties to the MEAs in a position they are in conflict with their obligations not to discriminate in their dealings with other members of the WTO. The treaties which are at the core of the problem are CITES, The Montreal Convention on Fluorocarbons and the Basle Convention on Transboundary Movement of Toxic Waste.

In each of those treaties, there are obligations to ban trade with non-parties to the treaties. The effect of these provisions is that the member of each MEA agrees to impose a penalty on non-parties because they have elected not to adhere to the MEA. The Australian Government has made it illegal for Australian companies to export to India products which, under the Basle Treaty, it may export to other members of the Treaty. The reason? India chose not to adhere to the Treaty. All other ratifiers of the Treaty have done the same thing. [4]

This is a considerable innovation in international treaty making of which not nearly enough has been made. The innovation is that Governments have decided to put sanctions on other Governments which elect not to join treaties. The right of sovereign governments to decide what is in their interests and not to be coerced by others, as set out in the Charter of the United Nations, is being disregarded. This was no doubt why all members of the UN at the Rio Summit re-affirmed respect for national sovereignty as a fundamental principle to guide all activity concerning trade and environment.[5]

The disregard for national sovereignty is also at the core of the conflict of obligations between the MEAs and the WTO. Like most other international treaties, the WTO also respects the principle of national sovereignty. Members may only restrict trade with other members on terms that are commonly agreed. Members may not independently set conditions on trade with other members, whether it is the United States acting unilaterally, as it has tried to do on a number of occasions, or whether it is a group of members acting collectively as parties to MEAs with discriminatory trade provisions.

[4] The key operational provision of the Basle Treaty is also likely to put WTO members into another position where they would breach the non-discrimination provisions of the Treaty. It requires each exporter to restrict exports until satisfied that the importer will handle them in "an environmentally sound manner". There are no objective criteria to determine what that is. Members will have to set their own standards. The likelihood of setting different standards for different countries is high. If members set conditions to trade which vary among members of the WTO, they would breach the requirement to treat all on the same basis.

[5] This principle is restated several times throughout the trade and environment principles.

The point that the trade provisions of the MEAs erode respect for national sovereignty is rarely made plainly in discussion about the MEAs. Representatives of the European Community have for a number of years chosen to differentiate between unilateral action to restrict trade on environmental grounds and collective action, such as by a group of states as members of an MEA, arguing that the provision in the MEA is somehow less of a problem because a number states impose a discriminatory trade measure, rather just one. [6] There may be comfort in numbers, but the disregard of the principle of respect for national sovereignty is the same.

It this issue were plainly confronted, the following responses could be expected from environmentalists on the basis of established positions. The provisions in the MEAs are necessary because the environmental interest is overriding. Traditional notions of the sovereignty of the nation state are eroding. It is necessary to take such action to protect the global commons. In a discourse such as this, the next step would be to consider each of these propositions, to all of which there is a sound counter. Rather than do this the question of the environmental effectiveness of these trade provisions in the treaties will be considered. From a purely logical point of view, if that is found wanting, there is no requirement to consider the contention that exceptional or new circumstances require reconsideration of traditional notions of national sovereignty. So have the trade provisions of the MEAs improved the environment and, if they have, were they the most effective approach?

Before considering the effectiveness of the measures, it is worth recalling the trade and environment principles which were adopted in Agenda 21 at the UN Conference on Environment and Development (UNCED), colloquially known as the Rio Earth Summit. The consensus at UNCED was that trade measures should be eschewed as instruments for environmental management. The UNCED countries were emphatic that international action to improve the environment should be implemented by voluntary accession to multilateral treaties. It recognized unilateral trade sanctions as a reality, but did not endorse it. None of the three MEAs are consistent with the UNCED trade and environment principles because all contain discriminatory trade provisions which do not respect national sovereignty. [7] In adopting this position, members of the UN effectively reserved judgement on the three leading MEAs.

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[6] At the WTO High Level Seminar on Trade and Environment in Geneva in March 1999, The EU circulated a paper entitled "Message of the European Community to the World Trade Organization High Level Symposium on Trade and Environment". It argues there is room for use of trade measures in MEAs and seeks to distinguish between measures in MEAs and unilateral measures. "The fact that such measures (trade measures in MEAs) were negotiated and agreed in a multilateral context is in itself a guarantee against unilateral action and that they will not be used for protectionist purposes." It goes on to note "Many of the conceptual difficulties we are facing are due to the fact that the GATT Article XX…..was designed to deal principally with unilateral measures." This is an uncommon interpretation.

[7] The approach endorsed by UNCED is set out in the trade and environment principles. Like most UN communiques, they were negotiated and do not follow a structured order. However, there is remarkably consistent philosophy. UNCED adopted the concept of cohabitation between systems for management of the environment and management of an open trading system. The summary conclusion was that measures to open up international trade and measure to protect the environment should be "mutually supportive". Each system operates independently, but with regard to economic principles which ensured that

CITES is based on the presumption that banning exports and imports will restrict demand for the endangered species and that this will lead to their conservation. The Basel Treaty presumes that banning trade between parties and non parties and empowering exporters with responsibility for enforcing environment policy in the importing country will prevent the dumping of toxic waste. In the case of the Montreal Convention, the presumption is that banning trade with non-parties on top of pre-existing obligations on parties to ban production and consumption will stop countries outside the convention from developing CFCs.

The case for not using trade measures for environmental, or for that matter any other non-trade interest, is widely accepted among economists. Indirect instruments are poor instruments for environmental management. How effective is it for a country that might import five percent of the total production of another nation's dairy industry to elect to restrict imports of milk powder because the industry in the exporter is not controlling its effluent from its dairy plants and is damaging the environment in order to protect that environment? Not very. The only effective means to protect that environment is for environmental standards to be set as a national policy on the production of skim milk powder by the national authority in the exporting country.

There are now a number of analyses which demonstrate the ineffectiveness of the trade provisions of these MEAs. Julian Morris of the Institute of Economic Affairs in London has recently prepared a comprehensive analysis for the Hoover Institute. [8]

The trade ban in the CITES Treaty has not stopped the decimation of endangered species. Zimbabwe's success at managing its elephant population illustrates the point that the most effective economic instrument for wildlife management is to attribute an adequate economic value to the preservation of the species concerned. In fact Zimbabwe argued successfully at the last conference of the parties to the CITES Treaty that the trade ban in fact impeded efforts at conservation and secured a waiver from the ban to export ivory collected from culling to use the proceeds of international sale to support the conservation program.

The trade bans in the Montreal Convention have not prevented production of CFCs in parties outside the Treaty. There is no reason why they should. They also had no impact

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instruments used in one did not impede the interests of the other. In the environment systems, instruments should address the root of the environmental problems. The trade system was to support growth to enable sustainable development. Discriminatory restraints on trade were formally discouraged. Collective action to improve the environment should be through international treaties based on consensus. The fact that measures had been used which were inconsistent with the foregoing was recognized. UNCED treated these measures as exceptions or instruments of last resort. Where trade measures were used in environmental agreements, they had to satisfy rigorous criteria, in particular the principle of non-discrimination.

[8] Julian Morris, "International Environmental Agreements: developing another path" now published in Anderson, Terry L. "The Greening of US Foreign Policy" Hoover Institution, Stamford, 1998.

on the capacity of parties to the Treaty to outlaw production of CFCs since parties were required in other provisions to ban production and consumption. [9]

The Basel Convention was designed to stop illegal dumping of toxic waste in foreign, principally developing, countries. The Basel Convention is an outstanding example of the wrong solution because of the wrong diagnosis of a problem. Toxic waste was being dumped in African countries. The problem was lack of enforcement of national laws which anyway prohibited this. The Basel Treaty does nothing about improving enforcement of laws in the importing country. Instead it erects a complex set of regulations which require exporters to take responsibility for ensuring that minimum standards of environmental protection apply in the export markets when products, most only very distantly to the dumped products, are exported. Since the problem had been created by illegal actions in the first place, it is hard to see how the treaty improves the prospect in the future of preventing further illegal action.

As far as is known, the practice of international dumping of toxic waste in West Africa has stopped. Since the incidence was of dumping localised and uncommon, the attention created by the brouhaha about the issue may have been enough to stop it. There is nothing which tells us why more elaborate export controls will make any difference. The Treaty however had a number of adverse economic effects. It has stopped trade in a number of low hazard products and impeded recycling of a number of low hazard products. (None of these were the "toxic wastes" the treaty was supposed to control). It has redirected economic activity from developing to industrialized economies. Recycling of lead acid batteries and computer scrap in the Philippines has declined. Greenpeace, an historic sponsor of the Treaty, is pleased with the result because it reinforces its philosophy that every country should take responsibility for its own waste. It appears that this objective was more important than the fact that it is at the cost of the economic welfare of developing countries with no noticeable improvement in the environment.

The experience with the MEAs demonstrates clearly how unintended effects arise when mechanisms which have only an indirect effect on the activity of concern are used to try to curb that activity. In all cases measures which directly worked on production and consumption would be more effective. They show how a poorer result for the environment can result. All these agreements would be improved instruments for environmental management if the discriminatory trade provisions in them were removed.

Controlling Methods of Production

The contention that the WTO should permit restrictions on how a product is made (where those processes have an adverse effect on the environment) has arisen generally in

[9] It should be conceded however that the trade ban in the Montreal Treaty did have a political economy effect: it helped secure support for the treaty from the major producers of CFCs in North America and Europe. The Treaty mandated a phase down period during which trade was permitted. The trade ban gave a degree of protection to the market of the producers in this phase down period. However from an economic standpoint, the ban was not necessary.

reaction to rulings by the WTO that efforts by the US to restrict trade on such grounds contravene the principles of the WTO.

The UNCED principles erect a simple test for the desirability of these measures. Why were not the traditional means of collective international action used instead of imposing trade sanctions? The traditional approach is to negotiate a treaty among interested parties so that they agree to apply common measures in their domestic jurisdiction, and in the process continue to abide by the principle that national sovereignty should be respected.

In all cases where the GATT has ruled against unilateral measures by the US, the UNCED sovereignty test stands up. In the case of the tuna/dolphin disputes, a treaty was negotiated among the fishing nations of the Eastern Tropical Pacific to adopt common rules governing tuna fishing boats. Environmentalists point out that this may never have happened if the US had not exerted pressure by applying a unilateral trade ban. That may be so, but what makes that desirable if the consequence is to employ and condone coercion?

An environmentalist may consider the issue was grave enough to warrant coercion (although in the case of the tuna dolphin dispute it is hard to see why that might have been so: the dolphin were never endangered as a species in the area concerned) but this reduces the contention to a simple point: either mere impatience to see a result or political preference that environmental issues are more important than others warrant disregard of the principle of respect for national sovereignty.

It was the rejection by the WTO of the US unilateral trade measures that lead to the realization that the WTO does not recognize how a product is made. The response from environmentalists is "why not?", followed quickly with the conclusion that it should.

The basic argument about the inefficiency of use of indirect mechanisms applies in this case as well as the case of protecting discriminatory trade provisions in the MEAs. It has been tried. The Austrian Government threatened to ban imports of timber from Asian countries which did not employ what Austria regarded as sustainable forest management practices. The Austrian government backed away when two Asian Governments threatened to raise the matter in the WTO and threatened to discriminate against Austrian companies with investment approvals. Suppose Vienna had stayed the course. Why would this be effective when the most effective solution is for the governments concerned to implement national policies on management of forestry? And if the purpose of the threat was not to achieve an economic result, but rather a political result - to attempt to coerce the governments to alter their policies - is that acceptable behavior in international relations?

Impacts on the WTO

The discriminatory trade measures in the MEAs have not much diminished the effectiveness of the WTO trading system. The trade benefits they have denied are small.

However, suggestions to alter the provisions of the WTO to accommodate the trade provisions of the MEAs have very serious implications for the effectiveness of the WTO.

Environmental groups have proposed several ways for the WTO to adjust. They have nominated changes to the procedures of the WTO and changes to the provisions of the GATT. The procedural changes are transparency in WTO proceedings and creation of a direct right to participate in WTO disputes proceedings.

It is odd that environmentalists have made these procedural issues such a "cause celebre" since there is nothing about them that is inherently related to the environment. Environmentalists are not the only non-government parties who have an interest in the work of the WTO; indeed if a substantive ranking were made of which interest groups were most affected by the provisions of the WTO, two groups which would command a substantial priority ahead of environmentalists would be business and consumers. They have not found cause to complain about the WTO in the manner of the environmentalists.

The proposals to give rights to non-state parties to participate in the proceedings of the WTO, particularly its disputes procedures, overlooks a fundamental feature of how the WTO is constituted. It is unique among international organizations in that its primary purpose is the regulation of measures that governments impose. The disputes settlement monitors compliance to commitments governments make to each other to follow the rules. The WTO is accordingly the business of governments. There is no scope or logic to giving non-state parties a role in a process which tests commitments among state parties. The natural place for non-state interests to make input into developments in the WTO is in national capitals where governments develop positions. There is no community of interest which NGOs represent which is not recognized in the processes of national administrations. This applies to business and consumers as much as to environmentalists. US based environmental groups have amply demonstrated how pressure through domestic processes can be effective in having their interests taken into account. There is a case for greater transparency of the proceedings of the WTO. But this is not a very significant issue.

The proposals for substantive changes are a different matter. They are to make sustainable development a leading objective of the WTO and to amend the GATT to justify trade restrictions to protect the environment.

The case to make "sustainable development" an objective of the WTO is a political proposition, no different in principle from arguing that improvement in health or a better state of mind should a leading objective of the Organization. This might please those who want any of these issues given political prominence by signposting them wherever possible, (and there is a general environmental push to make sustainable development an objective of every international body[10]) but how is it a practicable way of advancing the

[10] In the published version of his presentation to the WTO High Level Meeting on the Environment, Klaus Topfer, Head of UNDP, said " Building Mutually Supportive Environment and Trade Policies Requires More than Just Bringing together the Right Partners. We must Integrate Sustainable Development

interest? What is there about regulating the movement of products and services across national boundaries (the core business of the WTO) that is inherently related to managing of the environment? The WTO system has succeeded because it has focussed in a technical way on one area of international economic activity, and very successfully. To load the WTO up with objectives that are unrelated to its core mission risks diminishing its capacity to deliver without any improvement in the environment.[11]

Expanding the exceptions provisions of the GATT is much bigger issue. The idea which is most commonly promoted is to expand the grounds for exceptions to the application of the basic provisions of the GATT, which are set out in Article XX, to include protection of the environment. [12] The first, general point to make is that for any agreement to work, the number of exceptions permitted to the operation of the basic provisions must be kept to a minimum. If they are not, the exception becomes the rule. This is especially important in the WTO because the agreement is designed to equip governments to fend off powerful economic forces which are defending or seeking valuable economic rents. Any new opportunity to press these cases creates fresh opportunities to weaken the basic point of the system.

Any new grounds for exception therefore needs to have the highest level of justification. It has to be necessary to promote the overall integrity of the system. There is no such case warranting creation of a new exception on environmental grounds to the GATT. Environmental groups and some governments have taken to arguing that this is the case: unless the WTO is amended to recognize environmental needs, the credibility of the WTO will be weakened. Words do not create reality. This is basically a self-serving position. The test has to be not that some groups will think less of the WTO; it has to be that a substantial interest exists, satisfaction of which requires accommodation to maintain adherence to the basic provisions of the GATT. The reality is that there is no such major environmental interest today.

Principles into macroeconomic Policy at the National and International Levels. (Capitlisation is as published)

[11] There is a related idea which was put by Sir Leon Brittan at the WTO High Level Symposium on Trade and the Environment. It is that in every negotiating group in the forthcoming trade round, the goal of securing a sustainable outcome should be set. He described this as 'mainstreaming' sustainability. This is the concept used by the WWF. It magnifies the flaw in the idea of giving the WTO a non-trade mission.

[12] The European Coummunity is the leading advocate of this. In 1996, the EC circulated a proposal to this effect in the Committee on Trade and the Environment in the WTO. The EC paper was described as a "non-paper". This is a device to float ideas which typically do not have full support inside the EC. The aim of the Commission was to seek agreement at the meeting of Ministers of the WTO in Singapore in December 1996 to the change. The idea was strongly opposed, particularly by developing countries. The EC did not press the idea at Singapore. It remains EC policy. In his presentation to the WTO High Level Symposium on Trade and Environment in Geneva in March 1999, the EC Commissioner for External Relations, Sir Leon Brittan said " a new interpretation of, or even textual amendment to, WTO rules" should be considered if necessary to give confidence that "WTO rules do accommodate the aims of parties to the MEA". In late 1996, the idea received indirect encouragement from the US. It tabled an informal paper in the WTO Committee on Trade and Environment in which it stated that the operation of the trade provisions of the MEAs should not be impeded.

The second case for amendment is that the WTO should permit trade restrictions on how a product is made. The environmentalists talk only of the environmental consequences of how something is made, but the principle which would be altered is absolutely fundamental to the functioning of the GATT.

The traditional understanding of the provisions of the GATT is that they recognize only the physical characteristics of a product, not how it is made. There is a sound economic reason for this. GATT encourages countries to use only the tariff to restrict trade. [13] The tariff links the domestic price with the price prevailing in world markets. This link becomes a principal measure of how closely the domestic market is integrated with the global market. Having created this common link for all countries, the GATT can then activate its mechanism which enables countries to exploit most efficiently their comparative advantage. The mechanism is the reduction of tariffs. If this mechanism had to take into account how a product was made as well as what it cost, its capacity to function would be fundamentally impaired.

Environmentalists might argue that the environment is so important that such a change is warranted. No doubt they would argue that the change should be restricted to just environmental issues. This is not possible. Conceding the principle that trade can be restricted according to how products are made brings much more powerful interests into the game. Union movements and industries in industrial countries have long argued that imports should be restricted because of how they are made, specifically from countries with lower wages and lower industrial standards. They want to deny developing countries one of the strongest elements of comparative advantage they have - lower labor costs. This is no exception, this is a contrary value. Opening up this principle quickly leads to propositions that undermine the central values and mechanisms of the GATT. This exception can mutate very rapidly into a contrary value.

Conventional Wisdom and Common Sense

The presumption that there is something wrong the WTO is casually accepted and treated as a conventional wisdom. This was clearly reflected in the presentation by Klaus Topfer, the Executive Director of UNEP at the WTO High Level Symposium on Trade and Environment in March 1999. He set out a strategy to "articulate clear, acceptable trade and environmental policies". Kofper laid out three steps.

The first step is to "Identify the Environmental Strengths and Weaknesses of Existing and Proposed Trade Rule", the second is "Exploit the Environmental Strengths and Benefits of Trade Liberalization" and the third is to "Articulate and Clarify the Fundamental Principles of International Environmental Policy that Must be Accommodated by the Rules of the Multilateral Trading System".

[13] The argument is more complicated when it comes to services. There the strategy is to remove barriers which regulate the activities of foreign service providers. The strategy there is to create contested markets.

It is notable that Kopfer did not address the effectiveness of environmental policies nor the impact of the rules of the MEAs.[14] No serious progress will be made in the trade and environment debate until the question of what are effective instruments for the management of the environment is considered. The "trade and environment problem" is not caused by the incapacity of the WTO to accommodate the need to take measure to manage the environment, it is caused by use of measures which are inefficient for their purpose, undesirable from the standpoint of effective management, and inconsistent with the standing conventions laid out in the United Nations charter which govern how states should manage international relations.

This is the fundamental reason the trade measures in the MEAs conflict with the provisions of the WTO. What is the sense of amending the WTO to make it consistent with such provisions? The effect would be to preserve one regime which already has a number of public policy instruments and diminish he public policy effectiveness of another.

Improving Management of the Environment

The problem is not in the WTO, it is in the MEAs. There is nothing in the WTO which impedes effective management of the environment. Its instruments give considerable latitude already to national governments to use trade measures as exceptions to the rules of the WTO to protect the national environment.

The conflict of obligations between the MEAs and the WTO is not a matter for the WTO, but for the United Nations, for UNEP and for environmental policy makers in national governments. The quality of international environmental policy making is poor. International agreements are being negotiated without adequate regard to the ultimate purpose they are supposed to serve or adequate consideration for how their provisions should work. They do not even have regard for the basic principles which should govern these principles which have been adopted in the highest organs of the United Nations.

Although the trade and environment principles at UNCED effectively delivered a rebuke to the use of discriminatory trade provisions in the MEAs, use of the same instruments is still being advocated in UNEP and proposed in international environment fora. The parties to the Basle Treaty agreed on a Protocol which proscribed trade between

[14] Tofper's lack of reference to UNCED is interesting. It is most unusual for the Head of A UN body which is subsidiary to the principal organs of the UN system, in this case the General Assembly, not to refer the most high level pronouncements on any issue, especially in such a signature session as UNCED. It is observable that developing country representatives at the WTO High Level Symposium regularly referred to the outcome of UNCED, and that international NGOs such as Greenpeace or WTO almost never refer to the trade and environment principles of UNCED in the public utterances and statements on trade and environment. UNCED was not mentioned in the WWF "Open Letter" which was circulated at the Symposium. In its statement "WTO against sustainable development" which was circulated at the Symposium, Greenpeace only referred to UNCED to ask the question "Is the WTO complying with its obligations to give consideration to environmental protection in line with the principles of sustainable development as defined in the Rio Declaration on Environment and Development"?

developing and developed parties to the Treaty itself. Very few countries have ratified it so far so its future, mercifully, may be as a dead letter.

The parties to the Biodiversity Treaty set up a negotiating conference to develop a Protocol to the Biosafety Convention. Notwithstanding the cautions issues at UNCED about use of trade instruments to protect the environment, an international instrument was proposed of which the principle purpose was to attempt to regulate trade in products containing Genetically Modified Organisms. There was no political decision by the parties to the Biodiversity Treaty that trade was a major problem. In fact parties to the Treaty had in front of them a report from experts which did not support the idea of such an international instrument. Nevertheless, a decision was taken to set up a negotiating conference. Drafts for a convention which were put on the table by groups of countries being advised by environmental groups, particularly Greenpeace, which replicated closely the provisions of the Basle Treaty. At a negotiating conference in Columbia in early 1999, negotiations were suspended because differences between the parties were so wide.

The solution to the trade and environment issue lies not in 'mainstreaming' sustainability in the WTO, but in improving the effectiveness of international public policy towards the environment. However, while nothing is done to address that problem no effective action will taken to deal with the so-called problem of trade and environment.

Chapter 9

Linkage of Environmental and Labor Standards

See Chak Mun
Permanent Representative of Singapore to the United Nations

Attempts to link environmental and labor standards to the WTO and incorporate the social clause in international trade were not new. For example, labor standards were contained in the Havana Charter[1]. They are now part of the EU and US GSP legislation. Environmental issues were first raised in the GATT in 1971[2].

As the WTO could not divorce itself from political realities and social concerns of its member states, there has been a perennial debate on what Professor Jagdish Bhagwati described as the moral obligations of trade, their objectives and whether they should be part of the WTO agenda:

(a) Are there real intellectual arguments for such linkages, e.g. question of comparative advantage? A recent OECD study has observed that the actual economic effects of two ILO core principles, viz. freedom of association and the right to collective bargaining were very small and negligible, compared to other factors such as shifts in technology, raw material prices and terms of trade.

(b) If this is part of the post-war human rights agenda such as the abolition of child labor, would it be more effectively addressed in other international forums such as the ILO and the Commission on Human Rights?

(c) Are they intended to satisfy primarily sectarian concerns arising from economic insecurity or "race to the bottom"? Or, in Professor Bhagwati's words, do they represent attempts to use "moral arguments to advance what is in fact a protectionist agenda"?

While answers to the above would be addressed by others, this paper intends to focus on the possible impact if such linkages are incorporated into the WTO. We need to address two key questions:

(a) Are trade restrictions a necessary and efficient means to redress those perceived social and economic concerns?

[1] Havana Charter (Art.17) : "The Members recognize that unfair labor conditions particularly in production for export, create difficulties in international trade and, accordingly, each Member shall take whatever action may be appropriate and feasible to eliminate such conditions within its territory."

[2] A Group on an Environmental Measures and International Trade was set up in 1971 to prepare for the 1972 Stockholm Conference on the Human Environment.

(b) How would incorporating such extraneous subject matters impact on the WTO paradigm?

Environment

There have been suggestions (eg by the EU and Norway) that the New Round should provide legal clarity and certainty to two issues: (i) multilateral environmental agreements (MEAs), and (ii) non-product-related product and process methods (PPMs). There are currently about 18 MEAs which contain trade provisions although to a varying degree. The Montreal Protocol of CFCs is a clear example. Even though no party has brought any complaint about the MEAs at WTO, the issue remains very much alive concerning the rights of non-parties to the MEAs. Various suggestions have been made to provide legal certainty i.e. compatibility with WTO provisions. The idea of a waiver has been mentioned, but it has been rejected by others as either too sweeping an approach, or too inadequate a solution in addressing environmental concerns. A more practical way may be to consider the adoption of a Protocol which would contain a list of MEAs whose trade provisions are deemed justifiable under the GATT provided they satisfy certain conditions like necessity, broad participation, degree of scientific evidence, proportionality of trade measures, etc.

The other issue relates to prevention of "eco-dumping". Eco-labeling particularly those based on life-cycle analysis and non-product related PPMs could be controversial as the GATT recognizes only like products and does not distinguish between production processes which are incorporated in such products. If it is merely a matter of consumer preference, there is nothing much that WTO could do as it is beyond the reach of its jurisprudence. The question arises only if government decides to impose such eco-labeling or trade measures in breach of WTO provisions such as non-discrimination and which are not provided for under Article XX (Exceptions).

These are not insurmountable problems, but in order to move forward, there is a need to go beyond the current set agenda of the WTO Committee on Trade and Environment and address the following issues:

(a) Under what circumstances would MEAs not be in conflict with WTO provisions?

(b) In the area of market access, can we identify

- Possible areas where further trade reforms would have environmental benefits?

- Environmental measures that may impact on trade, especially in relation to developing countries, in particular to the least developed among them?

(c) Under what circumstances could environmental concerns over-ride WTO provisions, eg relating to market access restrictions?

- To what extent could these concerns not be sufficiently addressed or accommodated under existing WTO rules and procedures, eg Articles I, III, XX of 1994 GATT?

(d) If, in the view of some delegations, WTO rules and procedures are deemed inadequate to address those concerns, what sort of changes are being envisaged, and how would they impact on the existing WTO paradigm or system?

Labor Standards

There are apparently no known cases whereby the ILO has taken trade sanctions against a member for breach of its ILO obligations. Promotion of universal ratification of the ILO conventions is done through peer pressure and the review mechanisms. Even the recent ILO declaration on core labor rights pursues a promotional and non-punitive approach in achieving compliance. Despite this promotional approach, there has been some disturbing signs of growing militancy in resorting to sanctions as a means to enforce compliance. A recent case is that of Myanmar when the June 1999 ILO conference adopted a draft resolution which would suspend some of Myanmar's rights on ground of allegations about forced village labor. This is a worrying development even if we manage to confine the issue of labor standards in the ILO.

It has been pointed out that conceptually the WTO could possibly deal with labor standards as follows[3]:

(a) Broadening WTO procedures for review of trade policies to cover labor standards,

(b) Amendments to GATT provisions,
- Article XVI: Subsidies
- Article XX: General Exceptions

(c) Invocation of WTO dispute settlement procedures for nullification and impairment of benefits under Article XXIII.

The WTO does indeed allow measures to restrict importation of products produced by prison labor, but it is a very specific exception under the GATT. Otherwise, incorporating ILO conventions on core labor standards into WTO law would carry the

[3] See background paper "Workers Rights and International Trade" by Vinod Rege, Consultant, Commonwealth Secretariat.

presumption that a lack of observance or enforcement of such conventions by WTO members would ipso facto constitute a denial of trade benefits. This is because WTO is a complaint-based system whereby a violation could arise only out of nullification or impairment of members' rights. Even if presumption is incorporated into WTO law although in very specific cases (eg in the Subsidies Agreement[4] relating to prejudice against third country on account of a member's subsidies displacing exports of another member), presumption of denial of benefits due to lax enforcement of labor rights would give rise to at least two problems:

(a) What if the member concerned has not ratified the ILO core conventions?

(b) How would one measure trade benefits being nullified? This is important because way down the WTO dispute settlement process there is the question of compensation or the right of retaliation in the event the offending party refuses to withdraw or repeal its laws or practices which are found to be inconsistent with WTO provisions. Such compensation or retaliatory actions should be proportionate to the trade benefits deemed nullified.

Conclusion

There will be mounting pressure from environmental and labor groups for the WTO to demonstrate readiness to discuss their concerns, if not incorporate them into WTO law. We can also expect strong resistance particularly from the developing countries to such attempts.

