

## CAN INTERNATIONAL TRADE LAW RECOVER?

### WTO DISPUTE SETTLEMENT: CAN WE GO BACK AGAIN?

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The world's twenty-year experiment with a rule-based international trading order is most likely ending. Trade wars are raging again for the first time in two decades as World Trade Organization (WTO) members unilaterally impose and counterimpose sanctions.<sup>1</sup> In Geneva, the WTO Appellate Body, whose existence is essential to the functioning of the WTO Dispute Settlement Understanding (DSU), is on a trajectory to shut down in December 2020. For all the fireworks, however, many commentators retain an optimism that the recent events will be a passing phase and that the world will return to a more law-oriented trading system after the present crisis.

This essay is less sanguine and argues that recent events may have damaged the WTO irreparably. The present departure from enforcement norms is potentially devastating because it goes to the heart of what has provided the WTO with such influence in global economic affairs: the willingness of member countries to accept the WTO legal system as a binding constraint on state action, even when costly domestically. Having abandoned the DSU framework, will countries once again view the WTO rule-based system as mandatory? Or will the WTO become more like other global institutions whose ability to constrain member countries is modest, notwithstanding hard treaty obligations?

To illustrate why returning to a rule-of-law system will be so difficult, this essay describes the WTO enforcement norms and highlights why they are significant to WTO success.<sup>2</sup> It then explains how the current American administration has violated these norms and how other WTO member countries have followed suit in response, leading to widespread disregard for the DSU framework. Finally, it analyzes how the precedent of opting out of the DSU framework may have changed actors' beliefs about whether abiding by the DSU is obligatory and beneficial in the long-term. Once these beliefs have shifted, the political costs of returning to a rule-based system rise, and the likelihood of further violations increases. In short, a world of more power-based bargaining may be returning, and the value of the WTO to all countries will be greatly diminished.

#### *WTO Enforcement Norms*

The strong WTO legal system is unique among global institutions. Often called the WTO's crown jewel, the DSU establishes a rule-based adjudicatory process with compulsory jurisdiction over all WTO member countries,

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<sup>1</sup> For an overview of the various sanctions and counter-sanctions, see Chad Bown & Melina Kolb, [Trump's Trade War: An Up-To-Date Guide](#), PETERSON INST. FOR INT'L ECON. (Sept. 24, 2018).

<sup>2</sup> Even under the current rule-based system, economic power is still relevant at the WTO. Both countries' willingness to bring cases and their ability to bear economic sanctions will depend on their market size. Nonetheless, compared to the pre-WTO General Agreement on Tariff and Trade system, the dispute settlement system is more rule-based because it relies on legal argument, not market power, to resolve trade disputes. See generally JOHN H. JACKSON, [THE WORLD TRADING SYSTEM](#) (2d ed. 1997).

a broad jurisdictional scope over almost all of the WTO Agreements, a right of appeal to the seven-member Appellate Body, and procedures for assessing damages and authorizing retaliation (if a member country maintains its breach of substantive trade rules). However, the influence of the WTO legal system is equally due to the near perfect record of WTO member country compliance with the DSU framework. Not only do the WTO Agreements call for binding dispute resolution, but member countries have followed these rules faithfully, not acting outside of the DSU until recently. It is this acceptance of a constraint by member countries—and the beliefs of subnational actors that these constraints are unavoidable—that has made WTO adjudication such a force in international affairs.

WTO enforcement norms do not require WTO member countries to always comply with *substantive* trade rules. Instead, WTO enforcement norms provide a framework that structures how WTO members address allegations of noncompliance with trade rules.<sup>3</sup> In fact, many of the enforcement norms address circumstances where the respondent country does not ultimately bring its policies into compliance with WTO substantive rules. Thus, even as WTO members did not invariably comply with the WTO substantive rules, compliance with the enforcement norms—the rule-of-law framework that addresses trade policy—was nearly perfect until 2016.