Whereas a case could be made to accommodate some environmental measures under very specific circumstances, any attempt to incorporate labor linkage into WTO would have profound impact on the existing WTO paradigm. In the final analysis, the determining factor is whether there would be any tangible benefits for WTO members taking into account the market realities.

[4] Article 6.

Chapter 10

The Freezing Effect: Will it escalate?

Pradeep S. Mehta
Secretary-General of the CUTS Centre for International Trade, Economics and Environment, Jaipur, India

Introduction

Even before the ink could dry on the texts of various agreements under the General Agreement on Tariff and Trade (GATT) 1994, or the gains or losses could be reasonably assessed, the world trading system has burdened the bewildered and incapacitated South with extraneous issues like environment and labor standards. This will reduce their market access potential substantially. Furthermore, to improve their own market access, the North is pushing new issues like investment, competition, information technology and electronic commerce.

On the other hand, many of the Southern countries are crying hoarse about the implementation problems of the existing agreements, including about the non-implementation of the "special and differential treatment" clauses which exist in several agreements to provide concessions to developing countries.

Developing countries are also being pressurized to agree to a Millenium Round of negotiations, which is being designed with the above-mentioned new issues. They are being promised a re-look at the problem areas, as part of a bargaining package.

Many in the global civil society are also opposing the new round. To counter their opposition, they are being promised that a prior sustainable development assessment of the new proposals, and that the WTO acquis will be fitted with green windows.

This paper examines the incoherence and inequity of introducing environment issues and labor standards onto the World Trade Organization (WTO) platform, and their harm to the sustainable development prospects of the developing world.

What countries knew when signing the GATT 1994?

The contracting parties to the GATT 1994/WTO, during its launch were aware that they had entered into an era, which was going to be full of 'gives' and 'takes'. The countries were also aware that they now had to be very careful before they committed themselves further on any issue, as an agreement to a particular proposal would mean a binding commitment. More so, they could be hauled up before the dispute settlement mechanism of the WTO for not honoring with their commitments.

At the time of signing of the GATT 1994 it was well known that individual agreements contained loopholes and flexibilities that could be exploited to widen their scope. Furthermore, issues like environment and labor standards were not agreed to be a part of

any future negotiating agenda, as forcing them on the developing countries would have jeopardized the fate of the GATT 1994/WTO. But enough oxygen was provided to keep these linkages alive. For example, it was agreed to study the linkages of trade and environment and a decision to set up a committee on Trade & Environment was taken with a mandate to complete its work within two years.

Countries also realized the importance of the newly minted phrase "trade-related" and knew that in future this phrase could be used to include any "unrelated" economic issue to be discussed on the multilateral trade platform.

Most importantly, they created the most powerful global regulatory body, which would seek to promote brute competition in a globalizing and liberalizing economy. The third pillar of the unfinished Bretton Woods agenda was erected with the WTO in place.

What the developing countries did not visualize?

What developing and least developed countries could not visualize was the cleverness and aggressiveness with which these loopholes could be exploited; linkages could be loaded on and new issues could be pushed for being discussed on the WTO platform, all this having a 'freezing effect' on their existing and future opportunities to improve their own share of the world trade. Even to deal with the issues at an intellectual and political level, the South does not have sufficient resources. However one has the UNCTAD with a mandate to analyze issues for developing countries and also provide negotiating assistance. Though the overall analysis and documentation made available by UNCTAD is of high quality, unfortunately developing countries are not a homogeneous lot, and each has its own specific interests as well.

They were also unable to put their act together to be able to push the developed world to comply with the provisions in the text of individual agreements addressing their development dimensions. In other words, the freezing effect only intensified due to ignorance of some of the provisions of the existing agreements, and secondly the developed world did not volunteer to comply with the provisions of special and differential treatment to developing countries.

As the developing countries inch towards preparing the Agenda for the Seattle Ministerial Conference, once again, they find that they have to respond to an agenda already defined by the developed world, which includes environment, labor standards, investment, competition policy, government procurement, tariffs and trade facilitation. More so these issues are strong deterrents for developing countries to initiate discussions on how they could push developed countries to accelerate the process of fulfilling their commitments under Agreements on Textile and Clothing, and on Agriculture.

Developing countries are also flummoxed by the ways in which developed countries are effectively mobilizing or cashing the support from their civil society to provide them with necessary and sufficient arguments, in the area of environment protection and labor

standards. These countries appear to be firing the gun of protectionism by resting it on the shoulders of civil society.

It would be interesting to see as to how the 'freezing effect' is being intensified by developed countries using arguments in the realm of environment protection and labor standards.

Trade and Environment

Trade and environment is not exactly a new issue in the GATT. For long, vocal environmentalists in developed countries have been arguing that free trade without checks will lead to further environmental degradation, as is already happening in their countries. Free traders have been arguing that increase in incomes will lead to generation of extra resources for environmental preservation in developing countries. Both these arguments are flawed, as they are too simplistic while the issues are quite complex.

At Marrakech

At Marrakech in April 1994, it was decided to set up a Committee on Trade and Environment (CTE) with the remit of examining the intricate linkages between the environment, goods, services and intellectual property:

- the relationship between the provisions of the multilateral trading system and trade measures applied for environment purposes including those pursuant to multilateral environment agreements, e.g. Basel Convention, Montreal Protocol, CITES Convention, etc.

- the relationship between the provisions of the multilateral trading system and
  1. charges and taxes for environment purposes
  2. requirements for environmental purposes relating to products, including standards and technical regulations, packaging, labeling and recycling

- the effect of environmental measures on market access, especially in relation to developing countries, in particular to the least developed countries among them, and environmental benefits of removing trade restrictions and distortions.

The CTE had a period of two years to come up with recommendations before the first ministerial review meeting which would take place after two years in December 1996. It could not complete its report, and its life mandate was extended twice.

As the proceedings of the CTE continue one finds that an issue that was perceived to be a peripheral issue, such as life-cycle analysis and product and processing methods, becoming mainstream issues on the WTO platform. More so many developed countries have also taken a position that the issue of environment is a "cross cutting one" and therefore they would support full-scale negotiations on the issue of trade and environment, so that they can prove to their citizenry that they are 'green governments'.

This is already having serious consequences on the capacity of developing countries to penetrate markets of developed countries.

What is now turning out to be a major threat is that sections of civil society in the West are drumming up a storm to cement the linkage between trade and environment so that their governments could then launch negotiations in this regard. Witness the amicus briefs presented by the WWF and other environmental NGOs, to the dispute settlement panel of the WTO while adjudicating on the "shrimp-turtle" case. More so the decision of the Appellate Body in this case upheld the right of panels to receive information from any source, which include amicus briefs. This is bound to give a rise to new types of non-tariff barriers (NTBs) that might emerge in near future. Indeed a qualitative addition to the list of refrigerants! (see Box 1)

Box 1: *Important outcomes of the Shrimp-Turtle Case*

- The term 'exhaustible natural resources' has been expanded to include creatures like turtles.
- Non-governmental organizations now have the right to present amicus briefs before dispute settlement panels.
- The preamble of the WTO is no more a guiding principle but is now given an equal weight as that given to the various agreements negotiated under the WTO.
- Environment can no more be sacrificed at the altar of free trade.

The Ministerial Meetings

On studying the political economy of negotiations vis-à-vis the issue of trade and environment, one finds that developing countries have learnt quite fast from the mistakes they had committed during the Uruguay Round talks. The most important deficiency they have come over is that they have made an effort to effectively participate in discussions going on in the CTE, unlike their stand when negotiations were carried out during the UR accords such as TRIPs. And one finds that they are enjoying the fruits of their actions.

This was evident in the reports presented by the CTE to the General Council in the two Ministerial Conferences at Singapore and Geneva, which did not reflect any significant progress in favor of developed countries. Basically the CTE could not complete the task assigned to it due to very strong participation by developing countries. At Singapore it reported *inter alia*:

- the links between trade and environment will be highlighted….which will be paid due attention by the WTO;

- differences in the environmental standards between members will not be used to promote restrictive trade practices;
- accepting the link between poverty and environmental degradation, the CTE stressed for improved market access opportunities for developing country exports, which in turn would generate the necessary resources for sustainable management of environmental resources;
- the relationship between TRIPs and Convention on Biodiversity would be clarified, as TRIPs would be the principal accord under which transfer of technology and goods would take place.

The push of rich countries of raising environmental barriers, by making effective use of standards, by incorporating concepts like 'process and production methods', and of trying to find a final solution to the compatibility issues in the area of dispute resolution of multilateral environmental agreements (MEAs) and the WTO have been frustrated by well argued positions taken by developing countries. Thus developing countries were able to diffuse the strength of proposals in the environment that could have adversely affected their market access opportunities.

Interestingly, leaders of the G-8 countries (in their meeting during June 1999) have called for environmental considerations to be "fully taken into account" in the next round of WTO trade talks. It is expected that their main thrust would be on starting some concrete discussions in the area of standards.

Given this resolve of developed countries it would be interesting to see how the draft Ministerial Declaration reflects the aspirations of these countries. More so in the context of the commitments they made in the High Level Symposium on Trade and Environment during the first quarter of 1999, to formulate "win-win-win" strategies.

High Level Symposia on Trade and Environment

The issue of trade and environment has become all the more high profile with the organization of a high level symposium on trade and environment at the behest of the EU in March 1999. EU took the lead in organizing this event as it is interested in breaking the "logjam preventing significant progress in the work of the WTO Committee on Trade and Environment." Interestingly, developing countries were also successful to couple this event with a high level symposium on trade and development. The aim was to show that while protection and preservation of the environment is necessary, the universal commitment is to do so in a manner, which is consistent with the different levels of socio-economic development, and that poverty is a major environmental degrader. Consistency or coherence is a must. One cannot, and should not, preach religion to empty stomachs.

Box 2: *Reflections on the High Level Symposia on Trade and Environment & Trade and Development*

- Emphasis laid on exploring *'win-win-win'* strategies such that environment and sustainable development do not suffer at the cost of trade liberalization.
- No details on the methodology to be adopted to operationalize such a strategy by the developed countries.
- Emphasis laid on how a new trade round resulting in more liberalization would benefit developing countries from protectionist forces in the West.
- Cursory mention about the problems of poverty, debt, etc. from developed countries
- Suggestions to launch an initiative that would increase market access for least developed countries.

The outcomes

The views expressed by experts from developed countries and the views of developed countries at these symposia show their resolve to achieve out something concrete on the issue of trade and environment during the new round. It was reiterated that a number of issues like tariff escalation, agricultural subsidies, adequate implementation of special and differential treatment, cost-effective transfer of technology *et al* have a bearing on measures needed to protect environment vis a vis trade. Hence this "crosscutting" issue involves a number of complex questions that need to be cogently addressed by developed countries before putting it on the negotiating table.

Trade and Labor Standards

This is another contentious area like the linkage between environment and trade. It is also being pushed by a Baptist-bootlegger alliance in rich countries, who also do not know about the objects of the WTO. Baptists are the NGOs, while bootleggers, the protectionist local industry (see Box 3).

How did the debate begin?

The social clause is a proposed provision in international trade agreements that would make access to world markets conditional upon the respect of the most fundamental internationally- recognized trade union rights. The proposal, introduced by the International Confederation of Free Trade Unions (ICFTU) states: "The contracting parties (of the GATT) agree to take steps to ensure the observance of the minimum labor standards specified by an advisory committee to be established by the GATT and the

International Labor Organization (ILO), and including those on freedom of association and the right to collective bargaining, on the minimum age for employment, discrimination, equal remuneration and forced labor."

Introduction of a social clause in the WTO will make it possible to curtail or stop the import (or preferential import) of products originating in countries, industries or firms where labor conditions are inferior to certain minimum standards.

Of course, this was not the first time the social clause issue was raised during the multilateral trade negotiations. From its inception, the GATT Secretariat had been receiving proposals to introduce the principle of "maintaining reasonable labor standards" in international trade negotiations.

A comprehensive proposal was mooted through the 1948 Havana Charter, which stated: "The members recognize that.…all countries have a common interest in the achievement and maintenance of fair labor standards related to productivity, and thus in the improvement of wages and working conditions as productivity may permit. The members shall take whatever action that may be appropriate and feasible to eliminate such conditions within their territory."

Box 3: *Backdoor Protectionism!*

That the western concern for labor standards in developing countries is a protectionist measure has already become evident due to several recent actions. In 1996, the US stopped the import of garments made by children below 15. Bangladesh, one of the world's poorest countries, were the first to be hit. Garment makers had to send home at least 50,000 children employed by them. The 1.5mn families that depended on this source of income from child wage earners are now on the streets.

The nation too felt the pinch, as garments account for 55% of Bangladesh's export earnings. More so the garment exports to the US contributed US$ 700 mn. to the Bangladesh exchequer during 1995. Garment makers in Bangladesh agreed to phase out child labor by 1997, but the Washington based Child Labor Coalition would have none of this. It threatened to call a boycott of Bangladesh garments in the US.

Behind the Curtain!

There are two major reasons for a push for integration of labor standards in the WTO. They are based on the premise that lower labor costs in developing countries are due to an exploitative system. First, the loss of jobs is a new and growing phenomena in the rich countries, and unprecedented. Secondly, the fear syndrome, that this will continue to

increase because firms are shifting production to developing countries due to lower labor costs.

The first is true but growing unemployment in developed countries has nothing to do with lower labor standards in developing and least developed countries. Secondly, there is no conclusive economic proof on the alleged "race to the bottom" phenomenon.

The Ministerials

The ICFTU succeeded to get its foot in the door vis-à-vis the issue of labor standards in the Singapore Ministerial Conference (1996). Interestingly, developing countries were found celebrating their pyrrhic victory as they had to been able to get a statement included in the Ministerial Declaration that mentioned that International Labor Organization (ILO) is the competent forum to deal with issues in the area of labor standards.

In spite of this agreement at Singapore, In his speech at the Geneva Ministerial (1998), the US President called for support from other countries to help the US protect the rights of labor by suitable incorporation in the WTO system. Now as we near the Seattle Ministerial Conference, we find that the US Government is once again up in arms against violators of labor rights. The US President has directed his federal agencies to list products suspected to have been made by forced child labor in order to ban the import of these products.

Interestingly, the EU has taken a stand of not supporting any proposal for the Seattle Ministerial that aims at getting labor standards into the mainstream of WTO negotiations. The outgoing EU Trade Commissioner Sir Leon Brittan said that such a clause can lead to protectionism against developing countries. Therefore the EU would push forward for increased cooperation between the International Labor Organization (ILO) and the WTO, including giving the ILO observer status at the WTO, and convening a high level meeting on trade, globalization and labor issues.

EU is therefore expected to stop short of calling for trade and labor linkage, acknowledging that no consensus on such a linkage can be reached amid strong opposition from developing countries.

Box 4: Cost of Displacing Child Labor in India

Assumptions

1. A child laborer earns Rs. 3,600 per annum by working and half of this foregone income i.e. Rs.1800 per annum needs to be provided to attract the child to come and stay in the school.
2. The cost of providing books and stationery is Rs.100 per annum per child.
3. The exchange rate is US$1 = Rs.40 (currently it is Rs.44.50).

Cost per annum

S. No.	**Particulars**	*Rs.cr.*	*$bn*	*$bn*
1.	The cost of providing, the nearly 600,000 villages in the country, with **schools** and more than one **teacher** - Mr. L. Mishra, Labor Secretary, Government of India (*The Times of India* 26.4.99)		12	
2.	NSSO estimate of 17.2mn child laborers			
(a)	Cost of books & stationery (Rs.100x17.2mn)	172	0.04	
(b)	Cost of providing incentives (Rs.1800x17.2mn)	3,096	0.77	
	Total cost [1]+[2(a)]+[2(b)]			**12.81**
3.	55mn children estimated as potential child laborers			
(a)	Cost of books & stationery (Rs.100x55mn)	550	0.14	
(b)	Cost of providing incentives (Rs.1800x55mn)	9,900	2.48	
	Total cost [1]+[3(a)]+[3(b)]			**14.62**
4.	110mn child laborers estimated by unofficial sources			
(a)	Cost of books & stationery (Rs.100x110mn)	1,100	0.28	
(b)	Cost of providing incentives (Rs.1800x110mn)	19,800	4.95	
	Total cost [1]+[4(a)]+[4(b)]			**17.23**
5.	*146mn children in the age group 6-11 years*			
(a)	*Cost of books & stationery (Rs.100x146mn)*	1,460	0.37	
(b)	*Cost of providing incentives (Rs.1800x146mn)*	26,280	6.57	
	Total cost [1]+[5(a)]+[5(b)]			**18.94**

Cost of displacing child labor

Indeed everybody is worried about child labor. But what some sections of civil society and some governments of West fail to understand (or at least pose in that fashion) is that child labor is a complex socio-economic phenomenon. Observing the current wave of interest in banning child labor a question that arises is that would banning child labor provide a solution? Besides, who will determine whether the child was forced to labor in an abusive occupation. It will not only be highly subjective, but also impinge on the sovereignty of targeted nation.

International efforts are being directed towards defining "who is a child", "what is labor", "what are the abusive forms of child labor" and so on. However, it is sad that virtually no effort is made towards understanding the causes behind this social phenomenon. One needs to ask developed countries whether they would be in a position to provide the resources to help countries like India to get rid of the problem of child labor. (see Box 4)

Conclusion

The timing, nature, and support for arguments constituting the debate on 'linkages' reflects that:

- such objections are motivated by competitiveness considerations;
- multilateral discussions on trade could be crowded by ludicrous issues that have no relation to trade;
- these protectionist arguments are going to decelerate the pace of transfer of benefits of trade liberalization to the poor in the South; and
- such arguments are going to be major irritants for developing countries to benefit from the liberalizing multilateral trade regime.

The developing countries have already pointed out that ILO is the right forum to discuss issues in the realm of labor standards. The former WTO Director General, Renato Ruggiero, has also appealed that environment issues should be discussed on a forum other than the WTO (he has toyed with the idea of a World Environment Organization) and should not be allowed to crowd out the other substantive trade agenda to be discussed at the WTO. Must we not follow this sanguine advice.

Recommendations

- The WTO should not be allowed to be used as a forum for disputes relating to trade and environment or social standards
- Environmental protection should be a top priority and wherever there are problems in international trade, these should be resolved at an independent forum
- Labor standards are equally important in all countries and good and relevant standards should be pursued through all possible means

- Poverty is a major problem in the South thus affecting both environment and social standards, and that should be addressed through cogent and genuine means
- The letter and spirit of multilateral agreements relating to the differential socio-economic development standards prevailing in the world must be respected and no attempt should be made through a one-size-fits-all approach

Chapter 11

TRIPs and the WTO: An Uneasy Marriage

Arvind Panagariya
Professor of Economics, Co-Director, Center for International Economics, University of Maryland, College Park

1. Introduction

At the Columbia University conference on the Seattle Round, Jagdish Bhagwati, Martin Khor and others raised the issue of appropriateness of the inclusion of disciplines on subjects such as intellectual property, labor standards and environmental standards into the WTO.[1] In this paper, I address this issue with respect to intellectual property rights (IPRs), questioning their inclusion into the WTO through the so-called Trade-related Intellectual Property Rights (TRIPs) Agreement.[2]

There are at least three criteria on which we can judge the appropriateness of the inclusion of a subject into the WTO. First, is the subject sufficiently closely related to trade liberalization? That is to say, does the absence of a discipline on the subject hamper market access that has been granted by a country? Second, will the inclusion of the subject improve world welfare? And third, will the inclusion improve the welfare of each WTO member? The second criterion is, of course, necessarily fulfilled if the third one is. As such, the second criterion is weaker and is not likely to be accepted by countries that stand to lose unless the beneficiaries of the discipline compensate them.

I begin in Section 2 by arguing that TRIPs is a fundamentally different animal from trade liberalization and its inclusion into the WTO cannot be justified in the manner we justify multilateral trade liberalization under the auspices of this institution. I then offer economic analysis in Section 3, which demonstrates that the TRIPs Agreement is a welfare-reducing proposition not only for developing countries but the world as a whole. The claim of many that TRIPs was good for developing countries and the world fails to survive a careful scrutiny. Finally, in Section 4, I briefly discuss the implications of TRIPs for the optimal choice of the length of IPRs for the *demandeur* countries, market structure, and technology transfer and direct foreign investment. The appendix fills some details relating to the proposition in Section 3.

2. TRIPs and Trade Liberalization are Different

Trade liberalization and "non-trade" agenda, which includes TRIPs, labor standards and environmental standards, are fundamentally different from each other. Trade liberalization

[1] See Khor, Martin, "A Comment on Attempted Linkages between Trade and Non-trade Issues in the WTO," paper presented at the conference at Columbia University on Examining the Agenda for the Seattle Round, July 22-23, 1999.
[2] The paper grew out of a seminar presentation at the WTO on July 20, 1999.

benefits everyone including the country that undertakes liberalization. When undertaken multilaterally, trade liberalization produces positive efficiency effects without significant redistributive effects. "Non-trade" agenda, by contrast, produces efficiency effects of a dubious nature and large redistributive effects that often benefit rich countries at the expense of poor countries. In the specific case of TRIPs, as already stated in the introduction, taken in isolation, it promises to lower the welfare of not just developing countries but the world as a whole. As such, it is an efficiency reducing, redistributive exercise.

Jagdish Bhagwati offers a more animated description of the difference between trade liberalization and TRIPs. As he puts it, the WTO rests on a tripod whose third leg, namely TRIPs, is shorter than the other two, GATT and GATS. And from this third leg, we are now witnessing the growth of other shorter legs in the form of labor standards and environmental standards. These legs threaten to turn the tripod into a centipede, slowing down considerably the forward movement of the WTO.

One argument that I have encountered in favor of bringing TRIPs into the WTO is that it effectively outlaws "free-riding" on the system by a subset of the WTO members. Crudely interpreted, the argument seems to say that whenever developing countries choose lower standards or weaker rules than developed countries, they are free riding the system. The implication drawn is that we not only need the rules and standards to be harmonized but need to harmonize them upwards to the levels prevailing in developed countries. There is now a large body of scholarly literature, however, that conclusively rejects this inference.[3]

In the absence of a WTO agreement such as TRIPs, each country is free to choose what it considers to be the optimal IPR regime for itself. Given different levels of economic development, costs of innovation and attitudes towards IPRs, different countries are bound to choose different levels of IP protection. Why should this outcome be viewed as free riding on the system by the countries that choose weaker IPRs? The idea presumably is that the countries that choose higher levels of IP protection generate more positive externalities than do countries with lower levels of IP protection. This results in a net free ride by developing countries on developed countries. But how do we translate this fact into an argument for harmonization unless we argue that any time countries generate different levels of externalities for one another, even while acting entirely in their self interest, a WTO agreement is required to redistribute the benefits in proportion to the volume of the externality generated? I do not think such an approach is feasible without seriously wracking the system.

The only way we can understand and explain the incorporation of IPRs into the WTO is as an exceptional event resulting from an exceptional set of circumstances, which led developing countries to exchange the TRIPs Agreement for an end to the Multi-fibre Agreement (MFA). MFA was gigantic beast, requiring a weapon of exceptional power. Now that this beast has been slain and will, hopefully, be laid to rest effective January 1,

[3] See several of the contributions in Bhagwati, J. and R. Hudec, eds., 1996, Fair Trade and Harmonization: Prerequisites for Free Trade? Vol. 1, Cambridge, MA: MIT Press.

2005, it deserves noting that the existence of TRIPs offers neither a justification nor a model for incorporating more non-trade agreements into the WTO.

In passing, I should note a point about the TRIPs-for-MFA deal that has gone entirely unnoticed. The general impression is that this was a fair deal in which the developing and developed countries benefited equally. Yet, being an exchange of *trade* concession for *non-trade* concession, the bargain was necessarily uneven. Developed countries benefited from the abolition of MFA as well as TRIPs; developing countries benefited from the abolition of MFA but were hurt by TRIPs. As most theorists will tell us, given the uneven distribution of bargaining power between developed and developing countries, this outcome should not be altogether surprising.

3. The Economics of IPRs: Why TRIPs Hurt Developing Countries

I have stated that, taken in isolation, TRIPs resulted in reduced welfare for developing countries and the world as a whole. Let me now proceed to explain why. The analysis below will be presented in the specific context of innovations and patents but can be applied more generally to IPRs.

As a public good, innovations have two key characteristics: non-rivalry in consumption and non-exclusion. Non-rivalry in consumption implies that the use of innovation by yet another individual does not reduce its availability to the existing users. Stated differently, once the innovation has been done, the marginal social cost of its use is zero. The non-exclusion property implies that once an innovation is there, we cannot prevent others from using it.[4] If innovations are costly, given this characteristic, no one wants to engage in it since the costs cannot be recovered. This is quite different from a private good, say a bottle of Coca-Cola. If I drink the contents of the bottle, they are no longer available to you. Moreover, if I possess the bottle, I can exclude you from having it without payment of an appropriate price.

These two characteristics of innovations pull the desirable policies for patents in opposite directions. Zero marginal cost of supplying the innovation, once it is there, says that we should provide it freely to whosoever wants it; patents should be short-lived. The non-exclusion property says that short-lived patents may be insufficient for innovators to recover their costs and, thus, kill the incentive to innovate. Too few innovations will take place. This property pulls towards long-lived patents. Rather than being driven by "piracy" concerns, which focus exclusively on the interests of innovators, good policy seeks a balance between these two opposing forces.

Relying heavily on the work of trade economist Alan Deardorff of the University of Michigan, in the appendix, I present a simple theory, which captures this basic tension between the two characteristics of patents.[5] The essence of the theory can be stated here,

[4] Not all innovations have the property of non-exclusion. When publicly available information about an innovation is insufficient to copy it, exclusion is possible. A lack of patents regime is not an especially contentious issue in these cases.

[5] Deardorff, Alan V. 1992. "Welfare Effects of Global Patent Protection," Economica 59, 35-51.

however. Suppose the world is divided into two regions, North and South. North is much bigger than South in economic terms and has a comparative advantage in innovations. Initially, the patents are given a life of 20 years in North and five years in South. This means that innovators are able to exercise monopoly power over the product they innovate for 20 years in North and five years in South.[6] The introduction of a TRIPs Agreement, which extends patent life in South from five to 20 years, has two main effects. First, it extends the monopoly distortion in South on all products innovated from five to 20 years. The resulting inefficiency lowers the welfare of South as well as world. In addition, the extension of the patent transfers a part of Southern consumers' income to Northern innovators through higher product prices. This redistribution further lowers the income in South and raises that in North. The loss to South is larger than to the world as a whole.

The second effect of the extension of the Northern patent regime to South is the generation of some additional innovations. Prospects of the monopoly power in South for an extra fifteen years may encourage some more products to be innovated. Benefits from these innovations counteract the loss due to increased monopoly distortion on products innovated under the old regime. But given the small size of South, extra innovations generated are likely to be few. The loss from monopoly distortion for additional fifteen years is almost guaranteed to dominate the benefit from the extra innovations. This argument is developed more systematically in the appendix.

4. Additional Hypotheses Relating to TRIPs

There are four additional points that may be made with respect to TRIPs, which I have interpreted in this paper to mean an extension of IPRs prevailing in North to the entire world.

First, since innovators are concentrated mainly in North, the changes in social welfare in North due to the implementation of TRIPs more or less coincide with the changes in the welfare of innovators. We will not find any resistance to the implementation of TRIPs in North, while innovators will aggressively lobby for it. But this is not all. Assuming the North had initially chosen the length of patent optimally, once the possibility of extending a uniform patent over the entire globe is introduced, it is likely to seek a longer patent life. The reason is that its innovators are now able to exercise their monopoly power over the Southern market. At the initial equilibrium, the extra benefit from this increase in monopoly profits will more than offset any harm the longer patent life may do to North's consumers. *Ex post*, this hypothesis appears consistent with the observed reality. I am told by my friends at the United States Food and Drug Administration that by speeding up the approval process in pharmaceuticals since the TRIPs agreement, the United States has lengthened the effective life of patent by three to five years. The demand by North for longer IPRs

[6] This is possible because only the patent holder or his authorized agents can sell the product in North during the life of the patent.

protection in the presence of TRIPs is likely to be even stronger when IPR holders themselves are politically powerful in developed countries. This is graphically illustrated by the efforts under way, at the urging of the Seattle music industry, to extend copyright protection for phonograms from 50 to 70 years.

Second, in practice, the impact of the introduction of a stronger patent regime on prices appears not to be confined to patented products. While one needs to gather more evidence, casual observation suggests that, *ceteris paribus*, even generic drugs are more expensive in countries with tougher patent regimes than in countries with weaker patent regimes. Patents seem to fundamentally alter the market structure, making them more oligopolistic. Due to hysteresis, prices of name brand patented drugs remain high even after the patent on them has expired. And the prices of generic drugs that appear on the market become linked to the prices of patent holders' name brands. If this hypothesis is correct, the losses to developing countries from TRIPs will not remain confined to patented drugs. They will also spillover to drugs on which patent has expired and to their generic counterparts.

Third, defenders of TRIPs argue that the agreement will promote technology transfer and foreign investment into developing countries. There are three problems with this argument, however. First, if technology transfer and foreign investment are, indeed, highly responsive to IPRs, developing countries could have adopted stronger IPRs on their own. The argument rests on the obvious but common fallacy that the absence of TRIPs Agreement means the absence of IPRs.[7] Second, and more importantly, there is little evidence that technology transfer and DFI are highly responsive to IPRs. In a recent study, Mansfield surveyed patent attorneys and executives of major U.S. manufacturing firms.[8] According to the data collected by him, IPRs seem to have a major impact on technology transfer primarily in pharmaceutical and chemical industries. Interestingly, these are precisely the sectors where reverse engineering is easy. In sectors such as machinery and transport where reverse engineering may be more difficult, 60% or more respondents say that they are not deterred from transferring technology to developing countries through a wholly owned subsidiary. This is consistent with the hypothesis that in these sectors, imitation is difficult and hence the IP regime irrelevant. The market structure is likely to be monopolistic with or without patent protection. There seem to be at most a limited number of sectors where imitation is difficult in the absence of local production but becomes possible in the presence of it. Third, China offers a dramatic example supporting the hypothesis of low response of DFI to IPRs. China has been one of the most flagrant violators of IP rights. Yet, FDI into that country has grown dramatically in recent years. Likewise, prior to the Special 301

[7] B.K. Zutshi, India's Ambassador and permanent representative to GATT from 1989 to 1994, reminds us that India has had a world-class legislation in copyrights, which provided protection to computer programs on a par with that of artistic and literary works in compliance with the Berne Convention, 1971. He goes on to note, "India's opposition was to norms and standards of IPRs being brought into the GATT/WTO as on a conceptual basis these were not trade related." See, Zutshi, B.F., "Bringing TRIPs into the Multilateral Trading System," in J. Bhagwati and M. Hirsch, eds., The Uruguay Round and Beyond. Essays in Honour of Arthur Dunkel (New York: Springer, 1998), p. 41.

[8] Mansfield, E., 1994, "Intellectual Property Protection, Foreign Direct Investment, and Technology Transfer," IFC Discussion Paper No. 19, Washington, D.C.: World Bank.

threat by the United States, IP protection in many East Asian countries was quite weak and yet some of them (e.g., Indonesia and Thailand) were large recipients of FDI.

Finally, I should not fail to mention that a stronger IPR regime could generate some benefits for developing countries by encouraging research in tropical diseases and plant varieties. This is a possibility, though I have not seen any concrete evidence on the extent of these benefits. Even in this area, two factors make me skeptical of the desirability of TRIPs, however. First, I grew up during the times that Green Revolution took place in India. This success was achieved not through strong IPRs but R&D subsidies and active participation of the Ford Foundation, Government of India and other local and international agencies. Researchers in the Punjab Agricultural University were deeply involved in this process as well. Second, in the case of tropical diseases, given the level of poverty, it is not clear whether TRIPs will improve or reduce poor people's access to medicines. For one thing, even if some new medicines to fight tropical diseases are innovated, the losses due to reduced access to other medicines are likely to be massive. For example, imagine that a cure is found for AIDS. Millions and millions of patients in poor countries are unlikely to be able to afford this cure due to the high prices that will prevail, thanks to the existence of patent protection for 20 years. Needless to say that the search for the cure has not been any slower in the absence of IPRs in developing countries. But even leaving aside this point, the claim of the advocates of TRIPs regarding research on tropical diseases rests on the assumption that the alternative to TRIPs is doing nothing. To be sure, countries can subsidize research in the targeted sectors. In the area of medicine, there is a long tradition, including in developed countries, of R&D subsidies. In the United States, the National Institute of Health has an extremely large budget, which is funded from the federal budget. Even developing countries have not been oblivious to this possibility. Over the years, India has supported several institutions engaged in research in tropical diseases.

Appendix

To develop the argument in Section 3 formally, let us begin with a simple but unrealistic example, which I shall make realistic shortly. Consider a single country in isolation and pretend that everyone lives for only one period. Assume that there is just one product, called widget, waiting to be innovated. Innovation is costly and resources have to be diverted from alternative uses. Once widget has been innovated, it can be produced at a constant cost per unit. Whether or not investment in the innovation takes place depends on the value of widget to the society, the cost of innovation, and the policy regime. We can sort out the outcomes under various policy regimes with the help of either Figure 1 or numerical examples to be introduced shortly. Readers unfamiliar with the economists' standard analysis of perfect competition and monopoly can jump directly to the numerical examples without risk of losing the flavor of the analysis.

In Figure 1, DD represents the demand for widget, MR the associated marginal-revenue curve, and P_C the constant unit cost of production of widget after it has been invented. P_C does not include the cost of innovation, which is fixed at R by assumption. We consider three policy regimes: an R&D subsidy that covers the cost of innovation but permits no patent protection, patent protection for the entire life of the product, and no policy at all.

In the first case, the government gives R&D subsidy to the inventor to the full extent of the cost, raising the subsidy via a lump sum tax. Recalling that once invented, widgets can be produced at a constant average and marginal cost, P_C, the equilibrium price and quantity are P_C and Q_C, respectively, in Figure 1. The consumers' surplus equals area a+b+c (the entire area under the demand curve up to P_CP_C) while the producers' surplus or profit is 0. The net benefit to the society from the invention is a+b+c-R where recall that R is the cost of invention.

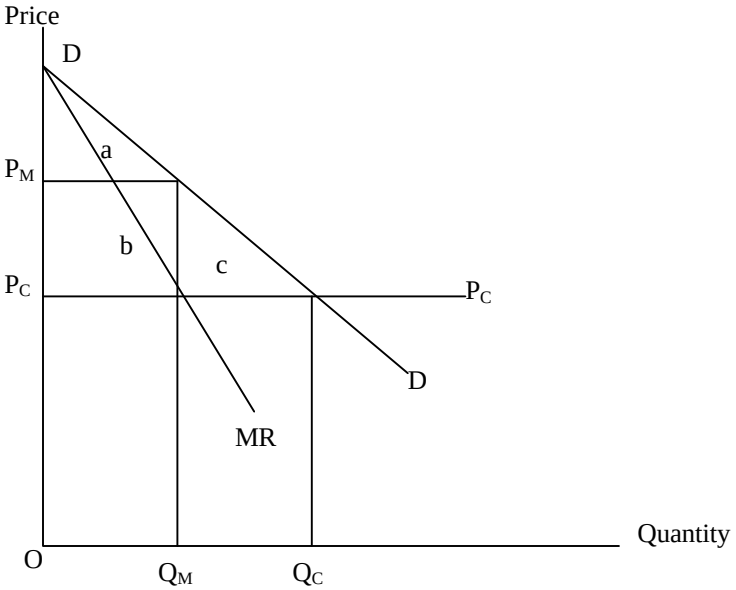

Figure 1

Next, consider the outcome under the patent. In this case, only the innovator can produce widgets. Therefore, the market for widgets comes to be characterized by monopoly. The innovator produces fewer widgets and charges a higher price than under competition. Consumers' surplus now declines to a (the triangular area under the demand curve up to price P_M), producer profits rise to b (the rectangle between price P_M and per-unit cost P_C up to quantity Q_M) and the social welfare declines to a+b-R. Area c in Figure 1 becomes a deadweight loss due to the inefficiency generated by monopoly.

Finally, if the government chooses neither to subsidize innovation nor to grant a patent, the product is not innovated at all. There is no innovation, production or consumption of widgets and net welfare gain from innovation is 0.

These same outcomes are illustrated numerically with the help of Example 1. The cost of innovation (R) is assumed to be $500. Under full R&D subsidy, the innovation is available to potential producers of widgets free of charge. Widget producers then produce and sell it competitively, leading to zero producers' surplus or profits. Benefits to consumers are $2000 (=a+b+c in Figure 1). Taking the cost of subsidy into account, net gain to the society is $1,500 (=a+b+c-R).

Under a patent regime, the innovator behaves as a monopolist in the production of widgets. He produces fewer widgets and charges a higher price. Consumer benefits decline to $500 (= a in Figure 1) while the innovator makes a profit of $1000 (= b in Figure 1) on the sales. Netting out the cost of innovation, his profits are 500. The total benefit to the society now is 1000.

Finally, suppose there is no policy of either R&D subsidy or patent. We have no production and no benefits are generated.

Two conclusions follow immediately from this example:

1. At least within the confines of this simple story, patent is not the first-best instrument. If R&D subsidies can be administered effectively, a superior outcome than under patents can be obtained.
2. It is entirely possible that, under a patent regime, a beneficial innovation will fail to materialize. For example, in Example 1, if the cost of innovation is strictly between 1000 to 2000, the innovation is still socially beneficial but patent will fail to generate it.

Example 1: One innovation, one period

Policy Regime	Production Outcome	Benefit to Consumers	Producer Profit*	Cost of Innovation	Net Gain to the Society
R&D Subsidy	Competitive Production	2,000	0	500	1,500
Patent to the Innovator	Monopoly Production	500	1000	500	1000
No Policy	No Production	0	0	0	0

*"Producer profit" refers to pure economic profits after labor, capital and other factors have been paid their competitive return.

A key limitation of Example 1 is that it is unable to distinguish between limited and unlimited patent life. To introduce this distinction, we must allow for at least two periods into the analysis. In this set up, we can think of a one-period patent as a limited patent and two-period patent as unlimited patent. Assume then that everyone lives for two periods but everything else is the same as before. We now focus on patents as the only instrument available to the government, distinguishing between two-period and one-period patent regimes. Example 2 below provides the details.

Example 2: One innovation, two periods. We extend Example 1 to two periods.

Policy Regime	Production Outcome	Benefit to Consumers	Producer Profit	Cost of Innovation	Net Gain to the Society
Two-period Patent:					
Period 1	Monopoly	500	1000	500	1000
Period 2	Monopoly	500	1000	0	1,500
One-period Patent					
Period 1	Monopoly	500	1000	500	1000
Period 2	Competition	2,000	0	0	2000

It is apparent from the numbers that a one-period patent is superior in this case. It gives the innovator sufficient incentive to generate the innovation but limits the monopoly distortion in production to one period. The two-period patent gives the innovator more

incentive than necessary to generate the innovation and leads to the monopoly distortion in both periods. We conclude:

> 3. In general, there is no compelling case for granting a patent for an indefinite period.

To add further realism to our analysis, let us introduce another product. We now have two products that can be innovated and everyone lives for two periods. One product is the same as in Example 2 while the second one is as shown in Example 3 below. I have chosen the numbers such that a one-year patent is insufficient for the second product to be innovated. But a two-year patent makes innovation possible (it is assumed that profits of 2000 in each period more than compensate the innovator for $2,500 incurred on the innovation in period 1). With these two products, what is the optimal length of the patent? A one-year patent implies second product will not be innovated but a two-year patent leads to an extension of the monopoly distortion to the second period.

Example 3: Two products, two periods. One product is as in Example 2 and the other as below.

Policy Regime	Production Outcome	Benefit to Consumers	Producer Profit	Cost of Innovation	Net Gain to the Society
Two-period Patent:					
Period 1	Monopoly	1000	2000	2500	500
Period 2	Monopoly	1000	2000	0	3000
One-period Patent					
Period 1	No production	0	0	0	0
Period 2	No production	0	0	0	0

In deciding whether or not to choose a two-period patent, we must consider the trade off between the extra innovation and the extension of the monopoly distortion in the first product to both periods. A longer patent life leads to more innovation but it also lengthens monopoly power on products that are profitable to innovate under the shorter patent life.

Our conclusion:

> 4. If a patent of uniform life across products is chosen, it should balance the gains from extra innovations generated by the extended patent life against the losses due to monopoly distortion for a longer period.

Continuing to get more realistic, allow now for many goods and many periods. It is easy to see that if we confine ourselves to a uniform patents regime, the optimal patent life is finite. Thus, starting from an arbitrary length of patent, consider the effect of an extension of the

patent life by another year. This change extends the monopoly distortion on all innovations by one year, which is harmful. But it also generates some new innovations, which is beneficial. If the initial patent life was very short, the initial stock of innovations will be small so that the benefits from new innovations will outweigh the losses from increased monopoly distortion. But as the initial patent life becomes longer and longer, the stock of innovations on which monopoly distortion is extended by another year's extension to patent life becomes bigger and bigger. Eventually, this loss will come to dominate the gain from extra innovations attributable to the extension of patent life by another year. Therefore, we will not want to extend the patent life indefinitely. We can state the conclusion:

5. If a uniform patent is chosen for all products, it should be for a finite period.

We are, at last, ready to introduce the geographical dimension to the patent issue. Suppose the world consists of two regions, North and South. Assume for the moment that these regions do not trade with each other. Given different levels of income, costs of innovation, and attitudes towards IPRs, it should be no surprise that the two regions will choose different lengths of patents. Assuming that North is richer and faces lower costs of innovation, it will choose a longer patent life than South.

Suppose next that the two regions open to trade. This change may lead the two regions to adjust the extent of patent protection but there is no reason for them to end up with identical length of the patent. We will still expect North to choose a longer patent life. For the sake of argument, suppose that North has a 20-year patent law while South has a five-year patent law, with each making these choices optimally.

Now introduce TRIPs whereby North's patent law is extended to South, making the length of the patent protection 20 years everywhere. What impact will this change have? Given the smaller economic size of South, much of the demand for new products is concentrated in North. Therefore, the extension of the patent regime to South will have at most a tiny impact on the total number of new products innovated per year. On the other hand, it will give innovators monopoly power on all newly innovated products in the Southern market. The loss from the extension of monopoly distortion from five years to 20 is almost guaranteed to dominate the gain from the small number of extra innovations. Our final conclusion is:

6. The extension of North's patent law to South will lead to both efficiency loss and transfer of benefits from Southern consumers to innovators. Since innovators are mainly located in North, South will lose on both counts: monopoly distortion and the transfer from its consumers to innovators in North. Global welfare will also decline.

It should be obvious that dividing the world into many developing and many developed countries is not going to change this basic conclusion. Depending on the degree of comparative advantage in innovation, at the margin, we may be able to find some developed countries that lose and some developing countries that benefit. But the broad conclusion that the majority of developed countries will benefit, majority of developing

countries will lose and the world as a whole will lose is likely to remain valid in this richer division of the world.

Chapter 12
Introduction to Competition Policy
Merit E. Janow
Professor in the Practice of International Trade, Columbia University

This Columbia conference on the Seattle trade summit has drawn together leading experts in all of the new issue areas, including the subject of competition policy that was introduced as part of the Singapore work program. Here, I would like to offer a few personal perspectives by way of introduction to the discussion on trade and competition policy. Competition policy, as Dr. Jenny's paper highlights, is a subject of intense deliberation in many capitals around the world. Much of the international debate surrounding competition policy has centered on what forms international cooperation should take in light of the problems that are perceived to exist. So far, the United States and the European Union are identified with rather different perspectives on whether horizontal competition rules should be part of the Seattle trade agenda. Generally speaking, there are three related but distinct approaches to the question of competition policy in a global economy that might usefully frame how we think about this subject.

First, how can nations enhance the operational effectiveness of antitrust regimes, both with respect to domestic competition problems and those problems that have international spillover effects? More than 80 countries have introduced competition laws or policies and more than half of which have done so in the last decade, so this question is not theoretical. Happily, competition laws and policies have been introduced because such measures are seen as a useful companion to economic deregulation, privatization, and the introduction of market forces. But it is also true that this proliferation of competition policy regimes is creating its own problems, for example in the area of premerger notification and review. The proliferation of international merger review regimes are subjecting a large number of transactions to notification requirements that are altogether unnecessary and or/disproportionate to any legitimate antitrust concerns. Simply determining whether merger control exists in all potentially affected jurisdictions is itself a daunting task. So too is determining whether the disparate (and often nonsensical) jurisdictional thresholds for merger notifications in these various countries are met.

The proliferation of competition regimes has also not resolved the international challenges to the sufficiency of national competition laws. Two examples may illustrate the problem: International spillover effects can arise, for example, by virtue of transnational cartels, that may require cooperation between authorities for effective prosecution. Indeed, the recent track record suggests a dramatic increase in prosecutions by the Department of Justice in transnational cartels. While not entirely clear whether transnational cartels are increasing or just U.S. detection of such anticompetitive arrangements, these cases often require (or at least benefit from) assistance from foreign authorities with respect to evidence located abroad. A second example is multijurisdictional mergers. By some estimates, approximately 50 percent of the merger matters under review at the FTC at any given time involve a foreign party, information located outside the United States or a foreign asset that is critical to the remedy. Review

of a merger by more than a dozen jurisdictions and involving multinational operations or international effects have become commonplace. U.S. officials often argues that bilateral cooperation agreements and expanded and intensive cooperation between competition authorities are the most useful way to advance the enforcement agenda in practice.

A second area of focus in the global competition policy debate has centered on the future role of the World Trade Organization. Is the WTO well suited to serve as the forum for the negotiation of a set of rules on competition (i.e., horizontal commitments), which would then be subject to WTO dispute settlement rules? The European Union is a forceful advocate for the view that the time is ripe for the negotiation of competition rules at the WTO. It has suggested that early efforts at negotiation oblige countries to have competition laws, enforce them in a transparent and non-discriminatory fashion, provide for international cooperation, and over time consider efforts at broader substantive coverage. The EU proposal suggests that these rules should be subject to dispute settlement, but that individual cases would not be examined, but rather "patterns" of cases. So far, the EU proposal has received some public support from Canada, Japan and Australia.

I personally do not think that there is sufficient consensus around the world--and certainly insufficient consensus within the United States--to support the negotiation of horizontal competition rules. In the United States, for example, the International Competition Policy Advisory Committee (ICPAC) held hearings in the fall of 1998 and in the spring of 1999 on this and other competition policy questions. None of the U.S. business groups that testified before ICPAC argued in favor of horizontal competition rules at the WTO.

I think we should also consider more deeply the consequences of *requiring* countries to have competition laws through an affirmative obligation in the WTO. It is more important that countries take steps to promote competition in their markets. If countries chose to do so through the introduction of competition laws and polices then certain features of those policies such as transparency and due process are matters that can be reinforced at the WTO, among other places. Such reinforcement might be very usefully undertaken at the WTO. Requiring that countries have competition laws may run the risk that further distortions are introduced into economies in the name of competition policy.

For these reasons and others, this is an opportune time for governments to consider some incremental steps that could now be taken at the WTO. Those steps should be aimed at enhance our understanding of the interface of trade and competition problems and finding specific areas for action that are mutually reinforcing of both trade and competition policy objectives. The WTO rules already contain some provisions of relevance to competition policy and this may point the way for some additional steps in the future. For example, the Basic Telecommunications Reference Paper and the Accounting Disciplines, among others, offer some interesting architectural ways of introducing competition policy safeguards into sectoral liberalization initiatives. As other sectors with comparable features (i.e., state enterprises, high degree of government regulation,

network features) become the subject of negotiations, competition safeguards should also be considered. The GATS framework may be particularly relevant in this context. Other modest but useful steps could include: continuation of the working group on trade and competition problems; including a "competition policy review" within the context of country reviews undertaken as part of a TPRM examination; expanding discussions, seminars, and other initiatives between the WTO and other international bodies such as the OECD, UNCTAD, and the World Bank in consideration of competition policy matters. These type of incremental measures may serve to educate us all on the linkage between trade and competition policies and ensure that measures taken by governments are consistent with core WTO objectives of transparency and non-discrimination.

From the point of view of the credibility of the WTO, it is important that any new rules negotiated in that fora prove judiciable and robust--general undertakings of the sort that are currently being proposed and debated may not be up to that challenge. The disputes that are now creating international friction on trade and competition tend to center on subtle questions of failure to enforce laws and rule of reason-centered disputes rather than facially discriminatory enforcement practices. Thus, I am not confident that rules that required countries to have competition laws and enforcement them would prove terribly responsive to the sources of international tension surrounding market access.

Since more competition problems are international in nature but not all competition problems are trade problems, this suggests the need for a possible third approach. It may also be timely to consider whether a new fora is needed to bring together competition officials from around the world to address a full range of issues confronting competition policy in the global economy. This perspective is advanced in Professor Fox's paper, but let me also put my own suggestions into our discussion. The obvious first question is: why do we need a new fora? Aren't existing fora sufficient? The OECD has served as an important fora for deliberation between and among its members on competition matters broadly and has recently achieved an important recommendation with respect to cooperation vis-a-vis hard core cartels. Important analytical studies have been undertaken at the OECD for many years. The OECD has also sponsored a great deal of technical assistance over the years to new competition regimes. Yet, the OECD does not routinely include all jurisdictions that have competition laws into their deliberations.

The WTO, for its part, is mostly focused on trade/competition interface issues and is not focusing on enhancing competition laws and policies, developing consensus on "best practices" in merger review, cartel enforcement or other such traditional competition policy matters. Bilateral cooperation is proving useful between a number of jurisdictions on practical and real enforcement matters. Bilateral cooperation arrangements are deepening and becoming more numerous, but are unlikely to cover all affected jurisdictions. Thus, while there is much that can be undertaken unilaterally and bilaterally it is also true that not all competition policy matters are likely to be fully resolved through existing channels.

Existing organizations such as the World Bank, WTO and OECD and their member governments collaborate with each other to establish an inclusive forum for discussion of

procedural and substantive elements of "best practices" in competition policy. This suggestion is not to attempt formal harmonization of either substantive law or procedural practices but rather to develop more coherence to policies around the world, informed where possible, by shared views on ways that private, hybrid and governmental anticompetitive or exclusionary practices can adversely affect national economic well being and international trade. And, for those nations that have chosen to introduce competition policy regimes, an expanded international dialogue could be useful to support institution building, the development of rule of law based systems and possibly even arbitration of disputes.

The agenda for such an effort should include traditional competition issues as well as trade and competition issues. Officials from transition environments often remark that international agreements or consultations can be extremely important to "lock-in" a reform agenda or secure added legitimacy for market-based reforms that face domestic opposition. At present, there is an expanding array of bilateral cooperation agreements that are serving some of this purpose as well as consultations occurring under APEC, Mercosur, and the WTO Trade and Competition Policy Working Group. Yet, each of these are limited by scope, mandate or membership. Further, there is currently a hodge podge of technical assistance programs offered by some international organizations and bilateral assistance agencies to support capacity building in competition law and policy.

This suggestion, which is consistent with that being proposed by Professor Fox but advances less of a role for the WTO, supports the creation of an inclusive, open new fora that develops consensus where possible, maintains information regarding existing technical assistance programs, hold seminars, and provides opportunities for discussion among competition officials and coordination, where possible. Broad international discourse on competition law and policy, if useful, is not intended to substitute for work underway in the WTO or in the OECD or elsewhere, but rather is intended to support it and the development of sound competition policy around the globe.

Chapter 13

Global Competition Policy as a Basis for a Borderless Market Economy

Hisamitsu ARAI
Vice-Minister for International Affairs, MITI, Japan

Introduction

Thank you, Professor Janow, for the generous introduction. It is an honor to attend this conference which has attracted many leading figures from a variety of fields. This conference on the WTO is a timely one given the growing importance of the role of the WTO should play is getting more and more important in the rapidly changing world economy, with the 21st century just around the corner. The Japanese government is now deciding its formal position in the next round of the WTO. Today I want to express my opinion not as the representative of the Japanese government but as an individual who has some expertise in international trade and competition policy.

World Economic Environment Toward the 21st Century

1. Current world economy and competition policy

Increasing globalization will make it even more important to introduce competition laws worldwide.

With the increasing globalization of world economic activities and ever greater capital mobility, we have entered an era in which companies choose among countries in search of the optimum business environment. The creation of an attractive domestic business environment has therefore become a crucial task, with more and more countries using tools such as deregulation to develop free and open competitive markets. Developing domestic competition laws is extremely important in order to ensure fair competition in such markets.

Internationally too, with corporate activities having an impact not only on their home countries but also further abroad, there is a growing call for worldwide introduction of competition laws as a means of facilitating trade and optimizing resource allocation, and efforts have been launched on both bilateral and multilateral levels. This trend is likely to accelerate geometrically in the 21st century as globalization advances.

2. Borders will Gradually Disappear in the 21st Century World Economy

Gradual disappearance of border will increase the importance of the worldwide development of competition policy.

In the 21st century, the advance of information technology and the further evolution of globalization will see the emergence of a world economic environment of a new and different nature. The bulk of added value will be intellectual added value, and networks will carry this smoothly across borders in the form of digitized information. It will

become enormously difficult for countries to accurately gauge and control the cross-border movement of this added value, with the result that the concept of borders, which had such an important meaning in the 20th century, and over which countries struggled so fiercely, will gradually disappear. Consequently, the 21st century will witness the full and entire globalization of economic activities. Markets will become increasingly integrated, ultimately leading to the formation of a single world-scale market. The rules needed primarily for the development of the domestic business environment in the 20th century, therefore, will need to be developed on a global scale in the 21st century toward the facilitation of trade. Arrangements such as the TRIPs Agreement, which stipulates rules in the intellectual property rights area beyond border measures, can in this sense be said to be the vanguard of these global-scale rules. Such trends will make the worldwide development of competition policy increasingly important.

3. Road to the WEO (World Economic Organization)

The WTO will expand its coverage and develop into the WEO in the 21st century.

The development of rules for the world economy as it evolves toward a single market in the 21st century will require active efforts within the framework of the WTO, which has a track record of multilateral rule development. For the greater part of its half-century of history, the GATT system, precursor of today's WTO, provided rules for trade in the narrow sense of exports and imports. What brought about a historical transformation in this role was the Uruguay Round. Through the Uruguay Round negotiations, services, intellectual property rights and other areas beyond border measures were brought under the wings of the GATT, effecting a transition to the WTO system. In that sense, the "T" in the WTO's title which stands for “trade” has come to mean not trade in the narrow sense of imports and exports but transactions as a whole and on a global scale. I believe that the WTO will expand its coverage still further, developing in the 21st century into a World Economic Organization, a WEO.

4. Civil society seeks the development of competition law for consumer protection

The advance of globalization in the 21st century will not be limited to economic areas. The increasingly widespread use of information technology will boost awareness of the views of individuals, furthering an international direct democracy. This will foster a global awareness of the wish for consumer protection and the importance of such universal values as the environment, human rights, culture and religion, which cannot be derived from the pursuit of economic rationalism. In this sense, we are witnessing the emergence of "citizens of the world" in the true sense of the word, to whose wishes countries will need to respond in good faith. The development of competition laws in particular can be cited as one important economic system for consumer protection, and from which perspective too pushing forward with the development of competition laws around the world will become a task of some urgency.

The WTO and Competition Policy

Whether or not to include trade and competition policy as an agenda item in the upcoming round of WTO negotiations is a key issue. Japan takes the position that the upcoming negotiations should not be limited to the theme of market access, but should also include areas contributing to the creation of basic rules for the world economy in the 21st century.

More specifically, Japan believes that the upcoming negotiations should be comprehensive, including not only the so-called "built-in agenda" of agriculture and services, but also tariffs on manufactured goods and the creation of investment rules. We have already proposed a wide range of agenda items in addition to tariffs and investment, such as anti-dumping, TRIPs, technical barriers to trade, electronic commerce, trade facilitation and regional trade agreements. In terms of negotiating modalities, we think the negotiations should be a single undertaking, aiming at reaching an agreement within around three years. This would allow the benefits of liberalization to be extended to all members and meet their diverse interests, resulting in the most effective expansion of global trade and investment flows. It would also lead to the formation of a new international economic order toward the 21st century.

In regard to trade and competition, the Japanese government is undertaking considerations toward submission of a proposal by the end of July as part of the WTO General Council preparatory process, but no formal decision has yet been made. As I mentioned at the beginning, my comments on whether or not to include competition policy in the WTO are my views as an individual, and thus do not represent the Japanese government.

1. Need for International Efforts

The introduction of competition policy is becoming increasingly important not only in Japan but also on the world level.

The issue here, I believe, is how to take forward the development of basic rules on a world level in response to the globalization of the world economy.

The globalization of the world economy is turning the worldwide introduction of competition policy into a critical task. Recently, Japan too has been advancing wide-ranging reforms as a priority task. Firstly, we have been introducing competition policy widely into the various domestic regulatory systems. We have also been strengthening competition laws. More specifically, as of June this year we abolished the system of exemptions to the Anti-Monopoly Law, such as recession cartels and rationalization cartels. Guidelines have been created and announced to increase the operational transparency of this law. Moreover, in addition to strengthening the Fair Trade Commission's system of enforcement, considerations are also underway toward enhancing systemic aspects such as the introduction of private claims.