The WTO norms that have effectively governed trade disputes for two decades involve three major principles: acceptance of multilateral adjudication, a prohibition on counterretaliation, and the regulation of remedies.

#### *Acceptance of Multilateral Adjudication*

A core principle of the WTO is that its members must not take any actions regarding alleged breaches of trade rules without going through the WTO dispute settlement system.<sup>4</sup> This means that complaining countries cannot impose sanctions (called “retaliation” or “rebalancing”) until the multilateral adjudicatory system has completed its work.<sup>5</sup> As an example, in the 1990s and early 2000s, the United States maintained that the European Union’s ban on beef treated with growth hormones was a breach of trade rules. Following WTO enforcement norms, the United States waited until it successfully challenged the European Union’s policy before it imposed sanctions. This is particularly notable since, under the General Agreement on Tariffs and Trade 1947 system, the United States had imposed unilateral retaliation for more mild EU restrictions on beef.<sup>6</sup>

Similarly, WTO norms require complaining countries not to impose any sanctions if they lose their cases in disputes settlement. For instance, in an early WTO case, the United States lost its claim against Japan regarding alleged unfair trading practices in the photographic film industry.<sup>7</sup> Although many influential legislators and

<sup>3</sup> In previous work, I have referred to this as the difference between *breaching* trade rules (first order rules) and *violating* WTO enforcement rules (second order rules). It is possible to breach trade rules but still remain within the WTO’s enforcement framework. See Rachel Brewster, *Pricing Compliance: When Formal Remedies Displace Reputational Sanctions*, 54 HARV. INT’L L.J. 259, 300–01 (2013).

<sup>4</sup> This principle is embodied in Article 23 of the DSU, committing member countries to multilateral adjudication of disputes. See [Understanding on Rules and Procedures Governing the Settlement of Disputes](#) art. 23, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401 [hereinafter DSU]. While the DSU has a number of rules and procedures, this rule is part of the fundamental bargain of the WTO system—that the United States would forgo unilateral sanctioning and accept multilateral adjudication of trade disputes if the system were legally binding and capable of authorizing retaliation. See Panel Report, [United States—Sections 301–310 of the Trade Act of 1974](#), WT/DS152/R (adopted Feb. 28, 2000) (describing how Art. 23 of the DSU is a core principle of the WTO dispute settlement system).

<sup>5</sup> The DSU permits arbitration outside of the WTO system if both parties agree. See DSU, [supra note 4](#), art. 25. Parties are also encouraged to settle claims without WTO adjudication. *Id.*, art. 3(7).

<sup>6</sup> See CHARAN DEVEREAUX ET AL., 2 [CASE STUDIES IN US TRADE NEGOTIATION: RESOLVING DISPUTES](#) 51, 72–73 (2006).

<sup>7</sup> See Panel Report, [Japan—Measures Affecting Consumer Photographic Film and Paper](#), WT/DS44/R (adopted Apr. 23, 1998).

industry groups urged the Clinton administration to impose unilateral sanctions on Japan to force its government to negotiate, the United States accepted the decision and dropped its complaint.<sup>8</sup>

### *Prohibition on Counterretaliation*

If a respondent state has lost its case but maintains its breach of trade rules, it must accept retaliation—most often in the form of higher tariffs—and cannot threaten counterretaliation. This aspect of the WTO enforcement norms is critical to preventing trade wars by limiting the right to retaliate to successful complainants. For example, when the United States successfully challenged the EU hormone-beef ban, the European Union refused to change its policy but nonetheless accepted the right of the United States to raise tariffs on EU goods so long as it was in breach of trade rules.<sup>9</sup> Similarly, when Brazil successfully challenged American cotton subsidies, the United States agreed to compensate Brazil, paying US\$147 million annually for several years, instead of threatening counterretaliation.<sup>10</sup>

### *Regulating Remedies*

Member countries must accept the WTO's authority to determine the appropriate level of retaliation. Complaining countries cannot impose additional economic sanctions to increase the pressure on recalcitrant respondents.<sup>11</sup> This principle prevents the escalation of trade disputes by placing limits on retaliation and provides clarity on the price of substantive noncompliance. Returning again to the EU's ban on hormone-beef, American sanctions were not sufficient to change the EU's policy, but the United States did not increase its retaliation above WTO-authorized levels to pry open European markets.