With the 21st century world economy becoming increasingly global, the introduction of competition policy should also be widely advanced on a world level. This is necessary for the following reasons. Firstly, the globalization of the world economy and the reduction of border-level trade barriers are boosting the importance of domestic crackdowns on anti-competitive behavior. Secondly, securing competitive conditions in the host country of investment has become more important as companies expand their international investment and develop their business activities offshore. Thirdly, competition policy is also becoming vital for the countries absorbing this investment as they open their markets to multinational companies.

Obviously, in terms of the concerns of competition authorities themselves, with individual cases of anti-competitive behavior becoming more international and the number of international mergers increasing, international cooperation is becoming important in terms of appropriately addressing these issues.

2. Matching the pace of international efforts on competition policy to economic activities

International efforts on trade and investment have been solid, while those of competition policy have been limited.

Multilateral efforts on trade now have a long track record stretching as far back as the GATT, while international efforts on investment have also been making rapid progress in recent years, including the conclusion of more than 1,300 bilateral investment agreements. By comparison, international efforts on competition policy appear to have been rather limited. The OECD has been working on this area for some time now, establishing cooperation among its members and voluntary guidelines. On the other hand, these measures provide no strict legal biding of OECD members in a strict manner. Only a handful of developed countries, with the United States and the EU at the forefront, have concluded bilateral agreements on competition policy. At present, most developing countries at the very least remain outside international legal frameworks.

Here I would like to touch upon the Agreement between Japan and the United States concerning Cooperation on Anti-Competitive Activities. At the Japan-U.S. Business Conference held last week, a businessman from the U.S. commented to the effect that while Japanese and U.S. anti-monopoly law was very similar in many respects, there were major disparities in terms of enforcement. For example, where the United States stresses market freedom, Japan's Anti-Monopoly Law aims at social stability. He felt that the aforementioned agreement between Japan and the United States agreed in May would lead toward a market more firmly based on the principle of competition. This was a surprising remark in that he appeared to have the mistaken impression that Japan's Anti-Monopoly Law is not applied as strictly as it should be to anti-competitive behavior.

As is evident in a comparison with Europe and the United States, a country's competition policy is closely related to its social market environment, and reflects differences in market environments. Japan's Anti-Monopoly Law is applied to the letter by the Fair

Trade Commission, which cracks down severely on anti-competitive behavior, and in this sense, the basic philosophy is no different from the U.S. Anti-Trust Law. It would be erroneous to expect a qualitative change in enforcement of the Anti-Monopoly Law as a result of the Agreement between Japan and the United States concerning Cooperation on Anti-Competitive Activities. Of course, the building of cooperative relations by the Japanese competition policy authorities in forms such as this Agreement between Japan and the United States is an important supplement to multilateral efforts, and we hope that these will lead to strengthening the productive relationship between both countries.

3. Competition rules are needed in the WTO

The WTO has already introduced a number of rules related to competition policy and crosscutting WTO effort on competition policy would have the following merits:

- *The introduction of competition policy can be addressed from the same standpoint as the development of trade rules.*
- *The introduction of rules can be advanced in a wide range of countries.*
- *Working within the WTO would allow the integrated development of trade policy and competition policy.*
- *By taking multilateral approach, legal and technical instruments could be used to handle disputes between countries over competition policy.*

I would next like to look at whether the WTO is an appropriate platform for the introduction of competition rules.

As you know, the WTO has already introduced a number of rules on competition policy, primary examples of which are the GATS provisions on monopoly and exclusive service providers (Article 8) and on commercial practices (Article 9), as well as the provisions on competition safeguards in the Reference Paper in the area of basic telecommunications. To regard the WTO as an organization unrelated to competition policy and to view the issue as a question of whether it would be appropriate for the WTO to handle competition policy as a new area would therefore be inaccurate. The trade policies handled by the WTO are closely related to competition policy in the sense that they aim at expanding economic welfare through competition; moreover, the WTO is already handling competition policy. The real question is therefore the timing and degree to which this treatment should be broadened and deepened.

Cross-cutting WTO efforts on competition law would have the following merits.

1. Firstly, the introduction of competition policy can be addressed from the same standpoint as the development of trade rules in the sense of breaking down trade barriers. Introduction of competition policy in the WTO would be useful in the sense of preventing the trade liberalization and international corporate expansion achieved as a result of WTO trade negotiations from being obstructed by anti-competitive behavior. Because discussion can be consistently rooted in a trade expansion perspective, strong momentum can be maintained toward the introduction of competition policy.

2. Next, the introduction of rules can be advanced in a wide range of countries, developing countries included, from a medium- to long-term perspective. As was evident in the economic crisis triggered by the 1997 Asian currency crisis, the world economy, including Asia, Latin America and other developing countries, is in the process of integration, and the WTO would permit discussion in a form which embraces such countries.
3. Thirdly, working within the WTO would allow the integrated development of trade policy and competition policy. Where tariffs are removed on certain products and the manufacturing and distribution of these are exempted from competition law, anti-competitive corporate behavior could cancel out the effects of tariff elimination. Both policies are closely related, and international efforts in regard to these should be integrated to the greatest extent possible.
4. Finally, the WTO has worked to avoid bilateral trade friction and apply legal and technical instruments to the greatest extent possible in handling disputes between countries over trade issues, and the organization has a fine track record in this regard. By using the WTO, this kind of multilateral approach could also be taken to competition policy.

4. Points for consideration

Several points such as follows should be considered in handling competition policy in the WTO.

- *The nature of the enforcement of individual cases under competition law, which is the complex establishment of fact based on massive amount of evidence, should be considered although the WTO has so far managed to deal with similar problem.*
- *The rules should be created which is adapted to the different stages of development and competition policy experience of the various countries.*
- *WTO efforts should not be considered as the be-all and end-all international efforts on competition policy. And, in this regard, the existence of bilateral agreements naturally does not annul the need for multilateral approach.*

However, there are several points where careful consideration would be needed in handling competition policy within the WTO framework.

1. Firstly, the enforcement of individual cases under competition law is characterized by, for example, the complex establishment of fact based on a massive amount of evidence, and the WTO dispute settlement mechanism does not have adequate experience in handling such cases. However, even under the existing WTO rules, a similar problem could arise in the case of a dispute relating to the application of concrete laws. For example, the same problem would occur if a WTO panel under the TRIPs had to re-examine the decisions on patent applications made by patent inspectors. In spite of this, the WTO dispute settlement procedures have so far managed to deal with disputes under the WTO rules. Of course, given the special nature of competition law, it would be necessary to give some consideration to this issue.

2. Secondly, because the WTO includes many developing countries, rules would need to be created which is adapted to the different stages of development and competition policy experience of the various countries. A variety of measures would be possible in this regard, including the establishment of a moratorium for application of some rules according to the stage of development of the developing country in question; the extension of differential treatment in regard to exemption measures; and the provision of adequate support. The various existing WTO agreements contain a number of special provisions which consider the conditions in developing countries. For example, the TRIPs Agreement has an 11-year moratorium for least-developed countries, while the Agreement on Subsidies and Countervailing Duties in principle allows least-developed countries exemption from application of the ban on export subsidies for an indefinite period. Lessons could be drawn from this experience in regard to rules on competition law.
3. Thirdly, WTO efforts should not be considered as the be-all and end-all of international efforts on competition policy. For example, the OECD is working on banning hard-core cartels, and according to the situation, there may also be cases where bilateral agreements provide valuable tools. Efforts should be advanced toward strengthening competition policy in a variety of fora, taking advantage of the particular characteristics of each.
4. Finally, in this regard, it should be noted that the existence of bilateral agreements naturally does not annul the need for multilateral competition rules. Efforts on a strictly bilateral level would exclude most developing countries, while the conclusion of an enormous number of bilateral agreements is also not particularly efficient. It is necessary, therefore, to establish a multilateral review in the WTO as a basic framework while continuing to work on bilateral agreements as necessary.

5. A possible framework for WTO rules on competition

The framework for WTO rules on competition should include the following elements:

- *WTO rules should address anti-competitive behavior which affects trade.*
- *Principles widely and generally accepted in the WTO such as transparency and non-discrimination should be introduced into the rules.*
- *The rules must require countries to develop basic domestic competition laws and enforcement mechanisms.*
- *The rules should incorporate provisions on international cooperation such as information exchange.*
- *Due consideration for the various countries which is in different stages of economic development and competition policy experience.*

Next, I would like to discuss a basic framework from which specific rules could be developed in the case that competition rules were established in the WTO. Japan's proposal in regard to the upcoming WTO negotiations is still under internal coordination, but speaking from a strictly personal point of view, I think the framework within the WTO should include the following elements.

Firstly, WTO rules should address anti-competitive behavior which affects trade. There are obviously a variety of anti-competitive behavior issues in terms of competition policy, but given the WTO's trade expertise, it will be important to adopt this trade effect perspective. While in-depth consideration needs to be given to which specific forms of anti-competitive behavior to address, the bottom line should be to address those actions which affect trade.

Secondly, if efforts are to be made within the WTO framework, principles widely and generally accepted in the WTO should be introduced into these rules. More specifically, the principles of transparency and non-discrimination are incorporated in the various WTO rules as concrete provisions, and these approaches also need to be reflected in considering rules on competition law.

Thirdly, rules on competition law must require countries to develop basic domestic competition laws and enforcement mechanisms. In countries' efforts to introduce competition law, advantage should basically be taken of the merits of the WTO's wide-ranging membership, which also embraces developing countries. From this perspective, rather than seeking WTO efforts in front-running areas of competition policy, it would be more appropriate to take a progressive approach, starting from the development of basic competition law and enforcement mechanisms. Certainly, due consideration should be given to the different development stages of developing countries in this regard, benefiting from the WTO’s extensive experience in other rule areas.

Fourthly, given the increasing internationalization of corporate activities, provisions on international cooperation such as information exchange should be incorporated in rules on competition law. In this context, consideration must also be given to opening the way for the development of rules of some nature toward avoiding friction arising from the international enforcement of an individual country's competition laws.

Finally, in developing these rules, due consideration must be given to the stage of economic development of the various member countries and the degree to which competition policies have been introduced. WTO members stand at various levels, with some having no competition laws at all while others have long experience in enforcing such laws. The specific content of rules on competition law in this regard needs to be developed with reference to other agreements in the WTO.

6. Concerns of competition experts regarding the linkage between competition and trade

There are some concerns regarding and the ability to create the rule within the WTO and the enforceability of the WTO rule on competition policy, but I believe they can be overcome.

1. There is some concern that rule violation such as the failure to create WTO-consistent rules might lead to the imposition of trade sanction measures if competition rules are established in the WTO. However, the current WTO rules provide that compensation measures should first be considered in the sector where the violation occurred. For

example, compensation measures for the violation of GATS rules should primarily be enforced in the service sector, and not in the goods sector. The current rules ensure their effectiveness while avoiding trade restraint measures as much as possible by allowing compensation measures in a different sector only when measures in the same sector are not possible or effective. Future consideration of compensation measures is needed under WTO competition rules, taking into account these current rules.

2. Given the need for expertise in competition law in formulating multilateral competition rules, the question has been raised as to whether the WTO, a forum for trade experts, is capable of creating appropriate competition rules. However, while the WTO provides a forum, competition experts can represent their countries in the WTO and play a principal role in competition rule-making. This will allow the establishment of the right kind of rules in the WTO by benefiting from the expertise acquired through various international efforts in the field of competition law.

7. Adverse effects of trade remedies on competition

Some trade remedies, particularly anti-dumping measures, are essentially based on the same idea as the concept of predatory pricing under competition law. While deepening discussion on competition policy, the approach developed under competition law needs to be gradually introduced in regard to trade remedies as well, in order to reduce the protectionist effect of current trade remedies

I would next like to touch on the issue of trade remedies. In dealing with competition policy, it will not be enough to simply discuss the introduction of international rules on competition law. Discussion will also be needed on the anti-competitive effects of trade remedies.

Anti-dumping measures are a particular problem in this regard. While they are essentially based on the same idea as the concept of predatory pricing under competition law, anti-dumping measures are being initiated on the basis of different requisites in regard to completely different forms of economic behavior.

Even in competition policy, selling goods at extremely low prices which undercut cost in order to exclude competitors might be considered anti-competitive and a violation of competition law. However, it is not always easy to distinguish between such low-price sales and ordinary price competition behavior, and over-regulation in this regard ends up restricting competition. Competition law is therefore applied on the basis of stringent conditions for example, where prices are extremely low, undercutting variable costs, and where the exclusion of competitors would probably result in monopoly and monopoly profit.

However, no such conditions are applied to anti-dumping measures, and these can be initiated, for example, even in cases where export prices have fallen in line with lower market prices resulting from an economic slump. The initiation of anti-dumping measures effectively forces foreign companies out of the market, and as anti-dumping measures are frequently applied when there are a limited number of domestic suppliers, such measures

have a substantial effect in terms of restricting competition. It should also be noted that the mere submission of a claim and the launching of investigations for anti-dumping measures have an enormous effect in terms of restricting exports. And, in most cases, anti-dumping measures are being applied to behavior entirely unrelated to what competition law refers to as predatory pricing.

In fact, it is well known that during the 1980s, there were a number of instances in the United States where the competition authorities questioned the initiation of anti-dumping measures by the anti-dumping authorities from the perspective of competition policy. While this has not occurred in recent years, it is at least obvious that this does not indicate that anti-dumping measures have become any less anti-competitive.

While deepening discussion on competition policy, the approach developed under competition law needs to be gradually introduced in regard to trade remedies as well, in order to reduce the protectionist effect of current trade remedies.

Further, in terms of the link with competition policy, it is often claimed these days that anti-dumping measures are being taken to combat anti-competitive behavior in exporting countries. However, not only is there the question of whether unilateral measures such as anti-dumping measures are appropriate in addressing this issue, but, moreover, the existence of such anti-competitive behavior in other countries is not a requisite in launching anti-dumping measures. In fact, there is an extremely strong risk that anti-dumping measures are no more than a protectionist device.

8. Experience in the Intellectual Property Rights Area

As the establishment of TRIPs stimulated WIPO activities and galvanized the discussion in the area of intellectual property rights, WTO efforts on competition rules are expected to complement work on competition policy in other fora such as the OECD, with the various different fora stimulating one another and furthering discussion on competition policy.

The establishment of the WTO in place of the GATT as a result of the Uruguay Round and the formulation of the TRIPs Agreement had an enormous impact on international rule-making efforts in regard to intellectual property rights. While providing rules for trade-related measures, the TRIPs Agreement in effect promotes the development of domestic rules on intellectual property rights and the enforcement of these, and I would like to say a few words based on that experience.

The establishment of the TRIPs Agreement, for example, resulted in the growing international awareness in the WIPO of the need to strengthen the protection of intellectual property. This accelerated the work on amendment of the Berne Convention for the Protection of Literary and Artistic Works, untouched since 1971, and 1996 saw the formulation of the WIPO Copyright Treaty and the WIPO Performance and Phonograms Treaty. As seen in these examples, the formulation of the TRIPs Agreement stimulated WIPO activities, leading to major progress in international efforts toward the protection of intellectual property. The two-way relationship between the TRIPs and the

WIPO has provided great mutual stimulation, working very effectively in galvanizing discussion.

As in the case of intellectual property, WTO efforts on competition rules are expected to complement work on competition policy in other fora such as the OECD, with the various different fora stimulating one another and furthering discussion on competition policy.

Chapter 14
Should Competition Join the WTO?
Eleanor M. Fox
Walter J. Derenberg Professor of Trade Regulation at New York University School of Law

I. Should competition policy be included in the WTO?

Competition policy issues of world dimension are emerging in the wake of globalization and liberalization. A discrete set of these issues lies at the intersection of trade law and competition law. There is a strong case for bringing these issues under the WTO roof.

This paper will, first, treat this intersection. Second, it will suggest an appropriate forum for the generality of the new world competition issues.

Competition policy is the policy that helps make markets work, free from artificial private and other commercial restraints. Trade policy helps make markets work free from artificial government restraints. Thus, the two policies are symbiotic. Preservation of competition in international markets enhances the efficient functioning of the world trading system, and contrariwise, the obstruction of competition in international markets undermines the world trading system. These observations may lead us to reverse the question and ask: Why should competition policy be fenced out of the WTO?

II. The negative case

A. Introduction

Two sets of arguments have been formulated in support of the proposition that no competition issues belong on the WTO agenda. One set applies without reference to trade law. It postulates: There is no need to internationalize competition law, and there are high costs of doing so. The second set applies with particular regard to trade law and the WTO. It postulates: Competition and trade policies are separate and normally hostile disciplines; trade concepts, which are producer-driven, will degrade competition concepts, which are consumer and market driven; the "house" of the WTO is inadequate to bear the weight of a competition competence; and the WTO — with its dispute resolution system — is inappropriate for solution of world competition problems.

B. The case of no need to internationalize

If there is a case of no need to internationalize competition law, the case is probably strongest from the view point of the United States. The argument is: Although many

markets and anticompetitive acts transcend national borders, U.S. law and processes, and U.S. cooperation with its trading partners, are almost always adequate to deal with those that might adversely impact the United States.

U.S. antitrust law has a greater extraterritorial reach than any other competition law. Not only does U.S. antitrust law extend to foreign actors that harm U.S. consumers, but also (it is claimed) U.S. antitrust law prohibits foreign agreements and acts on foreign soil that raise significant hurdles to U.S. exporters trying to sell into foreign markets, if those agreements or acts are anticompetitive.

Moreover, a large proportion of foreign actors capable of impacting U.S. competition or export trade do business in the United States and have assets here, so that as a practical matter the United States can obtain the necessary personal jurisdiction and can obtain enforcement. Further, the United States has the opportunity and power to conclude bilateral agreements with trading partners of its choice.

While seeing few or no benefits, U.S. enforcers fear high costs of international initiatives. U.S. antitrust law is seen as sound or even "correct," based as it is on an allocative efficiency, consumer welfare principle. Supporters of U.S. antitrust law often assert that more interventionist law is inefficient. The competition law of most other nations *is* more interventionist. Therefore, it is argued, if U.S. officials were to sit at a bargaining table to reach an agreement on international antitrust, they would almost inevitably be forced to give up the purity and correctness of U.S. law.

Moreover, internationalization would almost inevitably lead to bureaucracy far from the pulse of the people (it is said); and it would require dispute resolution, which would be entrusted to decision-makers who cannot be trusted to reach dispassionate, correct, efficiency-based decisions.

C. The case against mixing competition, trade and the WTO

The problems multiply when it is suggested that internationalization of competition law should take place within the WTO.

First, it is argued, trade law protects competitors; competition law protects consumers; the marriage is likely to turn competition law into a producer-protecting instrument. This is likely to occur both nationally and internationally. Nationally, the U.S. antitrust agencies will be forced to cede control to the U.S. Trade Representative (whose heart is with U.S. producers and whose expertise is in trade policy). Internationally, trade experts will be entrusted with the fate of competition principles, and this is inappropriate because competition law is technical and subtle and (it is implied) must be applied by antitrust experts to maintain its integrity.

Second, it is argued, the WTO is a thin organization that cannot handle the additional competence.

Third, it is argued, the WTO context is wrong for competition law. First, trade talks mean bargaining, thus compromising rule of law (antitrust) by horse-trading. Second, WTO competences nearly always involve submission to WTO dispute resolution panels. But competition issues are fact specific and incapable of being resolved by WTO panels; and if competition issues are treated as subject to panel resolution 1) issues will be resolved by individuals who lack expertise and may be politically influenced, 2) firms will lose control of their confidential information, 3) panels might rule against the U.S. agencies, second-guessing their (probably superior and politics-free) assessment, and 4) the United States will lose sovereignty.

III. Do the protesters protest too much?

The fears may be overdrawn. The concerns outlined above are not intrinsic to the mere idea of some internationalization of competition law to meet the reality of global markets. It might be useful to begin at another place — a modest proposal at the intersection of trade and competition — and to examine whether the concerns are relevant to the proposal.

IV. What aspects of competition law might be handled within the WTO? — a modest proposal

The most pressing trade and competition problem today is the problem of market access blocked by anticompetitive restraints. Within this area, the most pressing concern is not the absence of national competition law, but the nonenforcement of national competition law.

There are means of advancing consensus on the market access competition issue while solving the institutional and sovereignty concerns noted above. A possible solution would provide an overarching conception to which nations might be expected to agree; and it would then defer to national formulation of law, and be largely self-executing, thus adopting the concept of European framework directives. To avoid coercion, a plurilateral agreement could be contemplated. The agreement would be applicable only to transactions and conduct with significant transnational effects. It could provide:

1. Nations should have and enforce laws against anticompetitive [or, unreasonable] blockage of markets.

   The laws should be applicable to state-owned enterprises and to privileges granted by the state except to the extent necessary for the enterprise to perform an obligation of the state, as in the EC Treaty of Rome Article 86 (formerly 90).

2. Nations should enforce and apply their laws without discrimination as to nationality.

a. While nations should be free to regulate their economies in ways that derogate from competition policy, nations should agree not to use nationalistic policies (such as national champion policies) to trump anticompetitive restraints that have significant negative international spill-overs.

b. In analyzing competition problems with substantial international effects, nations should endeavor to count the costs and benefits imposed and realized abroad as if those costs and benefits occurred within their borders.

3. Transparency

a. Conduct or transactions challenged as anticompetitive should be analyzed first and separately under competition criteria. Noncompetition criteria that are admissible and applied (e.g., environment, national security) should be clearly stated in decisions and opinions.

b. Each nation should assure that its rule of law is clear, e.g. by the use of guidelines or policy statements.

4. Cooperation, process and due process:

a. As in TRIPs and as in positive comity agreements (e.g. US/EU), nations should provide in their laws opportunity for harmed nations and persons to complain to the authorities of an allegedly excluding nation, and protocols should be established for agency cooperation in discovery and enforcement.

b. The allegedly excluding nation should be obliged to provide an accessible litigation or administrative system accompanied by the safeguards of due process, thus assuring effective recourse to harmed nations and persons (as in TRIPs). If this rule is violated, the harmed nation or person should be free to bring suit in its own country, subject to the choice-of-law principle below.

5. Choice of law

a. Where the harm is to a person's or nation's exports or foreign investment and the challenged conduct and the directly harmed consumers reside in the importing/excluding nation, the law of the latter nation should apply, unless waived by defendants in favor of the forum law, as long as the law of the excluding nation prohibits anticompetitive market blockage and is non-discriminatory.

b. If a nation does not have a law against anticompetitive or unreasonable market blockage, or that law is discriminatory on its face, the harmed nation should be free to apply its own law.

6. Dispute resolution

Dispute resolution should be available for conflicts arising from provable breaches of the above obligations (as in TRIPs).

a. A dispute resolution panel should be comprised of antitrust experts chosen by the disputing nations with regard to their expertise and their freedom from nationalistic bias.

b. The panel should not have power to second guess application of national law by any national authority or court, as long as the nation has and has applied its own non-discriminatory antitrust law. The panel should, however, have the right to determine that a nation has not credibly applied its own law, as in NAFTA Article 19.

c. Dispute resolution should be rule-based. The panel should apply the rules above. The panel should be required to submit a reasoned opinion, which should be published and should be available as guiding authority.

d. Binding nature? Perhaps the decisions of the panel should be recommendatory only for a first term of years while experience is developed.

The second potentially most pressing trade and competition problem arises from the fact that several WTO agreements incorporate competition law principles, such as abuse of dominance by anticompetitive exclusions. This concept is incorporated into the GATS and its Telecoms annex. Questions regarding interpretation of the competition concepts are bound to arise. To a large extent, these issues are market access issues and can therefore be resolved in the context of the above proposal, with a dispute resolution panel applying the law of the allegedly excluding nation.[1]

I recommend (below) attempts to develop consensus competition principles in the context of a free-standing competition forum. The principles developed in this forum could also inform the deliberations of a WTO dispute resolution panel.

[1]See also Eleanor Fox, Trade, Competition, and Intellectual Property—TRIPS and its Antitrust Counterparts, 29 Vand. J. Transnat'l L. 481 (1996), proposing choice of law principles for intellectual property/competition cases.

Further, I recommend continuation of the WTO Working Group on the Interaction Between Trade and Competition Policy, which has operated for two years under the leadership of Frédéric Jenny and which has greatly advanced the dialogue and understanding among nations. The Working Group might continue to refine trade and competition issues, and it might identify additional issues appropriate for WTO treatment and others appropriate for resolution on competition ground.

V. The Principal Common Arguments Against an International Initiative Do Not Apply to the Modest Proposal

The proposal presented above alleviates the concerns that trade law will degrade competition law and that other countries' competition law will undermine U.S. antitrust law. It does so by providing that the standard for impermissible private or commercial market blockage is a competition-based standard and that the law to be applied is the law of the excluding country.

The proposal alleviates the concern of feared, untrusted and intrusive dispute resolution, and the concern of the practical limits of the WTO, by narrowing the scope for issues subject to dispute resolution and by allowing disputing nations to choose their own panel of experts.

The modest proposal thus requires a new assessment by the skeptics.

VI. What competition aspects should be handled outside of the WTO, now or forever? — A proposal for a World Competition Forum[2]

It may be argued that the proposal is too unambitious. Strikingly, it does not cover cartels as such, although cartels are — at least to Americans — the most heinous antitrust restraint. It does not cover even export cartels, which are the most obvious sort of anticompetitive beggar-thy-neighbor conduct. It does not cover antidumping law reform, although it is possible that repeal of antidumping laws would produce more wealth and consumer welfare for the world than does antitrust enforcement itself. It does not cover the multitudinous, redundant merger control laws that impose high avoidable costs on global mergers. It does not provide for common world substantive standards, which would grease the wheels of trade and provide a helpful referent for the competition competences that are tucked into existing trade agreements, such as the GATS and the Telecoms annex.

Each of these problems deserves attention.

A. The Excluded Trade and Competition Issues

[2]I thank Merit Janow for her rich ideas on a World Competition Forum.

Two of the excluded issues outlined above are tightly trade-related: antidumping laws and export cartels. Both deserve to be included in a WTO agreement. Both are excluded from the modest proposal for reasons of pragmatism.

The antidumping law controversy is so politically charged that its inclusion in a competition agenda at this time will sound the death knell of the agenda.

Moreover, the antidumping law issue is not a competition *law* issue. Antitrust predatory pricing law is not a credible substitute for antidumping law; low-priced exports are almost never a part of exporters' strategy to monopolize foreign markets. The antidumping law issue must be dealt with on its own terms.

The export cartel problem is of a different order. Nations (at least now)[3]against export cartels. Because of their persistent and successful efforts to establish a common market, they see more clearly the mutual interest in dismantling artificial barriers and actualizing an economic community. It is no longer thinkable that German firms should have a right to cartelize into France unless France is able to catch them, and vice versa. seem to resist an initiative to ban export cartels on grounds of "sovereignty."[4] (Why should we — nations ask — protect the foreigners?) The resistance is short-sighted. It is in everyone's interest to be free of export cartels in an integrated world.[5]Law: The Case for Modest Linkages of Law and Limits to Parochial State Action, 19 World Competition L. & Econ. Rev. 5 (No. 2, December 1995).

The resisters add: Inbound extraterritoriality is now widely accepted, and nations can protect themselves from off-shore cartels that harm their markets by applying their own laws and, if necessary, seeking cooperation from the cartelists' home country under principles of positive comity. Therefore national law works. At least, pressure is removed from the pressure point.

The effort to eliminate export cartels at their source remains significant both substantively[6] and symbolically; but politically and pragmatically the issue is not likely to advance the current competition agenda.

B. The (More Nearly) Pure Competition Issues

Each of the other problems is not tightly trade-related. Some are urgent. As to them, my

[3]European nations seem more receptive than U.S. Americans to a world agreement

[4]It could be argued, however, that the Safeguard Agreement, Article 11.1, prevents nations from exempting export cartels.

[5]See Eleanor Fox and Janusz Ordover, The Harmonization of Competition and Trade

[6]Most harmed nations do not have the power and practical ability to defend themselves against offshore cartels.

point is not that pragmatism requires reticence but that these issues are at the heart of *competition* law, not trade law, and they deserve to be placed on "competition" ground. In some cases, continued conversations may produce more convergence of law and analysis, common understandings, and common culture. As to some issues, nations may and probably should reach agreement, much as environmental, labor and intellectual property concerns have produced agreements outside of the trade arena to control externalities and to solve prisoners' dilemmas.

A free standing World Competition Forum should be created. A number of possible agreements and missions would fall within its aegis. These include consideration of: 1) An agreement on multinational merger control that rationalizes systems for notification, waiting periods and clearance.[7] 2) An agreement limiting beggar-thy-neighbor anticompetitive private action, constricting excessive state trade-restraining anticompetitive action, limiting excessive state immunization of anticompetitive private action, requiring nondiscriminatory treatment, and requiring transparency of rules of law and of the methodology of analysis;[8] thus drawing heavily from lessons of the European Union's internal market [9] and from the GATT/WTO. 3) An agreement for cooperative initiatives among agencies, multilateralizing and deepening current positive comity undertakings. 4) An agreement establishing rules for the protection of confidential information. 5) An agreement establishing rules for appropriate and inappropriate extraterritorial jurisdiction, and protocols in the event of clashes of jurisdiction regarding enforcement, liability and relief. 6) Information and technical assistance for developing countries that may wish to adopt or have adopted competition laws. 7) Peer review and bench-marking teams. 8) Development of recommendations on substantive consensus principles,[10]to form consensus not only on procedural and due process rights but also on analytical concepts such as market definition, barriers to entry, and abuse of dominance). with transparency as to derogations, along lines of the recent OECD recommendation on hard core cartels.[11] Follow-up subjects of recommendations would logically include coercive boycotts and naked monopolistic exclusions.[12] Naked means: The restraint is

[7]See J.W. Rowley and A.N. Campbell, eds., Policy Directions for Global Merger Review, A Special Report by the Global Forum for Competition and Trade Policy (Global Competition Review April 1999).

[8]See Eleanor Fox, World Antitrust: A Principled Blueprint, an essay in honor of Professor Wolfgang Fikentscher (November 1997). See also Anne-Marie Slaughter, The Real New World Order, Foreign Affairs, vol. 76, no. 5, Sept./Oct. 1997, 183.

[9]See Eleanor Fox, Vision of Europe: Lessons for the World, 18 Fordham Int'l L.J. 379 (1994) (introduction to symposium issue).

[10]See Joanna R. Shelton, Deputy Secretary-General, OECD, Competition Policy: What Chance for International Rules?, remarks at Wilton Park, UK, Nov. 25, 1998 (suggesting efforts

[11]Recommendation of the Council Concerning Effective Action Against "Hard Core" Cartels, C(98)35, adopted at Paris, April 27-28, 1998.

[12]See Robert Pitofsky, Chairman, U.S. Federal Trade Commission, Competition Policy in a Global Economy — Today and Tomorrow, remarks at European Institute's Eighth Annual Transatlantic Seminar on Trade and Investment, Washington, D.C., Nov. 4, 1998.

imposed only to impose costs on rivals or eliminate competition; not to respond better to markets and consumers. 9) A general forum for the sharing of ideas and developing awareness and common understanding, including an understanding of: a) the needs of less developed countries and the effect of competition policy on their development goals, b) the importance of LDCs' development to the industrialized world, and c) the significance of various nations' choices of goals in formulating and enforcing their national competition law.

The international competition enterprise needs a home. While proliferation of organizations is not a desideratum, no existing organization fits the need. The WTO is, foremost, a trade organization. It offers trade-style bargaining, and dispute resolution that is driven by trade objectives. The OECD is comprised of too small and elite a set of nations. UNCTAD gives priority to development concerns. Trade and development are both vital concerns, and should be (and are) treated in their own right. In order to develop and retain sound competition principles with knowable rules of law, the competition enterprise also should advance, in the first instance, on its own ground.

The new home may be built under the banner of a World Competition Forum, wherein competition enforcers and NGOs representing business and consumers could meet to discuss common problems and build consensus. The forum could be hosted, successively, by competition agencies of various nations, and should, as developed below, have a relationship with the WTO (among other organizations) so as to foster cross-fertilization for the trade and competition issues on the WTO agenda.

C. The Market Access Proposal is Not Trivial

In any event, an expanded competence for the WTO in market access only would not be a trivial addition. The anticompetitive closing of foreign markets is a major perturbation in the world trading system, and conversely, the opening of closed markets promises major improvements in the trading system. A market access protocol promises not only to regularize and institutionalize the means to eliminate improper private restraints, but also to narrow the occasions both for extraterritorial antitrust and for the use of antidumping laws.[13]they are less likely to be able to engage in international price discrimination. Moreover, they would need to recover from their sales abroad, just as they must from their sales at home, a return to fixed costs.

As we move into the next century, and if and as countries such as China join the WTO, the problems of market access will surely deepen, and the line between public and private restraints will be increasingly opaque.

An expanded market access initiative will not be a panacea; and the market access proposal contained in this paper will probably catch only the clearest and simplest of

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[13]If domestic firms cannot protect their home market and make monopoly profits at home,

consensus antitrust market-blocking wrongs; but at least we will have taken an important step forward to fill a gap.

VII. Interactive Regimes

I have outlined two models that, together, could protect against international antitrust restraints, rationalize excessive antitrust regulation, and check nationalistic strategies. First, I have proposed an expanded market access competence for the WTO. Second, I have proposed a free-standing initiative, which would be a forum for competition law representatives of nations, and representatives of business and consumers, and would work towards consensus.

The two systems would be interactive. For example, as noted, as a source of consensus antitrust principles, WTO authorities or panels applying competition-specific rules of WTO agreements might draw from recommendations developed by the free-standing body, much like courts in the United States refer to the principles formulated in the Restatement of Law volumes published by the American Law Institute. Moreover, trade authorities should be welcome at deliberations of the World Competition Forum, and should be invited to identify trade implications of its ongoing work, and competition authorities should continue to have important input on competition issues in the world trading system. Interactions with the WTO, OECD, and UNCTAD should be institutionalized.

VIII. Should a WTO competition initiative be limited to the industrialized countries?

The question of who should participate in an international competition initiative may be a function of the form of international initiative.

If one chooses to try to develop a supranational substantive competition law, there is a case for confining the effort to small groups of nations with similar economies.

On the other hand if we choose to link nations together by GATT/WTO-type disciplines assuring more nearly open markets, with rules of transparency and nondiscrimination and with deference to national formulations of law, we should include all nations.

In my view, no international initiative should exclude less developed countries. Not only do the people of these countries (which account for most, and an increasing proportion, of the people of the world) have a right to participate as equal partners in the development of world rules, norms and cooperative enterprises, but the people of industrialized countries deserve the opportunity to broaden their own perspectives. Moreover, the less developed and developing countries need access to the benefits of any world agreement more than do the industrialized countries, which have the power to enforce law against

multinational enterprises, to call to account recalcitrant states, and to make bilateral arrangements on their own.

CONCLUSION

At the point of intersection with trade, competition policy has a natural place on the WTO agenda. For competition issues at large, the international issues should be addressed at a free-standing World Competition Forum, interactive with the WTO.

Chapter 15

Globalization, Competition and Trade Policy: Issues and Challenges

Frédéric Jenny
Professor of Economics (ESSEC)[1]

For the last three years the trade and competition communities have hotly debated the question of how to address the interface between trade and competition in the context of the globalization of markets. Scores of conference have been held on this issue, hundreds of papers have been produced for academic conferences, all of the international organizations which deal with international economic relations have spent considerable time studying the issue. At times this debate has been highly emotional, at times it has been highly sophisticated. It has also been very complex because the study of the interface between trade and competition in the context of the globalization of markets raises political, economical, legal and institutional issues at both domestic and international levels.Very different opinions are still being expressed on how to deal with this issue and some may feel that we are no closer to building a consensus than we were three years ago and may wonder whether all the energy that has gone into the debate has not been spent in vain.

Yet, if we go beyond the political posturing which is inevitable before any upcoming WTO ministerial, it should be recognized that we are not where we were three years ago. For one thing, most participants in the debate now admit that the globalization process implies that the issue of the interface between international trade and competition has to be addressed in some way or , as Jim Rill would say, that « the elephant is on the table. It will not go away ». Second, the debate has allowed us to explore in much more detail than had been the case previously the differences and the complementarities between trade policy and competition policy both at the substantive and at the instrumental level. The fact that the trade and competition officials in each capital had to agree to present a national contribution at the WTO Working group has contributed to this process. In the course of the debate, competition law enforcers in many developed countries have had the opportunity to abandon their situation of splendid isolation, have become less intellectually arrogant (vis a vis trade officials or officials of developing countries) and have gained in credibility with economic policy makers. At the same time, trade officials, on the other hand, have become more aware of the fact that their negotiating skills and tools had limits for gaining effective market access. The Asian crisis has also contributed to making developing countries more aware of the benefits of competition (or rather the dangers of neglecting the role of competition forces) and the usefulness of controlling global markets. The remarkable progress

[1] Frédéric Jenny is Vice-Chairman of the Conseil de la concurrence, Chairman of the OECD Competition law and PolicyCommittee and Chairman of the WTO Working Group on Trade and Competition Policy. The views expressed in this paper are solely those of the author and should not be ascribed to the above organizations.

of reflection on bilateral cooperation instruments that has occurred in the context of OECD has also been partly a by-product of this debate.

Only time will tell if and how the international community will choose to build on these achievements.

In the remaining sections of the paper we explore some of the issues which were addressed in the course of the three year debate on the interaction between trade and competition policy.

1) The goals and benefits of trade liberalization

The benefits of international trade liberalization (which has so far mostly focused on the elimination of « at the border » trade obstacles) are well known. First, trade liberalization expands the economic opportunities of firms by allowing them to reach consumers located beyond their borders. By expanding the potential market of domestic firms, trade liberalization also allows them to benefit from economies of scale or of scope which they could not benefit from in a purely national context. Thus, it contributes to cost reduction and potential increase in real income.

Second, trade liberalization implies more market competition which in turn means that static efficiency gains in production and distribution are passed on to consumers and that innovations reach the market place.

Third, because trade liberalization is a two way street, it contributes to a reallocation of resources in each of the trading nations. Resources invested in domestic industries which produce at a relatively high cost compared to foreign industries tend to be shifted over the long run to industries where they create more value.

The above benefits constitute the main reason why the community of trading nations has pursued a determined effort to liberalize international trade for the last fifty years.

While increased domestic competition and increased foreign investment may entail long run gains for labor and consumers, trade liberalization also entails short or medium term adjustment costs and raises political difficulties.

First, although trade liberalization brings overall benefits for trading countries, the distribution of gains may be uneven among countries since some may be better able to take advantage of the enhanced economic opportunities because of their endowment in resources or of their level of economic development. In the context of trade negotiations in which concessions and commitments are exchanged the asymmetry of benefits from trade liberalization is a particular source of concern for developing nations.

Second, the process of reallocation of resources is not a painless or a costless process because during the process factors (whether labor or capital) will have to be redistributed. Behind these abstract terms, there are also social realities to be reckoned with: lives will be disrupted, firms will go bankrupt etc....The process of adjustment must therefore be monitored and adapted so that its pace is politically acceptable.

Third, one inescapable consequence of trade liberalization is to shift the monitoring of economies from governments to market competition processes.

To address those issues at least partially, the international community has developed a set of instruments. To begin with, trade liberalization takes place in the context of voluntary multilateral trade negotiations which offer some reassurance that commitments will be balanced. As a result the pace of adjustment will be faster in some sectors or in some countries than in others.

Next, a dispute settlement mechanism has been created in the multilateral context of trade liberalization commitments to make sure that those commitments are indeed respected.

Last, within this context, a diversity of instruments, such as safeguard measures or anti-dumping measures, can be used to slow down the pace of the process of trade liberalization in certain sensitive sectors or situations. These instruments play the same role similar to that of traffic lights. Traffic lights are designed to allow people to go faster than they would otherwise be able to go even though at first sight they seem to be contradictory with a goal of speeding up the traffic. The difference between traffic lights and some trade policy instruments is, however, twofold : first, while traffic lights fulfill a purely technical function, safeguard and anti-dumping measures fulfill both a technical and a socio-political function ; second, in the multilateral context, each country remains free to establish such measures and apply them to individual cases, which does not preclude the possibility that these measures will be used strategically.

Although, at least from a theoretical perspective, the tools developed at the multilateral level are by no means perfect, this may not be the important issue. The real questions one should address are : have these tools favored trade liberalization ? Would other tools on which the international community could agree to be better tools to promote trade liberalization ? The second question is more difficult. Theorists argue that the speed of trade liberalization would be faster and more meaningful if some trade instruments did not exist. They are probably right if one compares what happens in the real world with the ideal and frictionless world of long term economic theory. However, the answer to the first question is clearly positive. Yes, multilateral trade negotiation have been useful and have allowed a certain globalization of markets and a considerable degree of economic development.

2) The goals and benefits of regulatory reforms

In the real world the legal, social and political environments of business activity shape both the conduct and performance of firms. Domestic sectoral regulations, in particular, constrain the strategic behavior of firms in many sectors and their ability to compete effectively in the market place. One of the main problems associated with sectoral regulations is that of regulatory capture by a small number of operators to the detriment of society at large.

Because in recent years there has been a growing awareness of the social benefits for economic development of competition in the market place, the issue of the social cost of sectoral regulations which provide large benefits for small consitutencies but simultaneously imply a large cost to society as a whole is more frequently addressed. There is a growing perception that domestic economic regulations need to be made as consistent as possible with the desire to allow as much market competition as is politically and socially acceptable.

In some countries this issue emerged because there was a general feeling that although public monopolies performed a useful social function by allowing the provision of politically determined universal services, they were also sheltered from competition in areas in which they did not need such protection to provide universal services and that their protection from competitive market mechanisms led them to be relatively inefficient.

In other countries, in which some regulations protected a particular social group (such as farmers or small scale firms), the issue of regulatory reform arose from the growing awareness that there could be better ways (i.e less restrictive of competition) to achieve the desired result , for example by transferring income to these categories rather than by distorting competition in the market place.[2].

[2] In a paper presented at the Symposium on Competition policy and the Multilateral Trading System at the WTO on April 19 1999 Dr S Chakravarthy , a former member of the Indian Competition Authority noted that « Swaminathan S. Aiyar, has made a pointed reference to the plethora of laws and rules in India that explicitly protect favored players, reduce competition and give discretion in decision making to politicians and bureaucrats in the name of public interest. He has observed that « public interest is frequently and unabashedly invoked to protect one specific interest group (unionised labour, small scale industries, handloom weavers) with no explanation of how or why the interest of this group transcends all others ». He has provided the illustration of restrictive policies which impede competition like reservation of industries for the public sector (Coal, railways, Postal services, Petroleum etc...) , canalisation of exports and imports through the public sector (Petroleum and some agriculutral products), the jute packaging order (compelling fertilizer and cement producers to use jute rather than plastic sacks resulting in leakage of material), reservations of items for the small scale sector and reservation of items for the handloom sector in support of his contention that many Governmental policies are anti-competitive in character. He has also referred to the Industrial Disputes Act which makes it impossible to retrench labour or close units without Government permission, even if the units are unviable and to the Urban Land Ceiling Act which inhibits competition in using urban land. In the

Thus, many developed and developing countries have embarked on a wide-ranging domestic regulatory reform exercise. Australia was the first ; next came the OECD countries. Then the Asian crisis led some countries to realize that restrictive domestic regulations had a cost and should be reviewed (Japan and Korea for example). In many of these countries the competition authority has played a significant and central role in such efforts.

G. Feketekuty, addressing the issue of « Market competition and regulatory reform in services » in a recent seminar held in Geneva, emphasized the complementarity between trade liberalization and regulatory reform by stating that « while the primary objective of global negotiations, of course, is to focus on obstacles to global competition, you can't have competition from foreign products and entreprises if entreprises are not free to compete in the domestic market in the first place ». He therefore offers the view that «the economic rationale for a competition-oriented approach to replace a traditional trade barriers approach to trade negotiations is twofold. First, it more directly focuses on the impact of policy measures on the efficient functioning of global markets. Second, it includes, under its purview a wider range of policy instruments that affect international competition. All the economic arguments that have traditionally been made in support of trade liberalization per se would apply to negotiations aimed at removing barriers that impede international competition. Such negotiations would further enhance the functioning of international markets ».

3) The goals and benefits of competition policy

Let me now turn to the issue of competition. The actual functioning of markets for goods and services depends on various considerations. Entrepreneurship, endowment in natural ressources and level of technological development are all important. Equally important is the fact that trade liberalization allows foreign firms to challenge domestic firms. Beyond this, and as we just mentioned, there is the recognition that because firms do not operate in a vacuum, the legal environment of business in any country will be an important determinant of actual competition. Finally, there is the the fact that business strategies will shape the intensity of competition.

The market process is a decentralized process based on the notion that individual strategic behavior by myriads of firms and consumers will be consistent with general welfare only to the extent that firms face competitive pressure. In other words, whereas the natural inclination of each firm would be to eliminate competition, they must be prevented from doing this so as to keep them under the pressure of having to produce at the lowest possible cost and sell at the lowest

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name of public interest, runs his further argument, protecting job leads to sacrifice of efficiency, raises potential costs and risks and discourage new investments ».

possible price to consumers. In the absence of such a mechanism, the expected overall benefits of decentralized decision making will be partly lost and transformed into rents by monopolistic firms.

The major goal of competition law is thus to allow firms to take advantage of business opportunities and to make sure that through the competitive process the actual working of decentralized markets will foster static and dynamic economic efficiency to the fullest possible extent given the regulatory environment of these markets[3].

Thus, the goals of competition policy are clearly consistent with the ultimate goals of trade policy and of regulatory reform. Wheras trade policy and domestic regulatory policy allow for the possibility of increased competition, competition policy ensures that private strategies do not distort competition.

Competition, whether international or domestic, can entail significant difficulties for the firms exposed to competitive pressures. It therefore comes as no surprise that governments in many countries, while recognizing the long term benefits to be expected from domestic competition policy enforcement, have developed instruments which at first sight seem to be at odds with the ultimate goal of competition policy but which do tend to make such a policy more politically acceptable.

Also, concern with fairness has led many governments to adopt fair trade laws which in fact dampen the intensity of competition.

Furthermore, in many countries small and medium size firms benefit to a certain extent from an exemption from the prohibition of anticompetitive practices.

In the case of declining industries, certain anticompetitive practices may be tolerated if they allow a more orderly reallocation of resources than would be the case otherwise.

The desire of governments to retain control over a significant part of their economy also translates into exceptions to the competition principle (such as in agriculture, banking or with respect to the state action doctrine etc...).

Prosecutorial discretion is another tool used by competition authorities to calibrate their efforts in certain directions or regarding certain sectors.

[3] For an extended and detailed discussion of the goals of competition policy see « The Objectives of Competition Policy », Proceedings of the European Competition Law Annual 1997, Claus Dieter Ehlermann and Laraine Laudati eds, European University Institute, Hart Publishing, Oxford 1998.

It thus must be recognized that contrary to the claim of competition authorities, competition policy instruments are no more « pure » than trade policy instruments. However, this has not prevented an increasing number of countries from relying on the discipline of competitive markets to foster their economic development. Today between 80 and 100 countries have a competition law or are in the process of adopting one whereas ten years ago no more than 50 countries had such a law.

In short, the instruments of trade policy and competition policy both reflect the tension between what is desirable in the long run and what is politically feasible in the short run. Both sets of instruments can be misused and concerns about such possible misuses are entirely legitimate. Nevertheless, the history of trade negotiations just like the history of the development of competition policy has shown that overall, there is a growing awareness of the usefulness of pursuing both policies.

4) The challenges of globalization

Trade and investment liberalization, the development of international competition, regulatory reform and the rapid development of new technologies in sectors such as telecommunications have contributed to the globalization of world markets. This phenomenon has far ranging implications for public policy in general and economic public policy in particular .When markets become more global, the territorially limited economic policy tools governments can use to monitor business activity become increasingly ineffective and the need to find ways to regulate international markets becomes more urgent .

As noted by G. Feketekuty « the globalization process has resulted in a deepening of international specialization and a deep interpenetration of national economies that has been referred to as deep integration. This means that the economic interests of individual nations have become so closely knit together that the traditional distinction between a domestic economic policy instrument and a foreign economic instrument (foreign trade or foreign investment measures) has become less meaningful. Any measure that has a significant impact on production decisions by a globalized firm has become a matter of concern for other national governments and the world community as a whole. This is true whether one looks at the issue from a producer (i.e.traditional mercantilist) or a consumer point of view ».

Examining the responses to the challenge to the operational sovereignty of governments posed by the globalization of markets, Wolfgang Reinicke[4] observes that for the most part they have been reactive and defensive (for example calls for

[4] Wolfgang H. Reinicke, « Trilateral networks of governance, business and civil society : the role of international Organizations in global public policy », background note presented at the Pre-Unctad Seminar on the role of competition policy for development in globalizing world markets, Geneva, June 14-15 1999

tariffs, non tariff barriers, capital controls, and other territorially defined limitations that force companies and private actors in general to reorganize along national or regional lines or calls for investments incentives and competitive deregulation in order to improve the competitive situation of the nation or even calls for extraterritorial application of domestic laws). Noting that these responses have severe weaknesses either because they attempt to reverse the trend toward globalization of markets (protectionism), or because they aggravate the loss of a governement's internal sovereignty (competitive deregulation) or because they expose the country to retaliatory measures (extraterritoriality), Wolfgang Reinicke suggests that « if governments want to shape globalization rather than react to it, they will have operationalize internal soverignty in a non-territorial context ». He notes that « a global public policy would de-link the operational elements of internal soverignty (governance) from its territorial foundation (the nation-state) and institutional environment (the government) ». From that standpoint he suggests that international organizations such as the OECD, the WTO, the IMF and the World Bank must assume new roles and are already increasingly involved in matters of domestic sovereignty and warns that « This enhanced role of multilateral institutions will only succeed, however, if national bureaucracies establish permanent channels of communication and interact on a regular basis to facilitate the exchange of information in the open, transparent fashion necessary for informed global public policy. In the domain of global finance this has become evident at the institutional level in cases such as the collapse of Barings or the problems at Daiwa. At the systemic level, the financial crisis in Asia has alerted policymakers that these linkages are long overdue. There should be no doubt, however, that cross-national bureaucratic alliances need to reach far beyond the domain of global capital markets and cover a broad range of policy issues, including the growing number of non-tariff barriers to trade that the WTO, the OECD and other multilateral institutions have begun to address ».[5]

5) The complementarity between trade policy, domestic deregulation and competition policy in the perspective of globalization

[5] A similar analysis underlies Eleanor Fox's approach to the issue of trade and competition in a recent paper on « Competition Law and the Millenium Round » to be published in the Journal of Economic Law. In her conclusion she states : « The nation-state is shrinking. In matters of economics, national boundaries are losing their relevance for purposes other than protection ; and protectionism is, increasingly, a losing strategy for the people and the peoples of the world. One solution would be to bring all economic law under the aegis of an enhanced World Trade Organization, a superstructure sitting atop the trading nations of the world. This route may seem to threaten the benefits of pluralism and subsidiarity. An alternative way forward is to enable the era of the porous nation-state. Tightly-related trade issues may be brought into the family of the WTO. The panoply of non-trade world economic concerns might move forward, each on its own footing, solving its own problems while developing an open architecture hospitable to the linking of systems across nations and disciplines ».

Trade policy, regulatory reform and competition policy are complementary because whereas trade policy eliminates governmental barriers to international trade, deregulation aims at getting rid of domestic regulations which serve no useful purpose and limit potential competition as well as market access, and competition policy tries to eliminate business barriers which could defeat the objective of market access underlying trade liberalization or deregulatory efforts by governments.

They are also complementary in another way. Even without practices which prevent market access or restrictive regulations with the same effect, it is obvious that the possible benefits of trade liberalization will not be realized if anticompetitive practices are prevalent on national and international markets. The objective of trade and competition policy is to allow the competitive process to make our economies more efficient. It is not to give a license to firms with market power or to international cartels to prevent innovation, to charge abusively high prices or to prevent entry. Such practices reduce the global welfare of all nations.

Against the background of an increasingly global economy trade policy, regulatory reform and competition policy all have limitations. Trade policy cannot ensure market access because market access depends not only on the reciprocal commitments of governments to eliminate governmental barriers to trade but also on the domestic (behind the border) regulatory framework of the trading nations and on the market strategies of domestic firms. Competition policy, which is only a domestic policy, cannot ensure that competition will prevail because competition in any territory will be partly affected by the market strategies of firms located outside the territory and over which the competition policy enforcers of that territory will have no jurisdiction and because competition policy is powerless whenever governmental regulations limit or unnecessarily restrict the scope of competition on a domestic market.

From the standpoint of competition policy, it is important to recognize the private practices which are a subject of concern when one considers the interface between trade and competition policy. Two major types of private practices should be distinguished.

The first type are practices originating in one country but having an anticompetitive effect abroad. These include export cartels, transnational mergers or cross border abuses of dominant positions. These practices may not create a trade barrier but they may rob some countries which have liberalized their trade of the benefits of trade liberalization. Because these practices do not create a market access problem they tend to fall outside the scope of multilateral trade agreements. In addition, because these practices create a competition problem in foreign countries competition laws and policies of the countries in which they take place are usually powerless to curb them. Indeed, the jurisdiction of domestic competition authorities is usually limited to practices which affect competition in their own country. We should also include in this category international cartels which seem to be quite

frequent and to affect a number of countries but which can be difficult to prove because the evidence is scattered across a number of jurisdictions.

To eliminate the practices which do not create a trade problem but which do reduce the benefits of trade two things are necessary. To begin with, the affected countries must have some sort of competition policy or law. Also, each competition agency must be able to get assistance from comparable competition authorities in the countries in which the evidence proving the existence of such anticompetitive agreements is to be found or the help of the authorities of the countries in which the firms which implement the practice are located so that they can be sanctioned. Many such cooperation agreements already exist at a bilateral or a regional level.

The second type are transnational private anticompetitive practices having a market foreclosure effect. These include import cartels, restrictive vertical agreements, standards set by professional organizations or domestic abuses of dominant positions (including by state owned entreprises). Because trade liberalization or deregulation measures have in the past been exclusively concerned with governmental barriers to trade and to competition, they are not completely useful to eliminate these practices. As they tend to reduce competition in the country of import, they could conceivably be eliminated by domestic competition law if such a law exists in the importing country (and if domestic competition authorities were under pressure to eliminate them). However, to ensure that competition law enforcement is consistent with trade liberalization, there would have to be a mechanism ensuring that such anticompetitive practices having a market access dimension are in fact eliminated and that the competition authorities of the country in which market access is denied do not condone or turn a blind eye to these practices.

6) Competition policy and economic development

Although there may be a growing consensus on the ultimate consistency and complementarity linking trade liberalization, regulatory reform and competition policy, a number of developing countries are not convinced that the adoption of a competition law or policy is appropriate during the first phases of economic development. They argue that capacity building through industrial policy is more important in the initial development stages than promoting competition.

Part of the reason why economists (and in particular micro economists specialized in competition issues) have had a poor record in convincing policy makers in developing countries that they should adopt market oriented reforms is that while economists naturally tend to emphasize the long term benefits of competition (using the comparative static microeconomic model as a reference) , they often understate (or do not take into account) the transitional costs and difficulties associated with the dynamic reallocation of resources necessary to promote economic growth.

Policy makers are understandably particularly concerned about such transitional costs.

However, some economists, such as E.Graham or F.M. Scherer, have tried to integrate both approaches and explored more carefully the respective roles of industrial policy and competition policy in the process of economic development. In a very insightful article about Southeast Asia, E.Graham[6] suggests that while one of the major goals of industrial policy is to redirect resources into export-generating sectors and away from import competing industrie, as the economic development of a nation proceeds, export generating sectors change. As Graham puts it : " In the successful (...) nations, the reallocation has taken on the character of an ongoing process. As income levels rise in these nations, reflecting underlying changes in the economy that are in turn driven by the growth of increasingly complex and knowledge-intensive activities, comparative advantage shifts such that some activities that once generated exports become less competitive internationally, to be replaced by new export-generating activities". Graham then ventures that « when the leading exports sectors of a nation become increasingly complex, industrial policy fails to work as well as it apparently did at earlier stages of development. Hence in order to continue to develop internationally competitive export industries, governments(...) have found that, as a pragmatic matter, adoption of less interventionist policies has been necessary. »

Along the same line of reasoning, in a paper on International Competition Policy and Economic Development[7], F.M. Scherer stresses that : « The paramount task for LDCs in the early stages of industrialization is absorbing technology already implanted elsewhere in the world and implanting it firmly in local product designs and production processes ».

However Scherer takes the argument one step further by adding that « to absorb other's technology effectively, it must be recognized, it is essential to have a cadre of well-trained engineers, some of whom carry threshold amounts of independent technical activity (i.e. « R&D »). But what must mainly be achieved is what economists studying technological change call « diffusion » ».

Scherer then raises the question of the structural domestic conditions which must be met to achieve swift diffusion. As he puts it : « Making the leap to modern products and production processes is not easy. Technology must be absorbed from abroad, and until a considerable amount of learning by doing has occurred, unit costs may (despite low wages) be higher than the prices at which comparable products are available from industrialized nations. During these early stages of production, it

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[6]) Competition policies in the dynamic Industrializing Economies: the case of China, Korea, and Chinese Taipei, Mimeo prepared for the OECD Development Center.

[7]) International Competition Policy and Economic development, F.M. Scherer, Discussion paper N°96-26, Zenter für Europaïsche Witschaftsforschung Gmbh, Industrial Economics and Management series, May 1996.

may be necessary to shield LDC firms from foreign competition ». The underlying reasons for adopting « infant industry » policies in the early stage of development then appears to lie in the fact that scale economies require concentration on the home market, in the fact that export cartels may be more effective for conquering export markets and in the need to subsidize the cost of technology absorption, learning by doing and product development necessary to conquer world markets. However pursuing such policies is not without cost as we shall argue later.

The general view put forth by E. Graham and F.M. Scherer is consistent both with the fact that industrial policy can be successful in the initial stage of development, as was true up to a certain point in a number of Asian countries (for example in Japan and Korea) and in European countries in the immediate post World War II period, and with the fact that it can eventually become a clumsy instrument for promoting complex or high tech industries in a later stage of economic development. This view is also consistent with the apparent failure of European industrial policy of the seventies because this policy was directed specifically at promoting the growth of high-tech complex industries (such as computer electronics, telecommunications etc...) which are the least susceptible to development through such policies. Finally, it is consistent with the observation that as economic development proceeds and as products from technologically sophisticated industries become more and more important to the growth of all developed economies, there should a general movement away from government intervention in market mechanisms.

Leaving aside the intricacies of the complex theoretical relationship between market competition and economic development, policy makers from developing countries arguing against the adoption of domestic competition laws in the context of the debate on the interaction between international trade and competition have offered a variety of simple (and on accasion simplistic) arguments.

The first argument is that in small countries deregulation and open trade (which are themselves part of a broadly based concept of competition policy) are quite sufficient to force competition on domestic markets.

Typical of such an approach is the comment to the author by an official of a developing country indicating : « We regard competition law as just one of the policy instruments to implement a competition policy. Deregulation, privatization and a liberal trade and investment regime are examples of other policy instruments that are also important in promoting competition in an economy. We do not intend to undermine the benefits brought by competition law, but would like to point out that the absence of competition law does not necessarily lead to an anti-competitive trading environment. This is illustrated by the fact that not all of the forerunners on the list of freest economies put together by various international organizations such as the Heritage Foundation or the World Economic Forum have a domestic competition law ».

Similarly an official of another developing country remarked « (My country) is an open economy and the deregulation and liberalization policies already undertaken by the government, including under the GATT and WTO multilateral trade negotiations, make it fairly competitive in the domestic as well as in the international arena. As such there are views that (my country) does not need a specific competition legislation (....) ».

About this first argument, it should be pointed out that both in developing and developed countries, competition law can be a necessary or at least useful complement to deregulation policies because deregulation policies may in themselves be insufficent tools to bring about the expected benefits in terms of democratic process, the promotion of efficiency or the search for fairness. In the case of non tradeable goods and services (which often represent a substantial part of household consumption) the forces of international competition will not be felt and privatization and deregulation may well lead to undue concentration and lack of competition. In tradeable goods industries anticompetitive practices by domestic firms may defeat the market opening measures associated with trade liberalization.

As an example, in a recent seminar on competition policy attended by experts from Asian countries one of the speakers stated « It has been mentioned that (my country) is making the transition from a planned economy to a market economy. In this regard (my) government has implemented a series of deregulation policies since the early 1980s and it is highly likely that to enhance economic growth (my country) will continue to do so in the future in a more progressive manner. It has become a public secret, however that the main beneficiaries of this process so far have been the politically well-connected large businesses. This in turn , raises a basic issue that needs to be addressed properly : i.e. the large concentrations of economic and political power.(...).

« It was in the early 1970s that in order to boost economic development, the government began to work closely with the business sector. Since then, (my country) has witnessed the growth of « conglomerates », some created by the families of politically dominant figures, who relied heavily on special government facilities in running their business. Both parties - the government and the conglomerates- were interdependent in the sense that, on the one hand, the government needed conglomerates to create jobs and foster economic development and, on the other hand, conglomerates needed government to secure lucrative projects. (...) Hence high level collusion and monopoly of great industrial trusts became prevalent. »

« The picture has been getting better since the mid-1980s as various deregulation policies and reforms have increasingly exposed the business sector to the principles of the market economy, and the government has receded from its role as the main source of growth. In addition, there has been increased perception that growth, to a large part due to deregulation and reforms, has been inadequately accompanied by equitable distribution of the benefits. Yet most of the well-connected conglomerates

are still there, getting richer by cultivating their strong influence over the decision making process in government circles. As a consequence, we can easily notice that there has been a continuous tendency for reversal and inconsistent developments with regard to various government policies affecting competition. Even worse, the debate on competition issues in (my country) tends to be emotional and is gaining little support from principal players in the economy. »

« In such circumstances, it is difficult to improve the competition environment to ensure that market power is not abused, that the best possible allocation of national resources leading to high efficiency is achieved, and that the rights of consumers are well protected ».

A second argument sometimes invoked by skeptics of the usefulness of domestic competition laws in developing countries is that such laws may in fact be used as a Trojan Horse by multinational corporations to destroy the national economies of developing countries. For example, an official of a developing country which does not have a competition law stated to the author : « There exists a suspicion that advanced nations do not seem interested in countering the international anticompetitive RBPs of TNCs (trans national corporations), such as transfer pricing and other intra-firm practices. In other words the EU and the US especially aim at ensuring that developing countries institute effective antimonopoly laws at the national level but do not seem to be interested in dealing with anti-competitive behaviors and RBPs of their TNCs at the international level. (...) concerns over the greater concentration of economic power in (...) giant foreign corporations or MNC's should be the focus or rationale for implementing competition legislation, rather than giving these giants more market destructive clout. The curbing of global monopolistic practices by such multi-national corporations should be an integral 'built in' defence in developing countries' competition policy , rather than allowing big foreign companies to capture most of the developing countries' markets ».

This second argument raises the issue of the limitations of domestic competition laws to solve some of the problems raised by cross-border anticompetitive practices. However, as we shall argue later, the adoption of domestic competition laws is a useful and a necessary first step for countries wishing to be in a position to fight international anticompetitive practices which originate outside their territories but have an effect on their domestic markets (even if the adoption of such laws may be in themselves insufficient to solve all cases of international anticompetitive practices).

A third argument often presented by those who argue against the adoption of domestic competition laws by developing countries is that the laws that exist in developed countries may be inappropriate for developing countries. Thus the following view : «While competition is supposedly beneficial to all players in the economy, competition between producers may not always work to the best interest of the overall economy. If this happens , the government should seriously consider whether some sort of intervention should be carried out to achieve equally

important goals such as consumer safety, ensured access to a basic standard of living, and stability of the economy ».

This third argument is not an argument against the adoption of a competition law but merely makes the valid point that competition laws should be tailored to the specific circumstances and the economic and legal environment of the countries in which they are enacted (an issue to which we shall return when we discuss the issue of minimum standards). As we mentioned earlier, if domestic competition laws pursue the ultimate goal of fostering economic efficiency through competitive market mechanisms, they often also pursue broader « intermediate » goals. Thus, for example, one of the (intermediate) EU competition law goals is to integrate the European market whereas other competition laws usually do not pursue such a goal. In other jurisdictions, where there is a particular sensitivity to the risk that economic power may unduly influence political decisions and therefore competition laws, these jurisdictions have provisions prohibiting holding companies etc.... Thus, the enactment of a competition law does not preclude governments from seeking to achieve broad socio-political goals, but it does give them an incentive to ask themselves whether the best or the only way to achieve these goals is through restrictions of competition which have undesirable effects on economic efficiency.

A fourth argument sometimes presented against the introduction of competition laws in developing countries is that they could be misused and lead to undue bureaucratic control over market mechanisms. Typical of such a view is the following question raised by an official of a developing country : « While we understand the importance of enhancing (our country's) competitive edge, is legislation the best route forward ? (My country) is well known for its competitive , open and highly deregulated economy and free market forces have generally worked well there. Do we want to upset this mode of operation by enacting a comprehensive competition law which could be an overkill of potentially efficiency-enhancing collusive agreements ? These are some of the issues we have to take into account in examining this issue ».

This argument is probably the easiest to deal with. Indeed, there will not be the possibility of « overkill » if competition laws are designed to promote economic efficiency by stamping out anticompetitive practices which have no redeeming values but do include the possibility of exemptions for anticompetitive practices which have significant and demonstrable efficiency enhancing effects. Such competition laws exist in many jurisdictions.

On the issue of the relationship between economic development and competition policy, I would like to add a final comment which derives from the considerable amount of work which has recently been undertaken in the area of transnational anticompetitive practices.

It is increasingly clear that such practices, and in particular but not exclusively international cartels, not only are numerous and durable but also impair the process of economic development in developing countries. This is true for at least three reasons :

first because in the early stages of their industrialization, and given their narrow domestic industrial base, developing countries have to rely on imports. To the extent that such imports are subject to anticompetitive practices either by domestic firms (for example, because of an import cartel) or by the foreign suppliers of these imports (for example because of an export or international cartel), the importing country will be penalized by higher than necessary import prices;

second, because to achieve economic development, and in view of the fact that they have narrow based domestic markets which leads them to rely on export markets, developing countries will be penalized by international cartels, or by import cartels and by abuses of dominant position in the countries of export ;

third, because foreign firms feel all the freer to engage in across the border anticompetitive behaviors when the countries to which they export do not have a domestic competition law and can neither individually nor through cooperation with foreign competition authorities challenge the firms' market behaviors. Thus, countries which do not have a domestic competition law will be the prime victims of transnational anticompetitive practices.

Available evidence show that for long periods of time in the recent past international markets for goods as diverse as steel products, industrial diamonds, heavy electrical equipment, graphite electrodes, lysine, food additives, vitamins etc... were subject to established quotas of production or export and or to fixed prices which meant that importing countries were rationed and paid artificially inflated prices for their imports. This is of course just the tip of the iceberg, since we know that currently in the US there are thirty grand juries investigating international cartels. A common feature of some of these cartels (such as for example the steel cartel or the heavy electrical equipment cartel) was that they were applied to countries which did not have a competition policy and that they engaged systematically in predatory pricing or dumping whenever a developing country was building up a domestic industry.

If we now turn to examples of cross border abuses of dominant position, there is evidence (arising, for example, from a 1994 case in the US) that Pilkington monopolized the worlwide flat glass market for over three decades by entering into an unreasonably restrictive licensing arrangement with its likely competitors and using these agreements and threats of litigation to prevent these competitors (including some US firms) from competing to design, build and operate flat glass plants in other countries, even though Pilkington no longer had enforceable intellectual property rights to warrant such restrictions. These practices clearly harmed countries which sought to acquire the equipment to make flat glass.

If we now turn to international mergers, it is clear that some of these may have anticompetitive effects abroad and that such effects can be prevented only if the affected country has the legal means to block the merger on its territory or to impose the necessary domestic divestiture. For example, the Coca-Cola/ Cadbury Schweppes merger (which concerns more than a hundred countries throughout the world) has recently been blocked by, or raised objections from, competition authorities in countries such as Mexico, Belgium, Australia and a host of European countries. As a result, Coca-Cola and Cadbury Schweppes have abandoned their merger plans in those countries but still plan to go ahead with the merger in countries which are lacking a competition law, even though it is possible that this merger will significantly affect competitive conditions on the market for cola based drinks or on the market for carbonated soft drinks in those countries. To take another example, the Kimberly Clark and Scott merger in 1995 was likely to affect competition and ultimately domestic prices in a great many countries for a great many paper products. Competition authorities in a few countries such as the US, the EU, and Mexico imposed divestitures to accept the merger. But what is remarkable is that the scope of divestiture required varied from one country to another because the competition effects of this merger were not the same in all countries. One may observe that no divestiture could be ordered in countries which did not have a competition authority even though it is likely that this merger reduced domestic competition for at least some products in such countries and thus was likely to result in higher prices for their consumers. A similar story may be offered about the Colgate-Palmolive-American Home Products merger which took place in 1994. This merger affected competitive conditions in four markets : toothpaste, toothbrushes, dental floss and mouthwash. As result of this merger the market share of the merged firms would have been nearly 80% of the toothpaste market in Brazil, which used the merger provision of its competition law to force the divestiture of the Kolynos brand. Although it did not create a particular competition problem in some countries , this merger had the possibility of severely injuring competition in other countries where there was no competition authority to review it.

These few examples testify to the fact that even if one believes that competition law and policy is not an appropriate tool to foster domestic economic development in developing countries, it is clear that private international anticompetitive practices or monopolization by global firms of domestic markets can prevent economic development or limit its scope and that failure by developing countries to have adequate means to fight such practices exposes them to significant costs and setbacks on the road to economic development.

7) Options for the future

Let me now turn to my personal assessment of what has been going on in the context of the WTO working group on the interaction between trade and competition.

I think that everybody recognizes that as an educational tool this group has succeded in bringing much more clarity to the debate on the interface between international trade and competition.

Part of the reason for this success lies in the composition of the group which includes both trade policy specialists and competition policy enforcers, two communities which were previously suspicious of one another.

Whereas at the beginning of the group's activities much emphasis was placed on the differences between competition policy and trade policy, a second phase of the discussion focused on exploring the complementarities of the two policies. When we met in December 1998 for what was to be the last meeting of the group under its original mandate, there was a consensus that the work of the Working Group should continue and be more focused on how to achieve a better complementarity between the two policies. This has enabled the group to think in more concrete terms about what steps, if any, could be taken, whether in the WTO framework or elsewhere, to enhance this complementarity.

The second reason why the discussion was extremely useful in the context of the WTO is because developing countries contributed so much to the debate (irrespective of whether or not they had a competition policy and/or law) and brought a different perspective to the discussion than the more developed countries. The developing countries have become more aware of the fact that they need to address transnational anticompetitive practices because they are often the direct victims of such practices even when their economy is open to international trade. They have also emphasized that the tools of competition policy need to be adapted to their particular environment.

When one thinks about how to make progress on the issue of the interface between trade and competition, many questions and options must be considered.

The first one, of course, is whether there is any need at all for a multilateral agreement on competition or whether unilateralism and/or cooperation between competition authorities of countries which have such authorities is sufficient to address the problem. From that standpoint the successes of the recent US policy of investigating international cartels (and relying for this in certain cases on cooperation agreements) has been offered as evidence of the fact that there may not be a need to look for more constraining tools. These successes are indeed very impressive and certainly contribute to proving the usefulness of such agreements. The new tools of cooperation developed within the context of OECD (such as

positive or negative comity) may also prove effective although the scope for their use has not been tested yet.

However, three arguments can be offered in support of the idea that cooperation agreements are in themselves insufficient to address the issue of the interface between trade and competition at the global level.

First, the fact that sets of countries which already have a competition law and a competition authority might choose to enter into bilateral cooperation agreements, does very little to convince countries which do not have such a competition law or policy that they should adopt one[8]. As we know, only two thirds of the WTO members have such an instrument or are in the process of establishing one. In countries which have not chosen to introduce such a domestic instrument, domestic anticompetitive practices may block market access. This may be a particularly severe problem in the multilateral context since we know that the introduction of a competition law or policy and authority in a country is useful not only to eliminate private practices but also to suggest, through their advocacy function, modifications of regulations which unnecessarily restrict competition and market access. In addition, private practices which originate in countries which have not chosen to introduce a domestic competition law or policy may restrict competition in other countries which have a competition law without permitting the competition authorities of such countries to seek assistance in eradicating these practices. Thus the first advantage of a multilateral agreement on competition would be to include a commitment of a number of countries to address the issue of competition as it relates to internantional trade.

Second, entering a cooperation agreement is a voluntary process. This means that each country decides with whom it wants to cooperate and with whom it chooses not to cooperate. Thus countries which have a competition law may not always be in a position to enter into a cooperation agreement with the competition authorities of countries in which international private practices which negatively affect their trade or competition interests take place. This raises the issue of whether the discretion that countries have to establish cooperation agreements with some trading partners and not with others is consistent with the non discrimination principle of the GATT. In a world in which international transactions may simultaneously affect the interest of many countries this may create a particular problem if some of the countries involved (but not all of them) have a cooperation agreement. A multilateral framework for competition would imply a commitment on cooperation and would treat trading partners who have committed themselves to

[8] In a recent pre-UNCTAD X symposium held in Geneva in June 1999 Professor Dr Ernst-U. Petersmann noted « Just as trade liberalization is politically easier on the basis of reciprocal international obligations rather than unilaterally, the introduction of competition laws and policies is politically easier in a framework of reciprocal international rules. Most countries in Europe introduced national competition laws only after they had previously accepted international competition rules (e.g. in the EC Treaty or in free trade agreements concluded with the E.C.).

have an effective competition law in a less discriminatory way. In the context of the Kodak Fuji dispute, the case was not brought to the Japanese Fair Trade Commission for a formal ruling before it was brought to the WTO dispute settlement panel and escalated into a potential trade war. The argument presented at the time was that the JFTC was not to be trusted and this appears to have been a very thin argument in the light of the fact that US antitrust authorities trust the JFTC enough to have since then entered into a cooperation agreement with the Japanese competition authorities. One may wonder whether such a dispute would not have been more efficiently handled had there been a commitment of cooperation between the Japanese and the US competition authorities at the timeit came up.

Third, within the context of most cooperation agreements, cooperation on specific cases is voluntary and undertaken when such cooperation is in the mutal interest of the parties to the agreement. Thus as we mentioned earlier, whereas such agreements can be very useful when the interests of the parties to the cooperation agreement are similar, they may be much more difficult to use when the competition effects of the practices considered are asymetric (i.e. affect one country but not the other) or when they create a trade problem. From that standpoint, it comes as no surprise that such agreements have mostly been sucessful in stamping out international cartels. But the record shows that they are rarely if ever used to eliminate export cartels or, import cartels or even mergers with differentiated effects on competition. For such practices a commitment to cooperate seems to be necessary to achieve what voluntary cooperation cannot usually achieve.

Because of the perceived limitations of voluntary cooperation several countries have suggested that it would be useful to establish, in the multilateral context, a basic framework of competition rules and cooperation for international trade consistent with the general WTO principles of transparency and non discrimination as well as a cooperation commitment. This is the approach favored by the EU, Japan , Korea and a number of other countries. The proposals of these countries have some common features. A broad and basic principle they share would be to require countries to commit themselves to adopt an instrument to eliminate private anticompetitive practices that distort trade and competition. This principle would be backed by specific provisions on substance, enforcement procedures, cooperation and dispute settlement. The specific provisions and enforcement mechanisms should be transparent and non discriminatory.

A number of observers have noted that certain elements of the TRIPS model could be useful for the establishment of such a multilateral framework on competition. Indeed, both intellectual property laws and competition laws deal with private behaviors in the marketplace and in both areas some countries lack a law and others may have different legal regimes and institutions.

As with the TRIPS agreement, an international competition framework could endorse the broad principles of non-discrimination, national treatment, most favored nations and transparency[9]. Indeed there does not seem to be an incompatibility, but rather a general consistency or complementarity between these principles and the underlying principles of competition law. However, the precise implications of the endorsement of these principles in the context of a competition framework would have to be detailed as they are in any multilateral agreement.

At the substantive level, the TRIPS agreement contains a comprehensive set of substantive obligations dealing with all major intellectual property rights. Although the TRIPS agreement recognizes that private anticompetitive practices may have an

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[9] Article 1 §3 of the TRIPS agreement provides that « Members shall accord the treatment provided for in this Agreement to the nationals of other Members ».

Article 3 §1 of the TRIPS agreement provides that « Each Member shall accord to the nationals of other Members treatment no less favourable than that it accords to its own nationals with regard to the protection of intellectual property rights..... ».

Article 4 of the TRIPS Agreement provides that « With regard to the protection of intellectual property, any advantage, favour, privilege or immunity granted by a member to the nationals of any other country shall be accorded immediately and unconditionally to the nationals of all other members ». This article also provides for some exemptions of this obligation.

Article 63 of the TRIPS agreement provides that :

1 Laws and regulations, and final judicial decisions and administrative rulings of general application, made effective by a Member pertaining to the subject matter of this Agreement (the availability, scope, acquisition, enforcement and prevention of the abuse of intellectual property rights) shall be published, or where such publication is not practicable made publicly available in a national language, in such a manner as to enable governments and right holders to become acquainted with them. Agreements concerning the subject matter of this Agreement which are in force between the government or a governmental agency of a Member and the government or a governmental agency of another member shall also be published.

2 Members shall notify the laws and regulations referred to in paragraph 1 to the Council for TRIPS in order to assist that Council in its review of the operation of this Agreement.(...).

3 Each member shall be prepared to supply, in response to a written request from another Member information of the sort referred to in paragraph 1. A Member having reason to believe that a specific judicial decision or administrative ruling or bilateral agreement in the area of intellectual property rights affects its rights under this Agreement, may also request in writing to be given access to or be informed in sufficient details of such specific judicial decisions or administrative rulings or bilateral agreements

4 Nothing in paragraphs 1,2 and 3 shall require Members to disclose confidential information which could impede law enforcement or otherwise be contrary to the public interest or would prejudice the legitimate commercial interests of particular entreprises, public or private ».

effect on trade (and in particular that some licensing practices may consitute an abuse of intellectual property rights having an adverse effect on competition in the relevant market) and that members may wish to take appropriate measures to prevent or control such practices, it does not commit signatories to adopt a competition law to eliminate such abusive practices and leaves the determination of unlawful practices to member states. It does provide, however, for a cooperation mechanism between countries in its section on the control of anti-competitive practices in contractual licensing[10].

[10] Article 8 paragraph 2 of the TRIPS agreement provides that :

« Appropriate measures, provided that they are consistent with the provisions of this agreement, may be needed to prevent the abuse of intellectual property rights by right holders or the resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology ».

Article 40 of the TRIPS agreement provides that :

«1 Members agree that some licensing practices or conditions pertaining to intellectual property rights which restrain competition may have adverse effectson trade and may impede the transfer and dissemination of technology.

2 Nothing in this Agreement shall prevent Members from specifying in their legislation licensing practices or conditions that may in particular cases constitue an abuse of intellectual property rights having an adverse effect on competition in the relevant market.As provided above, a Member may adopt, consistently with the other provisions of the Agreement, appropriate measures to prevent or control such practices (...)

3) Each Member shall enter, upon request, into consultations with any other Member which has cause to believe that an intellectual property right owner that is a national or a domiciliary of the member to which the request for consultations has been addressed is undertaking practices in violation of the requesting Member's laws and regulations on the subject matter of this section, and which wishes to secure compliance with such legislation without prejudice to any action under the law and to the full freedom of an ultimate decision of either Member. The Member addressed shall accord full and sympathetis consideration to, and shall afford adequate opportunity for, consultations with the requesting member, and shall cooperate through supply of publicly available non-confidential information of relevance to the matter in question and of other information available to the Member, subject to domestic law and to the conclusion of mutually satisfactory agreements concerning the safeguarding of its confidentiality by requesting member.

4 A Member whose nationals or domiciliaries are subject to proceedings in another member concerning alleged violation of tha other member's laws and regulations on the subject matter of this Section shall, upon request, be granted an opportunity for consultation by the other Member under the same conditions as those foreseen in paragraph 3.

Article 69 of the TRIPS agreement provides that :

« Members agree to cooperate with each other with a view to eliminating international trade in goods infringing intellectual property rights. For this purpose , they shall establish and notify contact points in their administrations and be ready to exchange information on trade in infringing goods. They shall, in particular, promote the exchange of information and cooperation between custom authorities with regard to trade in counterfeit trademark goods and pirated copyright goods ».

The TRIPS agreement sets out broad effectiveness standards and specific procedural guarantees applicable to the enforcement of intellectual property rights through administrative and judicial proceedings. It was the first multilateral agreement to impose detailed obligations regarding private and public enforcement. TRIPS requires procedures which permit « effective action », grant expeditious remedies sufficient to deter infringment and are « fair and equitable ». The general effectiveness standards in TRIPs could undoubtedly be useful reference for a competition agreement[11] since the effectiveness of the enforcement mechanism is crucial to competition policy.

It should also be noted that some of the provisions of the GATS agreement could also be useful references in the context of the negotiation of a possible competition multilateral agreement. Besides endorsing the general principles of most favored nations and transparency, the GATS agreement contains competition provisions regarding the behavior of monopolistic suppliers as well as provisions regarding other business practices of service suppliers which «may restrain competition and thereby restrict trade and services » and establishes a consultation and cooperation mechanism[12].

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[11] Article 41 of the TRIPS agreement provides that :

« 1 Members shall ensure that enforcement procedures as spcified in this Part are available under their law so as to permit effective action against any act of infringement of intellectual property rights covered under this agreement, including expeditious remedies to prevent infringements and remedies which constitute a further deterrent to further infringments. The procedures shall be applied in such a manner as to avoid the creation of barriers to legitimate trade and provide for safeguards against their abuse.

2 Procedures concerning the enforcement of intellectuel property rights shall be fair and equitable. They shall not be unnecessary complicated or costly, or entail unreasonable time limits or unwarranted delays.

3 Decisions on the merits of a case shall preferably be in writing and reasoned. They shall be made available at least to the parties to the proceedings without undue delay. Decisions on the merit of a case shall be based only on evidence in respect of which parties were offered the opportunity to be heard.

4 Parties to proceeding shall have the opportunity for review by a judicial authority of final administrative decisions and, subject to jurisdictional provisions in a Member's law concerning the importance of a case, of at least the legal aspects of initial judicial decisions on the merits of a case. However, there shall be no obligation to provide an opportunity for review of acquittals in criminal cases.

5 It is understood that this part does not create any obligation to put in place a judicial system for the enforcement of intellectual property rights distinct from that for the enforcement of law in general, nor does it affect the capacity of members to enforce their law in general. Nothing in this part creates any obligation with respect to the distribution of resources as between enforcement of intellectual property rights and the enforcement of law in general. »

[12] Article II of the Gats Agreement provides that :

What is more, the GATS agreement contains a specific feature which could be of use in the negotiation of a competition agreement, given the fact that some (developing) countries feel that they are not yet ready to adopt such a competition law or to eliminate exemptions or exceptions to such a law. Indeed, in the context of the GATS agreement a large measure of flexibility and progressivity is built into the process through the possibility of successive negotiations of a schedule of specific commitments (which can themselves be modified with compensatory adjustments)[13]. with a view to achieving a progressively higher level of liberalization.

It thus appears that previously negotiated multilateral agreements and in particular the TRIPS and GATS agreements have already dealt with Members obligations in the area of the regulation of private practices in a flexible and progressive manner, thereby recognizing the necessary complementarity between market competition

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« 1 With respect to any measures covered by this Agreement, each member shall accord immediately and unconditionnally to services and service suppliers of any other members treatment no less favourable than that it accords to like service suppliers of any other country.

Article III of the GATS agreement establishes transparency obligations of the members along lines similar to those seen previously in the TRIPS agreement.

Article 8 of the GATS agreement provides that :

« 1 Each member shall ensure that any monopoly supplier of a service in its territory does not, in the supply of the monopoly service in the relevant market, act in a manner inconsistent with that member's obligations under article II and specific commitments.

2 Where a member's monopoly supplier competes , either directly or through an affiliated company in the supply of a service outside the scope of its monopoly rights and which is subject to that Member's specific commitments , the Member shall ensure that such a supplier does not abuse its monopoly position to act in its territory in a manner inconsistent with such commitments.(....) ».

Article IX of the GATS agreement on Business practices provides that :

« 1 members recognize that certain business practices of service suppliers, other than those falling under Article VIII, may restrain competition and thereby restrict trade in services.

2 Each Member shall, at the request of any other Member, enter into consultations with a view to eliminating practices referred to in paragraph 1 . The Member addressed shall accord full and sympathetic consideration to such a request and shall cooperate through the supply of publicly available non-confidential information of relevance to the matter in question. The member addressed shall also provide other informations available to the requesting Member subject to its domestic law and to the conclusion of satisfactory agreement concerning the safeguarding of its confidentiality by the requesting Member ».

[13] Article XIX of the GATS

and trade liberalization as well as the necessity of taking into account national circumstances.

However, when it comes to a possible multilateral competition agreement, two additional concerns have been voiced. The first one is related to the definition of substantive obligations in such an agreement, the second one is related to the applicability of the multilateral trade dispute settlement mechanism to competition law matters.

As regards the first concern, the issue involves knowing what competition law provisions would have to be adopted by Member countries party to such an agreement in order to meet their commitments. Some observers have noted that because competition law provisions differ from one country to another, it is very unlikely that an agreement could be reached in a multilateral context. Other observers have suggested that possible differences between substantive standards are not of great importance because most of the problems related to the interface between trade and competition arise out of alleged ineffective enforcement of domestic competition laws rather than because of differences in substantive standards. Thus, for example, Eleanor Fox considers that : « Proposals for minimum or detailed substantive antitrust rules assume that multitudinous sets of national rules create conflicts and obstruct trade. But the antitrust conflicts among nations have generally not been caused by different formulations of substantive principles. Generally the conflicts have been caused by non enforcement of law, different interpretations of permissible extraterritoriality, and nationalistic action that is either protectionist, blindered to global impacts, in disregard of sovereign prerogatives, or the credible perception that one has occurred ». E. Fox considers that it would thus be sufficient to require countries to « have a law that qualifies as « antitrust » within the range of common understanding. A law would not be a full fledged antitrust law if it did not have a provision against cartels and against monopolization or abuse of dominance. Control of mergers with significant spillover effects could be a requirement. It is more doubtful that the community of nations would force sister nations to include a law against vertical restraints other than those caught by laws against abuse of dominance or oligopoly power and by laws against horizontal conspiracies (cartels including boycott) »[14]. Although the

[14] Eleanor Fox « International Antitrust : Against Minimum Rules ; for Cosmopolitan Principles » The Antitrust Bulletin, Spring 1998, pp5-13. In this article and a subsequent article to appear in the Journal of Economic Law, Eleanor Fox focuses on the market access problem and argues that this issue, although a sub issue of the general interface between trade and competition is one « where the interests within and among nations converge ». She proposes that a market access commitment, whereby Nations would commit themselves to « have and enforce laws prohibiting commercial conduct that reasonably impair market access » would be a useful addition to the existing WTO obligations and adds « this proposal does not require that all countries adopt full blown competition laws. Merely they must not allow unreasonable restraints on market access. The most obvious but not only way to do so is bythe adoption of - at least- a competition law (...). If a nation such as Singapore could guarantee an environment free of anticompetitive impediments to market access by means of assuring absolutely free entry into markets (i.e. no governmental barriers), perhaps they should be allowed to try ; this is a detail ».

European Commission initially suggested that minimum standards of competition laws should be embedded into a multilateral agreement on competition, it seems that it has become more convinced that such an approach was neither politically feasible nor useful and it has recently shown willingness to adopt a more flexible approach. Other countries which have suggested the negotiation of a multilateral agreement on competition have followed the line suggested by Eleanor Fox.

Some commentators have expressed the fear that such a general approach would lead member countries having a competition law stricter than what the multilateral commitment would suggest to weaken their domestic competition laws. Such a view (which assumes that countries which had an interest in adopting a strict competition law when their trading partners did not have such a law would see it as being in their interest to weaken their laws because their trading partners comitted themselves to have a competition law) does not make logical sense. In addition, it does not seem to rest on any empirical evidence since (to the best of the knowledge of the author) no one has offered evidence that countries which had strict competition law provisions against abuses of dominant position weakened this regime after and because of the adoption of the GATS agreement.

A more serious question is that of the scope for the applicability of the dispute settlement mechanism to a multilateral competition agreement. There is widespread recognition that the WTO dispute settlement mechanism is not well suited to the review of decisions taken in individual cases both because of the fact intensive nature of such cases and because of the development of innovative approaches that are frequently case-specific in the enforcement of competition law. Such a mechanism would , in any case, be all the more difficult to apply to individual decisions that the substantive obligations contained in such an agreement are cast in general terms rather than as precise provisions. Furthermore, because competition decisions are often judicial decisions, making them subject to the dispute settlement mechanism raises obvious questions about national sovereignty.

However, a dispute settlement mechanism could be useful to solve disputes about the fulfilment of procedural obligations (such as the commitment to adopt a competition law covering specific practices, and the commitment to respect the principles of non discrimination, national treatment or most favored nation, the commitment to consult and cooperate etc...). In other words for the near future (and until a consensus emerges, if it ever emerges, on the ways in which the dispute settlement mechanism could be used to assess individual decisions) the use of the dispute settlement mechanism could be limited to provable breaches of commitments[15]. Furthermore, it should be noted that the WTO Understanding on

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[15] Eleanor Fox suggests in her article on « Competition Law and the Millenium Round » to be published in the Journal of Economic Law, that « As for dispute resolution, the only issue subject to dispute would be the violation of the terms of the agreement itself ; for example, not adopting the agreed substantive or procedural law. A dispute resolution panel would not act as a trial court to resolve facts. It could determine, on the basis of the

Rules and Procedures Governing the Settlement of Disputes includes a mechanism to allow experts to play a useful role in assisting panels. Thus experts with the necessary qualifications in the area of competition law could be brought into the proceedings at the request of a party or of the panel. Indeed Article 2 paragraph 2 of the Understanding provides that : « Panels may seek information from any relevant source and may consult experts to obtain their opinion on certain aspects of the matter. With respect to a factual issue concerning a scientific or other technical matter raised by a party to a dispute, a panel may request an advisory report in writing from an expert review group ». Several multilateral agreements provide for the possibility that the panel be assisted by an advisory technical expert group either at its own initiative or upon request by a party to the dispute. In some cases the technical expert groups findings are binding for the panel[16].

Finally, another option proposed by some countries, (Hong Kong China in particular) would be to negotiate a «free trade and competition commitment », rather than negotiating a commitment on the adoption of domestic competition law. Such an approach would in their eyes have two advantages. First it would not

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record and with deference to national court, whether the national law was credibly (non-discriminatorily) applied- the standard of review under NAFTA article 19 ».

[16] For example, article 11 of the Agreement on the application of Sanitary and Phytosanitary Measures provides that : « In a dispute under this Agreement involving scientific or technical issues, a panel should seek advice from experts chosen by the panel in consultation with the parties to the dispute. To this end, the panel may, when it deems it appropriate, establish an advisory technical expert group, or consult the relevant international organizations, at the request of either party to the dispute or on its own initiative ». Similarly Article 14 of the Agreement on Technical Barriers to Trade provides in its paragraph 2 that : « At the request of a party to a dispute, or at its own initiative , a panel may establish a technical expert group to assist in questions of a technical nature, requiring detailed consideration by experts ». The annex 2 of this agreement sets the rules governing such expert groups in particular concerning the treatment of confidential informations.

The Agreement on Subsidies and Counterveiling Measures goes further than the Agreement on the Application of Sanitary and Phytosanitary Measures. Article 24 paragraph 3 of the Agreement provides that «The (Committee on Subsidies and Counterveiling Measures composed of representatives from each of the members) shall establish a Permanent Group of Experts composed of five independent persons, highly qualified in the field of subsidies and trade relations. The experts will be elected by the Committee and one them will be replaced every year. The PGE may be requested to assist a panel, as provided in paragraph 5 of Article 4. The Committee may also seek an advisory opinion on the existence and nature of any subsidy.

Paragraph 5 of Article 4 provides that : « Upon its establishment, the panel may request the assistance of the permanent group of experts (...) with regard to whether the measure in question is a prohibited subsidy. If so requested, the PGE shall immediately review the evidence with regard to the existence and nature of the measure in question and shall provide an opportunity for the member applying or maintaining the measure to demonstrate that the measure in question is not a prohibited subsidy. The PGE shall report its conclusions to the panel within a time-limit determined by the panel. The PGE's conclusions on the issue of whether or not the measure in question is a prohibited subsidy shall be accepted by the panel without modification ».

necessarily imply that all committed countries must have a competition law since the means by which each country would live up to its «free trade and competition » commitment would be left to its own initiative. Second, such a commitment would have the added advantage of being broader than commitments to eliminate transnational anticompetitive practices because it would presumably cover a commitment to eliminate domestic public regulations (or possibly trade regulations) which impair trade and competition. As Professor Petersmann remarked at a recent UNCTAD seminar[17] « The « WTO approach » recommended e.g. by Hong Kong focuses on the complementary market-freeing functions of liberal trade and competition rules, rather than on the regulatory functions of competition laws(e.g. as regards merger control laws, limitation of abuses of market dominance, setting-up of independent competition authorities). The strengthening of the existing GATT and GATS market access commitments (e.g. by extending them to exclusionary anti-competitive practices of private and public undertakings), and the liberalization of the still pervasive governmental and private market access barriers (e.g. in the context of protectionist antidumping policies protecting import-competing industries from foreign competition), are viewed as more important than the long-term competition policy goal of adoption of competition laws in all WTO Members ».

Conclusion

While exploring the possible avenues for addressing the issue of the interface between international trade and competition several things should be kept in mind.

First, because of the existence of vested interests, the constituency for competition is relatively limited in a number of developing countries, thereby limiting the ability of such countries to engage in market oriented reforms or to adopt a competition law. It thus would seem that building a culture of competition where it is lacking is a necessary condition for facilitating the adoption of instruments allowing a better complementarity between trade liberalization, regulatory reform and competition policy. International cooperation and technical assistance are important instruments for building a competition culture or developing appropriate institutions.

Second, the community of trading nations is a very diverse community. Economic structures differ greatly from one country to another, systems of laws are not the same, the economic history of each country is specific to that country and societal goals reflect the culture of each country. This means that any solution to the general problem of promoting the complementarity of trade liberalization, regulatory reform and competition policy must be flexible enough to allow such national differences to continue to exist. Thus it seems that mechanisms that would provide for a supra national competition law or the establishment of similar domestic

[17] Pre-Unctad X meeting on the Role of Competition policy for developments in Globalizing World Markets, geneva June 14-15 1999

competition laws including detailed substantive or procedural rules would be difficult and undesirable. It should be noted from that same perspective that existing international commitments at the multilateral level in the trade area are not designed to prevent countries from pursuing the domestic policies they see fit to pursue. Multilateral agreements allow differences in national legislations as long as these differences are not contradictory with the underlying principles of the WTO. A multilateral commitment on competition should have the same characteristics[18].

Third, the existence of differences in levels of economic development among countries implies that not all countries are equally able to benefit from the opportunities offered by international market competition.. It must be observed that this issue is also relevant in trade negotiations (since not all countries are equally able to benefit from the opportunities offered by trade liberalization measures) and yet has not prevented the multilateral community from agreeing on trade commitments. Instruments have been devised in the trade agreements area to allow a certain progressiveness or flexibility of commitments depending on local situations[19]. Such progressivity or flexibility should also be allowed in the competition policy area.

Fourth, if we go back for a moment to the typology of transantional anticompetitive practices I briefly mentioned previously, it should be clear that to eliminate those practices, and barring the existence of a supranational law which is not advisable for the reasons already mentioned, decentralized domestic competition instruments and institutions are needed. The first type of practices (i.e. transnational anticompetitive practices which do not create a trade problem but rob trading nations of the benefits of trade liberalization) can be fought through bilateral or regional cooperation mechanisms between competition authorities (such as agreements on exchange of information or positive or negative comity arrangements). Thus irrespective of what may happen on the multilateral front, developing voluntary bilateral or regional cooperation among competition authorities is not only useful but also necessary. The second type of practices (i.e. practices which create a market access problem and a competition problem) might not be so easily removed through voluntary cooperation because the trade interests of the countries involved tend to conflict.

Fifth, because trade liberalization, regulatory reform and competition policy are obviously complementary and because some private transnational anticompetitive practices may lead to market access problems, some countries have suggested that it would be desirable for the multilateral community to include the topic of competition

[18] See , on this issue « International antitrust : against minimum rules ; for cosmopolitan principles, Eleanor Fox, The Antitrust Bulletin, Spring 1998

[19] See for example the « Decision on Measures in Favour of Least Developed Countries » or the « Decision on Measures Concerning the Possible Negative Effects of the Reform programme on Least Developed and Net-Food Importing Developing Countries » adopted by the Trade Negotiations Committee on 15 December 1993

policy on the agenda of future negotiations in the WTO. They have observed that the complementarity between trade liberalization and competition policy has already been acknowledged in the context of the WTO, for example in sectoral agreements, such as the GATS agreement. In this respect it has been observed that the underlying WTO principles of non discrimination, national treatment and transparency were relevant to the basic objectives of competition policy. However, such principles are probably insufficient in themselves to ensure an effective competition mechanism in the multilateral framework and they must be adapted to the issue of competition policy. For example, the application of the national treatment principle to competition policy raises the question of the treatment of export cartels (which usually do not fall within the ambit of domestic competition laws). Similarly, the question has been raised of whether the transparency principle should be applied ex ante to competition rules or ex-post to individual decisions. Thus if a multilateral negotiation is undertaken in the context of the WTO one should keep in mind that just as competition policy principle at the multilateral level has to be adapted to the specific interface between trade and competition, the trade principles will have to be adapted to the specificity of competition policy or law.

Chapter 16

Antitrust and the WTO: Some Heretical Thoughts

Robert E. Litan
Vice President and Director, Economic Studies Program, and Cabot Family Chair in Economics, The Brookings Institution

Now that successive trade negotiating rounds have mowed down most tariffs, trade negotiators have been focusing on the remaining "weeds" that impede cross-border trade. One of the weeds – or the more technically neutral term, "non-tariff barriers" – that has attracted much attention is the difference in competition policies between countries.

"Competition" is a broad word and has different meanings to different people. Narrowly construed, it covers only antitrust policy, or domestic rules designed to ensure that firms compete against each other in ways that benefit consumers. Broadly construed, competition policy also includes regulatory policies that may promote (or more often impede) competition and trade rules (specifically antidumping rules and countervailing duties) that also affect the terms on which consumers are able to buy goods and services.

In these short comments, I'll offer some views about both how to proceed on both the narrow and broad competition policy agendas. I will be realistic, accepting political conditions as they are for now. But I also will be bold, and indeed argue that a bolder strategy may be a more successful one -- eventually.

I am mindful throughout that trade negotiations are about more than just what makes good economic sense. Trade deals get done because they serve the interests of those who want them to get done. More specifically, although trade agreements are designed to promote the interests of *consumers*, they generally are negotiated on behalf of *producer* interests who want greater access to foreign markets. In the process of serving producer interests, trade negotiators incidentally happen to serve the interests of consumers, but consumer organizations typically are not represented during trade discussions (a point I believe some non-governmental organizations should keep in mind when complaining that labor or environmental interests are also given short shrift at these meetings). It is imperative, therefore, that any discussion about a possible competition policy agenda at the next trade round consider who might support that agenda and what political interests it might serve.

Why Competition Policy Should Be On The Trade Agenda

It is useful to begin, however, by reminding ourselves of at least two reasons why competition policy – at least narrowly construed -- even deserves to be on the trade agenda.

First, ineffective competition policies can deny market access to exporters. Boycotts can be just as effective in preventing entry of foreign products or services as tariffs, quotas, or outright prohibitions. In essence, this is what the Kodak case was all about. Kodak lost

primarily because the WTO found that the private acts allegedly committed by Japanese film distributors were not covered by current international trade rules.

Second, anti-competitive acts undertaken abroad -- even entirely by foreigners -- may raise prices of goods sold to consumers in other countries. This is why, for example, the Justice Department sued Japanese fax paper companies for fixing prices of exports to the American market. This cartel raised prices on fax paper imports and in the process had a significant adverse affect on U.S. consumers, thus giving U.S. prosecutors substantive jurisdiction to proceed (a view that was challenged by the defendants but upheld by a federal appellate court).

In short, bad competition practices have cross-border externalities that make them the legitimate subjects of international negotiation. Put another way, if every country enforced effective antitrust laws and thus ensured workable competition in their markets, consumers at home and abroad would benefit.

Progress So Far

Even without having a WTO-sanctioned agreement on competition policy, U.S. antitrust authorities have enjoyed some progress toward increased cooperation on procedural antitrust matters with various countries:[1]

--The United States has entered into "positive comity" agreements with the EU, Canada and Australia whereby countries offer to undertake antitrust investigations at the request of other parties.

--The U.S. and the EU have conducted a number of investigations jointly, notably the initial Microsoft matter (which prosecutors from both sides of the Atlantic negotiated in tandem), and a number of merger matters involving companies doing business in both the U.S. and Europe.

--The U.S. has entered in "mutual legal assistance treaties", or MLATs, with about 20 countries, under which enforcement officials exchange information and assistance during the course of criminal investigations (with appropriate safeguards for confidentiality).

--In 1994, the Justice Department worked with the Congress to obtain passage of the International Antitrust Enforcement Assistance Act which gives DOJ and the FTC authority to enter agreements with other countries to exchange otherwise confidential information on a reciprocal basis (except in merger cases). The first such agreement negotiated under the Act was with Australia, which updated the cooperation agreement between the countries reached in 1982.

I am reasonably certain that in his remarks today, Joel Klein will cite these various initiatives as having borne fruit in a series of grand jury investigations, consent decrees and fines involving price-fixing and other cartel-type behavior by foreign defendants.

[1] For a more detailed summary, see Janow [1998].

A Realistic Short-Term Competition Policy Agenda

If progress is being made toward increased cooperation on competition issues, then why should the subject be considered by the WTO at this time?

The best answer is that private restraints may be significant impediments to foreign commerce in many countries around the world, especially in the developing world where many countries either do not have formal antitrust statutes on the books, or if they do, they lack sufficient resources to enforce them effectively. The question is what to do next?

One answer is out of the question. Although the idea has enjoyed some support in the academic literature, the notion of creating a world antitrust enforcement authority, or giving antitrust enforcement authority to the WTO, is a political non-starter. No nation, including the United States, wants to cede so much of its sovereignty to an international enforcement body.

Fortunately, there are certain steps that might be achievable -- provided the political muscle were available to get them on the agenda and through the negotiation.

At a minimum, the next WTO round could establish a presumption against so-called "blocking statutes", or laws that prohibit foreign investigators from gaining access to evidence against targets residing in the countries having such statutes. These appear to be more popular in other developed countries (Canada, the Netherlands, Great Britain, Germany, France and New Zealand, among others) than in emerging markets. The strong form of an agreement in this area would seek simply to eliminate existing blocking statutes, or at the very least put an international standstill against the adoption of any new such statutes by countries that now don't have them. A less draconian approach might be to require countries to suspend enforcement of existing blocking statutes (and related "claw back" statutes that limit enforcement of foreign antitrust judgments) where a country's investigators demonstrate that "reasonable cause" under its antitrust laws exists for pursuing the investigation outside the country. An expedited WTO review panel procedure could be established to adjudicate disputes between countries on whether the reasonable cause test has been met.

A more ambitious agenda would seek to have the WTO codify a set of minimum competition policy standards. As Graham and Richardson (1998) and other observers have pointed out, there is no universal consensus on all of acts that should be punishable under an antitrust regime. However, there is reasonably wide understanding that price-fixing, group boycott and related cartel behavior should be forbidden. The minimum standards could cover only these subjects and avoid the more controversial areas of dominant firm behavior, vertical restraints, and merger policy, where there clearly is no international consensus. Another purely parochial advantage from the perspective of our antitrust authorities of sticking to the area of cartel behavior -- which is nearly universally deemed to be bad -- is that it eliminates the risk of having our antitrust standards in the

other controversial areas watered down, either by our own trade negotiators or by their counterparts in the WTO.

Janow (1998) suggests a different approach. Rather than focusing on generic minimum standards, she suggests sectoral negotiations, aimed at expanding competition in specific areas where competition heretofore has been lacking. The example she cites is of the telecommunications agreement under the Uruguay Round, which appears gradually to be leading the signatories to open up their telecom markets to all kinds of new competition, foreign and domestic.

I can think of two prominent areas where additional sectoral progress would be welcome: airlines and ocean shipping. Both markets historically have been heavily sheltered from competition around the world; indeed, shipping price-fixing cartels are not only allowed, but encouraged.

I personally would love it if these issues were added to the next trade round, but I have no illusions of the political difficulties in doing so. I won't discuss them further here, since in both cases (and even in telecom) the major problem is not the absence of effective antitrust laws, but instead affirmative government policies that actually restrict competition in these two other industries. Whether removing these restrictions are advanced under the "competition policy" banner or under some other heading makes little difference. It would be desirable just to get it done.

Returning to the issue of minimum standards, a key issue once they are placed in an international agreement is how to ensure that they are effectively *enforced* by national antitrust agencies. This is the lesson from the Basle capital accord, by the way -- an international agreement among 12 industrialized countries on minimum capital adequacy standards for banks. The standards were adopted in 1989 but then were not effectively enforced by a number of countries, especially Japan, whose deep banking problems have been avoided (until recently) by the government, which has granted weak institutions "forbearance" from the requirements. Meanwhile, there is little or nothing that other Basle parties can do about this, except complain. The markets help a bit -- putting a "premium" on the interest rates that Japanese banks have to pay to induce large depositors to hold their funds in Japanese banks.

In principle, the markets could perform a similar function in the antitrust area. It is possible that international investors may penalize countries that announce tough anti-cartel policies but then don't enforce them. In the clever terminology introduced by Tom Friedman (in his best seller, *The Lexus and the Olive Tree*), the "electronic herd" of foreign investors may shun such countries that pretend to put on the "golden straightjacket" of Western capitalist institutions (of which sound antitrust policy is one) but don't actually do so. Still, I wouldn’t bet much on this actually happening.

How else can WTO minimum competition policy standards be enforced? One possibility is to distinguish between a country's failure to follow through on a *specific* cartel

investigation and the broader or more *generic* failure by the country to devote adequate resources to the enforcement of its minimum anti-cartel provisions.

For example, if a country fails to adequately pursue a specific investigation -- as determined by a WTO panel -- then enforcement agencies from exporting countries harmed by this inactivity might be given *a limited period of time* in which to pursue their own investigation in the non-complying country, armed with whatever compulsory processes exist in that country. A broader failure to enforce the law in its entirety -- a more difficult determination to make since it would require a pattern of inactivity over a several year period -- might justify invocation of the "nullification and impairment" provisions of the WTO, which as I understand them, entitle countries harmed by the failure of a party to adhere to its WTO commitments to impose offsetting measures -- for example, raising tariffs on or otherwise impending exports from the offending country.[2]

I will be the first to admit that neither of these penalties may be sufficient to prod countries to enforce their minimalist antitrust statutes. In addition, I assume it would be difficult gathering evidence in a WTO panel proceeding demonstrating that countries have failed to honor their commitments. In effect, the hearings would amount to prosecutions of the prosecutors within different countries, hardly easy or friendly undertakings. Nonetheless, this is probably what lies ahead if nations agree to a set of minimum standards and want to have at least some way of effectively enforcing them.

A Bolder --And Conceivably More Realistic -- Competition Policy Agenda

Any parent raising a child probably has learned at least one thing about influencing behavior: carrots generally work better than sticks. Punishments may work once or twice or even for longer periods, but over time, penalties build up resentments, and may even stop working. Rewards, in contrast, light up kids' faces and often produce the result desired by the parent. Of course, rewards may have declining impacts as well. Larger and larger rewards may be required over time to generate the desired behavior.

In the trade arena, it is noticeable that rewards are almost never used. Instead, the enforcement machinery of the WTO -- and the GATT before it -- relies on the threat or actuality of trade sanctions to deter undesirable behavior. I will admit that sanctions often work, but in recent times, the proliferation of trade sanctions for all sorts of reasons (for human rights, for national security reasons and so forth) has been severely devaluing their currency. Moreover, repeated threats of sanctions undermine trust between countries on a broader set of issues, just as they may poison relations between parents and their children.

[2] Graham and Richardson suggest that the WTO panel only report its findings and make no remedy recommendations; but they write in a context in which nations have not agreed to minimum standards as part of their WTO obligations [Graham and Richardson, pp. 563-65]. Presumably, the authors would welcome a bolder enforcement approach if minimum antitrust standards were explicitly included in the WTO.

It would be nice, therefore, to find and make use of some kind of reward to encourage countries to implement and enforce sound competition policies. Fortunately, there is an obvious choice: use the antidumping laws, which no sensible economist today defends,[3] in a creative fashion to provide the needed inducement.

I can predict the first reaction that many of the practically-minded in this audience will have even to my mentioning the idea: forget it. Antidumping has been the third rail of trade politics for the obvious reason that even free trade-minded politicians have trouble explaining to constituents how the "unfair trade laws" actually may punish behavior that would be legitimate if engaged in by domestic firms.

But hear me out for a moment before totally writing off what I'm about to say. The idea I have in mind is not to eliminate the dumping laws and replace them with antitrust laws, although I confess that is my first-best recommendation. Instead, I propose more realistically that countries that adopt and enforce some minimum set of antitrust standards would be entitled to have their firms qualify for somewhat less onerous -- and to be blunt, less protectionist -- antidumping provisions in the event they are subject to antidumping investigations abroad. Countries that meet an even higher threshold of antitrust prosecution and enforcement -- namely those that do more than enforce the minimum anti-cartel statutes -- might qualify for even more lenient antidumping treatment, but I'll leave that bell and whistle for the future.

What might the relaxed antidumping provisions look like? Several possibilities, all not mutually exclusive, come to mind (although for practical political reasons probably only one of these could be chosen): elimination of the cost of production test, a tougher injury test than "material" cause of injury, or the addition of consumer benefits as an offset to consideration of injury.

One trick in implementing my proposal is defining the criteria that a WTO panel would use to certify that a country's competition policy has passed the threshold and that qualifies it for the more sensible antidumping treatment. At a minimum, of course, the country would have to enact the minimum antitrust standards. It might then have to demonstrate that its government antitrust agencies have at least a certain minimum number of enforcement officials (relative to GDP or the population, or some or other objective standard). Alternatively, or in conjunction, the country might be able to show that it allows private rights of action and that its courts actually entertain and handle such suits. Yet another approach is to automatically certify any country once it adopts the minimum standards, and then take away its special antidumping treatment as a penalty for failure generically to enforce those standards (as discussed above).

I believe my approach would have all the right incentives. It would encourage developing countries -- or those now with the weakest competition policy regimes yet frequently subject to our antidumping laws -- to upgrade their antitrust efforts. Meanwhile, since the EU would qualify right away for the special treatment, my proposal would at least help

[3] For detailed critiques of the antidumping laws, see Congressional Budget Office, 1994 and 1998; and Willig.

smooth the waters over the increasingly acrimonious trade relationship between the U.S. and the EU. And finally, the recommendation accords with economic reality and common sense. About the only justification left for antidumping laws that I hear these days is that they are needed to punish countries that close their domestic markets, encouraging their firms to "dump" abroad. My proposal would meet this argument head-on by rewarding countries that use competition policy to prevent private behavior that has a market-closing effect.

The Politics of Competition: Getting From Here to There

Up to now, I've discussed a possible competition policy agenda at the next round of talks in a political vacuum. I've focused on potentially good policy, but as I've noted, trade deals only happen when interest groups on all sides of the table want them to happen. The result may be good policy, too -- but not necessarily.

Who wants competition policy to be in the next trade round? In principle, U.S. antitrust authorities want it there -- but probably only under certain conditions. They don't want negotiations that weaken our own standards. And they probably putting some kind of enforcement or decisional power in the hands of new international bodies or the WTO.

I can't speak for the antitrust authorities from Japan, Europe and elsewhere. They may have similar interests as those of the U.S. authorities. Or they may be even more fearful of establishing new international institutions that might intrude on their sovereignty or make life more difficult for some of the leading firms in their countries.

What about the private sector? Exporters who now find it difficult to crack foreign markets are likely to be supportive of any deal that can be pitched as helping to break down private barriers to entry, such as those enforced by group boycotts. But it is doubtful that many firms in developing countries will be enthusiastic about having new enforcement initiatives directed against them. Indeed, the same might be true of many firms in developed economies, who although they might welcome greater access to foreign access, might also worry about being investigated by a whole new set of actors.

In short, I find it hard to see what broad-based constituency -- other than a few enforcement agencies, and these are doubtful -- actually wants competition policy, as it is traditionally and narrowly framed, to be included on the next trade agenda.

That leads me back to my heretical suggestion to tie at least some modest relaxation in antidumping law to some minimum competition policy standards as the best way to move forward. The dumping law reforms would be enthusiastically welcomed by foreign exporters. In addition, they might also be championed by American exporters who increasingly (although not yet universally) are being subject to antidumping investigations in other countries that have learned these techniques so well from the United States (see CBO, 1998 for data in this regard).

I admit that the political sticking point with my proposal is in the U.S. Congress, where import-competing industries such as the steel industry have considerable influence. However, if properly explained, the proposal might have a chance. Again, the point is not to eliminate our antidumping law, but instead provide a small, and potentially effective, carrot to induce other countries to upgrade their antitrust enforcement against cartels that disadvantage U.S. exporters. I hold no illusions about the prospects of success in making such an argument, but then again, I'm afraid I don't see much else in the competition policy area on the horizon that both promises consumer benefits and that has a reasonable constituency behind it.

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Chapter 17

MAI: Main Points

Donald Johnston
Secretary-General of the Organization of Economic Cooperation and Development (OECD)

The "MAI" -- or multilateral agreement on investment -- is the name of a draft agreement that was negotiated by the OECD countries from 1995 to 1998. It is also a generic concept. It is important to distinguish the two in discussing what happened to bring negotiations to a halt in OECD and in considering what should happen next.

The fact that negotiations have stopped at OECD does not mean that the need for multilateral rules for investment has gone away. OECD countries remain convinced that rules are needed, in the interests of the international community as a whole and perhaps especially the smaller developing countries whose markets may otherwise be less able to attract the "patient" investment capital they desperately need to grow and develop (see the OECD Secretary-General's Report to Ministers on International Investment, Attachment 1).

New multilateral rules for investment will not come about unless we learn from the experience of the MAI negotiations. If the diagnosis is wrong, the corrections might simply create new problems or allow the same mistakes to be repeated. With respect to OECD, it would be wrong to conclude that the Organization is ill-suited to develop "rules of the game". It is true that the dispute settlement procedures envisaged in the MAI went a step beyond anything previously agreed upon in the Organization, but the OECD has always had rules for its members. Recent examples include: the (legally-binding) Anti-Bribery Convention, the Corporate Governance Principles, Transfer pricing rules and the current work on harmful tax competition.

Different approaches to investment rules -- bilateral, regional and multilateral -- are possible and can be mutually supportive: Indeed the world is already better served with investment rules than is generally recognized. Hence, new multilateral rules need not be comprehensive from the outset.

OECD has a new work program on international investment and multinational enterprises based on two main pillars. First, analysis and discussion of key issues that emerged from the MAI negotiations as needing closer attention in the development of investment rules by the international community. Most of these issues arise at the interface of rules designed to provide non-discriminatory treatment to foreign investments and the responsibility of sovereign governments to regulate in the broader interests of their societies (see Attachment 2). Second, a thorough Review of the OECD Guidelines for Multinational Enterprises which since 1976 have provided a benchmark for good corporate behavior for corporations and a vehicle for promoting corporate responsibility. We are also studying the increasingly important phenomenon of codes of corporate

responsibility. These two pillars reflect the economic and social balance needed in any modern approach to international investment questions.

Attention is now focused -- quite properly -- on the forthcoming Ministerial Meeting of WTO in Seattle. If it decided to include investment in the Millennium Round, the WTO will have our full support. There is absolutely no question of "transferring" the MAI -- or any other OECD text -- to WTO or any other sovereign institution. But the results of OECD activities will, of course, be made available to all.

Issues for Discussion

1. Core Disciplines

The starting point must be to encourage more investment to flow. If the rules do not achieve that they will not be much use. Better transparency is the obvious place to start. Then a choice may have to be made between two broad approaches:

a) investment protection rules, as in the 1500 or so bilateral investment treaties. Typically, these provide legal security for established enterprises and other forms of property. They have no obvious counterpart in trade agreements, and since the bilaterals are already in place it is arguable that investment protection rules are not the main priority.

b) a non-discrimination rule for new as well as existing investments. We find this principle already applied to investment flows in the OECD instruments (the Code for the Liberalization of Capital Movements, and the National Treatment instrument) but without formal dispute settlement procedures for enforcement. We also find it in NAFTA and Mode 4 (commercial presence) in the GATS, but not in most bilateral investment treaties.

A decision is also needed about the breadth of the definition of investment. The MAI negotiators were searching for a broad all-encompassing definition, accompanied by special provisions for exceptions and safeguards to allow countries to employ restrictions in crisis situations subject to IMF surveillance Since the recent financial crises, it has become more fashionable to argue for a narrower definition to exclude volatile short-term capital flows. But given the ingenuity and complexity of financial markets, is it feasible to develop a definitional distinction that would work in practice?

2. Integrating the Social Agenda

Investment rules cannot provide a comprehensive legal framework for business activities. They do not replace national laws or international agreements on such matters as competition, intellectual property rights, health and safety, environmental protection, labor laws or social security.

But investment rules must be designed so as to respect the social agenda. Useful ideas were developed (though never fully agreed) in the MAI negotiations. These ideas were largely overlooked in the public debate, but may be useful in discussions to come. For example:

- Preambular statements of commitment to sustainable development and environmental protection and management.
- A general statement of the government's "right to regulate" in a non-discriminatory way.
- A general exception provision to allow governments to take measures to protect the environment and to protect health and safety.
- A rule to discourage or prevent host governments from lowering environmental or labor standards to attract investments.
- Annexing the OECD Guidelines for Multinational Enterprises to provide a framework for promoting corporate responsibility.

Beyond the substance, mentalities need to change. Academics and officials whose life's work is devoted to investment or trade may be wary of the views and influence of colleagues concerned by health and safety questions or the environment. The reverse is also true. These different intellectual communities need to work more closely together to ensure a coherent result. We are testing this out at present in the work on revising the OECD Guidelines for MNEs and the results so far are encouraging. A more severe test would be the negotiation of binding investment rules.

3. Globalization and Sovereignty

Much of the campaign against the MAI -- and much of the ongoing challenge to free trade -- is an argument against globalization and in defense of national sovereignty. Part of this argument is so emotional it cannot be met by analysis or balanced argument. But we must rise to the challenge of those who feel deeply about these matters and are ready to debate them on empirical grounds by offering sound analysis and better communications.

- Globalization is here to stay. It won't be turned back. But we need to demonstrate that globalization brings many benefits as well as disruptive change and that remedies can be found that are consistent with free and open markets for trade and investment.
- Sovereignty of national governments is indeed challenged by rapid change and globalization. But the careful negotiated use of sovereignty to improve international co-operation may better protect society's interests than defensive reliance on national law. Indeed, public opinion often calls for greater public action to defend human rights, health and safety and the environment in ways that require governments to give up sovereignty to some degree.

From a sovereignty viewpoint, the most controversial feature of the MAI was the investor-state dispute settlement regime which gave foreign investors the right to sue host governments in international courts in ways not available for domestic investors.

4. The Political Process and Public Debate

It is obvious that governments need to consult widely before entering into major international negotiations. The richer the public debate the more likely it is that the subsequent negotiations will be fruitful and avoid unpleasant surprises.
It helps to have clearly identifiable benefits from the negotiations of international rules. The benefits are more difficult to quantify in the case of investment than trade (especially compared with tariff reductions). Hence, developing rules alone may not be sufficient. When agreements will include liberalization commitments requiring national policy changes, it may be necessary, in addition, to reach them in a manner perceived as fair to all parties. More work is needed in this field on both substance and communications.
The claims of some NGOs who take credit for sinking the MAI have alarmed some observers who question their representativeness and their campaigning methods and fear undue interference in future governmental negotiations. But NGOs are just as much part of reality as globalization itself. Indeed NGOs with their Internet hotlines are themselves a globalization phenomenon. The issue is not to invite them to become negotiating partners on the same footing as governments, but they must be given greater access to the process of consultation and dialogue.

OECD's approach is to open the doors wider to public debate: by declassifying documentation whenever possible, and by including civil society more often in seminars and consultations with our committees. Governments are doing their share at national level, too, although there is still some reticence. We are also looking at other ways of improving the participation of NGOs in OECD work.

But there is a counterpart challenge to NGOs: they need to decide whether they want to be part of an orderly public debate, invited to contribute directly to focused discussions on current issues and taken into the confidence of government officials dealing with sensitive policy matters. This is not an easy transition for campaigning NGOs, but it represents a real challenge and opportunity for the NGO community as a whole.

Chapter 18

Making the Case for Multilateral Rules on Foreign Direct Investment

Richard Eglin
Director, Trade and Finance Division, WTO Secretariat

Introduction

Huge opportunities for foreign direct investment (FDI) to expand have appeared in the 1990s, in the wake of world-wide trade liberalization and the growth of global markets for goods and services. Attracting FDI has become the instrument of choice of many developing countries and transition economies to try to integrate faster and further into the world economy, and established host countries (and states and provinces) dig ever deeper into treasuries of investment incentives to ensure they can continue to attract more than their fair share. Annual flows of FDI are growing faster than world trade, and they exceeded $600 billion in 1998. The emerging markets' financial crisis has not put a dent in the euphoria – the fact that FDI by and large stayed put while other foreign capital fled the scene has even added to its luster.

Times have probably never seemed better to make the case for negotiating multilateral rules for FDI. Yet the collapse of the OECD's attempt to conclude an MAI, the apparent lack of interest of the U.S. government in the subject, only lukewarm support from international business, opposition from several influential developing countries, and intense hostility from environmental and development NGOs, suggest that bringing FDI into the WTO may be an uphill battle. Is it indeed, as Jagdish Bhagwati suggested recently, "a bridge too far"?

One of the many lessons to be learned from the OECD's experience is that if there is to be a negotiation on this issue in the WTO, the purpose of creating multilateral rules for FDI must be made crystal clear from the start, and it must appeal to the full range of WTO Members. Otherwise, negotiations risk losing momentum and direction and becoming an easy target for criticism.

It is not enough to suggest that the purpose is to promote the growth of FDI – one would surely expect that to be an important result, but with FDI currently thriving in the absence of any multilateral rules the case is not compelling.

Nor is it enough to point to the efficiency gains of replacing hundreds of bilateral investment treaties (BITs) by one standardized multilateral agreement. For many host governments, the costs of negotiating and implementing BITs seem to be considered insignificant when compared with the flexibility BITs offer to suit individual circumstances and preferences – in times of keen competition among host countries to attract FDI, a dose of discrimination to distort the market in your favor can pay dividends.

Most damaging of all is to lead with the argument that the aim is to increase foreign investor confidence by making the world a safer place for them to do business. Whether or not to include investor rights[1] in a WTO agreement is certainly something to consider, but apart from the fact this infuriates those who believe the "sovereignty" of most developing countries is already under extreme threat without subjugating it further to the interests of transnational corporations, it is of little immediate interest to the vast majority of WTO Members who are at present only host (not home) countries to FDI and are likely to remain so for the foreseeable future.

The case for negotiating multilateral rules on FDI in the WTO in the next trade Round needs to be built on two propositions:

- that doing so would contribute to achieving the WTO's core, trade-related, objectives;

- that it is important for WTO Members to continue developing the "architecture" of the trading system, in a forward-looking way, so as to ensure it is up to the task of helping them coordinate their domestic economic policies effectively.

Admittedly, neither of these propositions are headline-grabbers, particularly in the context of the way in which the Seattle agenda is currently shaping up around high expectations of achieving substantial increases in market access for trade in agriculture, industrial products, and services

Market access has been the traditional core of multilateral trade negotiations, and there is still a big agenda of trade liberalization to tackle. But making that the sole objective of the next Round would be to miss the bigger picture of the role that the WTO ought to be playing in the world economy. Many WTO Members have shown their willingness to continue to liberalize their economies autonomously, over and above their Uruguay Round commitments[2]. Global markets are vastly more open, integrated and competitive today than they were fifteen years ago when the Uruguay Round began, and national economies are increasingly tied together, not only through trade in goods and services, but also through FDI and international capital markets. As economic inter-dependence ("globalization") increases, governments have more need of clear and consistent multilateral rules to help them work out ways to achieve national policy objectives cooperatively. The only rules on FDI they have at their disposal at present are those scattered through various WTO agreements, particularly the rules relating to "commercial presence" in the GATS, but these fall far short of being comprehensive or even, in certain respects, coherent (see Annex).

The case for rule-making on FDI in the WTO now is therefore, in essence, based on anticipating continued global economic integration, with FDI playing an increasingly

[1] Evidently, rights would have to go along with obligations.

[2] Albeit to different degrees. It is primarily the developing countries and the transition economies that have shown most initiative in this regard. The developed countries seem completely wedded to the notion that trade liberalization makes sense only in the context of an exchange of concessions with their trading partners.

important role, and on believing that multilateral disciplines to guarantee non-discrimination, transparency, and a liberal policy environment for FDI can enhance the political, economic and social benefits of that process, in much the same way that they have done for the past fifty years for trade.

One final word of introduction is that making a case for multilateral rules for FDI should not be confused with making a case for FDI *per se*. In conditions of imperfect competition on domestic and international markets, views differ on how FDI may affect the development of individual economies. Notwithstanding the fact that most studies find that on balance the impact is strongly positive, some WTO Members are still persuaded that the costs well outweigh the benefits (or at least that the risks are not worth taking) without a tight corset of discriminatory regulations to control which investors are given market access and how they behave once established. The position of these Members has to be taken as given and respected. Equally, however, they should not stand in the way of others which are interested in exploring whether multilateral rules can assist them in attracting more FDI on more favorable terms than at present, and putting it to better use for their economic growth and development.

This is not a veiled threat to the consensus principle of the WTO. It points rather to the kind of agreement that should probably be in mind from the start -- one that provides opportunities for collective gain from a rules-based system, coupled with opt-out room for those that do not wish for the time being to liberalize their FDI regimes: something along the lines, in other words, of the GATS.

Trade and Investment

The starting-point for building a persuasive case to bring FDI into the WTO is that it would contribute to achieving the WTO's objectives -- that is, increasing trade opportunities through an improved allocation and use of resources and deepening the international division of labor -- and it would broaden and strengthen support for the open, non-discriminatory, trading system.

FDI is a very attractive candidate for inclusion in this respect. It has long been recognized that it represents not only the reallocation of long-term capital but also, and more importantly, a bundle of intangible assets such as entrepreneurship, technology, managerial and marketing know-how, that often are highly immobile internationally when unbundled into their constituent parts. The capital infusion is attractive for host countries, since it is comparatively stable, it has no fixed interest payments associated with it, nor capital repayment, and it contributes directly to productive investment rather than consumption. To a great extent, however, it is the intangible assets of FDI that host countries are primarily interested in, since it is these which can make the biggest contribution to increasing the productivity of their endowed factors of production. These assets are in short supply in many developing countries and transition economies, and FDI represents often the most economical way, and sometimes the only way, of acquiring them.

It is well established empirically that a host country's trade policy stance has a lot to do with the quality of intangible assets that it can hope to secure from FDI. The more restrictive is trade policy, the more likely it is that FDI, if it comes at all, will focus on supplying the domestic market, where it will be protected against competition from imported goods and services and will have only to compete with local firms that fall below world standards of efficiency. In these circumstances, a second-rate bundle of intangible assets (obsolete technology, no export marketing capacity, etc.) is likely to suffice from the foreign investor's point of view, and domestic market saturation will set a limit on the volume of FDI that can be accommodated.

In contrast, host countries with open trade policies can hope to attract FDI both to supply the domestic market (if that can be done more efficiently than by exporting to it) and to export, building on existing comparative advantage. In a competitive environment such as this, a first-rate bundle of intangible assets (state-of-the-art technology and know-how) is likely to be the natural choice for the foreign investor, with a strong presumption that this will be kept up-to-date and that it will be in the foreign investor's interest to encourage its diffusion within the host economy through backward and forward linkages, so as to reinforce its own competitive position. The more the host country offers free (non-discriminatory) access to FDI in conjunction with an open trade policy, the more it can expect to acquire the best FDI available.

Once established, FDI can be expected to play an important role in trade policy formulation, particularly in small host countries where the threat of closure or withdrawal, even from individual foreign investors, can be meaningful. FDI that has been attracted by a restrictive trade policy environment may easily develop into a local protectionist force, arguing for the maintenance of trade restrictions to protect its operations from foreign competition. FDI that has been attracted by a liberal trade policy environment is more likely to press to keep markets open and competitive, and for further liberalization to enhance its competitiveness on export markets and to generate more dynamic growth opportunities in the host economy market.

It seems reasonable to expect that export-oriented FDI will press to keep markets open abroad as well, in its home country and elsewhere. It can create a valuable and powerful constituency in this regard, particularly given the importance of intra-company trade in industries that have diversified their production base globally. In this way one may be able to count on some moderating influence being brought to bear against pressures on home governments to use contingent protection measures, restrictive rules of origin, local content requirements, and the like against overseas competition.

In sum, strong synergies exist between trade and investment. Good trade policies produce good FDI practices, and good FDI policies produce good trade practices. The interests of the multilateral trading system are well served by open markets for FDI and by making foreign investors major stakeholders in the system, and individual Members can capitalize on the benefits they derive from open trade by opening up to FDI.

That said, to make the case for constructing multilateral rules for FDI it still has to be shown that leaving things simply to the market will not suffice, and that multilateral rules are superior to bilateral investment agreements.

Why not leave it to the market?

FDI is thriving today in the absence of multilateral rules, and many governments have been liberalizing their access restrictions on FDI for the past decade or more. Why not leave it to the market, and to "policy competition" between host countries, to drive things to an efficient solution?

Most FDI is trade-related, and much of it is very trade-intensive indeed, either in substituting for imports or in generating exports. WTO Members have a collective, systemic interest in ensuring that FDI complements and reinforces the advantages of an open, market-based trading system.

One reason why it may not be satisfactory to leave it to the market to do that is the existence of market failures and imperfections. FDI operates typically in imperfect market conditions. Given this, certain coordinated policy interventions can be expected to be global welfare-enhancing[3].

Foreign investors appear, on the face of things, to be comfortable in letting the market sort things out. Judging from business surveys, they have an interest in rules that would guarantee open and non-discriminatory access to host countries and that would reduce or better still eliminate performance requirements and the like, but their support seems to be lukewarm at best. The reason is probably that often they are big enough individually to work things out for themselves with host country governments, and/or flexible enough to adapt to or work their way around most policies that are introduced which affect their activities, or in the final analysis free not to invest at all and go elsewhere. It is the first of these which gives rise to most concern from the point of view of the functioning of the trading system. Individual investors that set about using their proprietary assets to raise entry barriers, coupled with host country policies that discriminate in their favor and reinforce their market domination, makes for a potent cocktail of trade restriction and distortion.

It is easy to overlook the fact that there are now some 45,000 foreign direct investors in the world, many of them small and medium-scale enterprises which do not have the bargaining power to overcome entry barriers or adapt to discriminatory treatment. Potentially, this can form an influential constituency through home country governments in favor of multilateral rules to guarantee more equal treatment to compete for investment opportunities abroad.

[3] Coordinating national competition policies at the multilateral level is the most obvious candidate in that regard, and negotiating multilateral rules on competition policy in the next Round would be a natural complement to rule-making on FDI.

A second reason for doubting the power of the market to produce an efficient solution is that "policy competition" is not a one-way street leading to undistorted markets. Many FDI policies are inherently discriminatory and distorting, both to the market for FDI itself and to markets for goods and services in which FDI operates. They can, nonetheless, be packaged in ways that are acceptable to individual foreign investors. Host countries have been reluctant to leave things entirely up to market forces. Many apply access restrictions, incentives, and post-establishment policies, such as performance requirements, to FDI to try to maximize national welfare. Providing certain foreign investors with preferential rights to establish locally, subsidizing their investments, and distorting their post-establishment behavior all undercut the value of market-access commitments for other trading partners.

Of the many specific objectives host countries seek to achieve through their policy interventions, some are common to a large number of host countries and would need to be accommodated in multilateral rules. Concerns that foreign investors operate typically in imperfect markets with a competitive advantage derived from their proprietary assets, for example, coincide with similar concerns about the effect of this on global welfare, and should be addressed through provisions on competition policy. This could probably take care also of concerns about the "largeness" of foreign investors relative to domestic firms, particularly in developing countries, but where necessary it could be augmented by providing leeway for access restrictions in certain sectors or industries, as long as these were applied on a non-discriminatory basis. Similarly, the "foreignness" of FDI prompts host countries to worry about national security and cultural issues, but this could again be addressed through non-discriminatory access restrictions.

FDI policies with potentially the most significant trade restrictive and distorting effects, that warrant being brought under multilateral disciplines, are measures applied by individual host countries to secure a share of the proprietary assets FDI brings with it (e.g., entrepreneurship, technology) or, failing that, to secure a share of the rent. Investment incentives are used to attract these assets to the host country in larger quantities than would otherwise be the case, where FDI is the most economical way of procuring them and/or in times of excess demand to lure investors away from competing host countries. Performance requirements, sometimes linked to investment incentives, are used to force the foreign investor to disseminate the benefits of the assets within the domestic economy and share them with local producers where these do not spillover naturally, or to try to capture part of the rent (although they can easily end up reducing the size of the rent instead through forced inefficiency). Some of these measures have been identified already as being so trade-distorting that WTO rules have been agreed on to discipline them, but the current rules are limited and disjointed. Export performance requirements, for example, are prohibited when linked to a direct subsidy, but not otherwise.

Individual host countries clearly believe they end up with a better solution than the market alone would provide in terms of national welfare as a result of applying these measures, otherwise they would not do it. On the face of things, they should have an interest in bringing investment incentives to attract FDI under multilateral rules, since the

result of competing with each other is simply to bid up the price unnecessarily. One obvious result is that the vast proportion of developing countries do not have the resources to enter the bidding. Those host countries that are successful in attracting FDI this way seem to believe that the price they pay is still modest relative to the benefits FDI brings with it. Much the same could be said, however, about the use of straightforward trade subsidies, in agriculture for example, and the argument in favor of multilateral disciplines is no less compelling when applied to investment incentives.

Host countries that apply post-establishment measures such as performance requirements seem even more reluctant to contemplate bringing them under multilateral rules. They regard them as essential aspects of industrial policy, notwithstanding the weight of empirical evidence that shows these measures are not only costly, but often also ineffective[4]. Nevertheless, these can constitute the most trade-distorting FDI policies of all.

In summary, there is no compelling reason to believe that leaving things up to market forces and to policy competition will lead inexorably towards liberal and undistorted markets for FDI, any more than one might hope that individual WTO Members should recognize the intrinsic good sense of liberalizing their trade policies unilaterally.

Do BITs do it better?

Apart from providing the principal means for home and host countries to come to an arrangement to provide legal protection for foreign investors' assets in host countries, BITs have been used by host countries to apply their post-establishment policy mix. They therefore lock in the current policy-induced trade and investment distortions. That is a good enough reason on its own to reject the notion that they are an acceptable substitute for multilateral rules for anyone other than those benefiting directly from the discrimination.

They have other weaknesses too. One is the cost for all concerned of dealing with so many different agreements. On current count there exist over 1,600 functioning BITs in the world economy; theoretically, it would take more than 7,500 to accommodate all WTO Members. Second, their provisions are not standardized, leading to uncertainty, potentially inconsistent rules, and legal conflicts. Third, most BITs focus only on the post-establishment phase of an investment, and are silent on access rights. They do nothing, therefore, to improve the allocation of investment in the world economy; on the contrary, they tend to distort it further.

There may be a case for BITs continuing in parallel with multilateral rules, as long as they are not inconsistent with them, on the grounds that they can be negotiated and adapted more quickly and they can go further than what might be contemplated at the

[4] Theodore H. Moran, Foreign Direct Investment and Development, Institute for International Economics, Washington D.C., 1999

multilateral level. In this regard, they may prove a useful complement to a basic set of multilateral rules centered on the non-discrimination principle.

What kind of multilateral rules

The case for multilateral rules for FDI should ideally rest on creating a more liberal investment climate, on improving the international allocation of capital, and on creating more secure and predictable conditions for governments and foreign investors in the global economy. In other words, it should be a true investment agreement.

At the present time, this looks like a tall order. The key protagonists have failed to reach agreement in the like-minded setting of the OECD, and chances seem infinitely more remote of selling anything as ambitious as the draft MAI to the one hundred WTO Members that did not participate in the OECD negotiations, and who represent by and large only FDI-importing countries.

The case for constructing multilateral rules on FDI in the WTO needs to be more modest, and based first and foremost on the contribution it would make to improving the trade opportunities of WTO Members and the functioning of the trading system.

First, the benefits WTO Members derive from the steps they are taking to reform and liberalize their trade policies can be increased if they pursue a parallel course of opening up to FDI. The one complements the other. Access restrictions could be negotiated case-by-case through a positive or negative list approach, but where access is to be allowed there is a strong presumption in favor of it being non-discriminatory. Not every FDI project will contribute positively to economic welfare in a directly measurable way, but it is doubtful any government bureaucracy has the means of reliably "picking winners", and the cost of inaccurate intervention is high. Letting foreign investors compete openly to establish in the host country is the way to secure the best quality FDI on the most favorable terms.

Second, investment incentives (i.e. subsidies) applied by the host country not only distort investment flows and penalize other host countries too poor to compete for FDI in this way, they also distort comparative advantage in international trade and reduce trade opportunities for other overseas producers. They should be disciplined more fully than is currently the case under the WTO Subsidies Agreement.

Third, post-establishment policies applied to FDI can distort goods and factor markets domestically and internationally. Some, such as local content requirements, do this so explicitly they are prohibited already by the WTO. Others should be examined with a view to establishing their trade restricting and distorting effects, and suitable disciplines should be created. Generally speaking, there should be a presumption in favor of applying all post-establishment policies to both foreign and domestic investors through a national treatment provision.

Fourth, providing certain foreign investors with preferential rights to establish, subsidizing their investments, and influencing their post-establishment behavior, can all undercut the value of market-access commitments to other WTO Members. The right of these Members to challenge these policies should be recognized under the WTO's integrated dispute settlement procedure.

Admittedly, this package is a modest one. It could never be mistaken for an MAI in disguise, but that is no bad thing. Anything less than the elements listed above would probably not be worth the effort. Nevertheless, the main point is to get a basic framework of FDI rules firmly implanted in the WTO. Further improvement of the rules and liberalization of access for FDI can be part of the agenda of future trade Rounds. The GATS experience shows that agreement on a basic set of rules, coupled with a flexible, country-by-country, approach to liberalization, can prove to be extremely effective, so much so that five years on from agreeing on the GATS rules in the Uruguay Round there are high expectations that deep liberalization in trade in services can be one of the main results of the next Round.

The kind of agreement outlined here has two additional advantages. One is that it should be possible to negotiate and conclude relatively quickly. Some WTO Members which would favor new multilateral rules on FDI in principle, including the United States, have been concerned that finding consensus on rule-making under a "single undertaking" would risk being too time-consuming, and holding up trade liberalization in agriculture, industrial products and services that can be agreed on quickly (a target of three years is widely spoken of). Admittedly there is that risk, but with the experience of the GATS to build on, the kind of agreement on FDI that is suggested here should not pose the kind of technical complications that would require a marathon to sort out.

The second is that it would be possible to build in to the agreement the kind of development dimension that developing countries are seeking in the next Round. Within a common framework of rules on non-discrimination and transparency, and of market access guarantees, there would be scope for developing countries to take account of their financial, economic and development objectives when phasing in liberalization. At the same time, they would benefit from one of the main advantages of locking in their policy reforms under WTO rules, which is to reduce the gap between the perceived and the actual risk of their policies changing so that their liberal policy stance is taken as seriously as it warrants by foreign investors seeking out new locations to invest.

It is worth adding that creating legally-binding WTO rules on FDI can make a singular contribution from the point of view of those worrying about how to restore greater systemic stability to international capital markets.

ANNEX

What exists already in the WTO?

(i) GATS

The integration of investment and cross-border trade in the WTO is most evident in the General Agreement on Trade in Services (GATS). Although the GATS is not an investment agreement as such, it counts investment as one of several different ways of gaining access to a market, through the "commercial presence" of a service supplier in the territory of another WTO Member.

The GATS addresses not only the terms and conditions upon which an investor may enter a market, but also the conditions of operation in the post-establishment phase. With regard to "establishment", an MFN commitment applies, but beyond that the GATS market access concept (Article XVI) permits governments to condition the extent to which (non-discriminatory) entry by foreign suppliers will be permitted.

With regard to post-establishment, by defining "national treatment" as an obligation that relates only to scheduled commitments and not as a principle of general application, the GATS is different from a number of other inter-governmental investment agreements in which national treatment has the same status as MFN. Moreover, the GATS provides for national treatment to be granted only partially, or subject to specified conditions.

The GATS does not contain the kind of investment protection provisions commonly found in many bilateral and regional investment agreements, nor does it include such features as a mechanism for investor-state dispute settlement (it provides, however for state-state dispute settlement).

(ii) TRIPS Agreement

The definition of "investment" in many other inter-governmental investment agreements expressly includes intellectual property.

Although the TRIPS Agreement does not address foreign investment specifically, its provisions on minimum standards for the protection of intellectual property, domestic enforcement procedures and international dispute settlement are directly relevant to the legal environment for FDI.

(iii) TRIMs Agreement

One of the objectives of the Agreement on Trade-Related Investment Measures (TRIMs) is to facilitate investment across international frontiers. It clarifies that certain investment measures contained in an illustrative list (mainly local content and trade-balancing requirements) are inconsistent with the GATT, and requires that they be eliminated.

The TRIMs Agreement provides for a review before the end of 1999, in the context of which consideration is to be given to whether the Agreement should be complemented by provisions on investment and competition policy.

(iv) Agreement on Subsidies and Countervailing Duties

Certain fiscal, financial and indirect investment incentives which are used to attract FDI could fall under the definition of a "subsidy" under the WTO Subsidies Agreement: for example, tax credits, grants loans and equity infusion, and the provision of land and infrastructure at less than market prices. They are prohibited if granted contingent upon exportation of goods produced by an investor, or upon use of domestic over imported goods, and could otherwise be actionable.

(v) The Plurilateral Agreement on Government Procurement

In respect of signatories and covered procurement operations, the GPA requires no discrimination against foreign suppliers nor against locally-established suppliers on the basis of their degree of foreign affiliation or ownership. These provisions date back to the 1979 Tokyo Round Agreement on Government Procurement.