In sum, WTO members' acceptance of these three principles of dispute settlement provided the foundation for the rule-based trading order. Although governments do not always comply with WTO substantive law, countries' commitment (until recently) to these enforcement norms provided a stable and beneficial basis for international economic relations.

### *The Breakdown in Norms*

Recent practice by the United States represents a dramatic departure from major economies' past respect and careful cultivation of WTO enforcement norms. The U.S. actions have additionally had follow-on effects with other global economic powers, including the European Union, China, Canada, and others. There are at least three ways in which American policies have violated WTO enforcement norms and prompted other countries to similarly abandon these norms: Section 301 actions, Section 232 actions, and the block on the Appellate Body appointments.

<sup>8</sup> Paul B. Stephan, *Sheriff or Prisoner? The United States and the World Trade Organization*, 1 CHI. J. INT'L L. 49, 57–58 (2000).

<sup>9</sup> The European Union continued to contest whether its ban was a breach of the Sanitary and Phytosanitary Measures Agreement. Appellate Body Report, [United States—Continued Suspension of Obligations in the EC—Hormones Dispute](#), WT/DS320/AB/R (adopted Oct. 16, 2008).

<sup>10</sup> Randy Schnepf, [Status of the WTO Brazil-U.S. Cotton Case](#) 3–4 (Congressional Research Service, Feb. 11, 2014).

<sup>11</sup> Panel Report, [European Communities—Regime for the Sale, Importation and Distribution of Bananas—Recourse to Arbitration by the European Communities under Article 22.6 of the DSU](#), para. 6.3, WT/DS27/ARB/ECU (adopted Mar. 24, 2000).

### *Section 301 Actions*

In June 2018, the U.S. government imposed unilateral sanctions against China for allegedly engaging in unfair trade practices with regards to intellectual property and state subsidies.<sup>12</sup> The United States filed claims at the WTO regarding some of these allegations, but it left the DSU framework by immediately imposing sanctions on Chinese products (initially US\$50 billion in June 2018, but increased to US\$250 billion in September 2018).<sup>13</sup> This is the U.S. government's first use of Section 301 sanctions outside of the WTO framework since the WTO's creation.

The American action created a situation where the Chinese government had to decide whether to respond quickly or wait for WTO adjudication. Unsurprisingly, given the unilateral nature of the American action, China responded immediately and unilaterally as well, and also applied sanctions without making use of the multilateral system.<sup>14</sup>

Both the American and the Chinese actions violate the principle of multilateral adjudication of trade disputes and the principle that the WTO should determine the remedy (if any). The countries' disregard of these rules has created the most dramatic and rapidly escalating trade war since the end of the Cold War.

### *Section 232 Actions*

The United States has also imposed tariffs on aluminum and steel imports from WTO members, in the name of national security. The American claims of national security justifications for these goods strain credulity, and the tariffs have imposed unexpected economic costs on military allies and adversaries alike.<sup>15</sup> The European Union filed a complaint at the WTO, but also declared that it will treat these tariffs as safeguards, a domestic measure designed to respond to a surge of imports. By reclassifying the tariffs as safeguards, the European Union claims that it can adopt compensatory measures—through higher tariffs—immediately. Although the EU's unilateral measure is an understandable attempt to react in real time to the United States' very broad national security claim, it also violates the WTO enforcement norms that these matters should be subject to multilateral adjudication. Other states, such as Mexico and Canada, have similarly adopted unilateral responses.

### *Block on Appellate Body Members*

Although the U.S. block on the appointment or reappointment of Appellate Body members is not a breach of any rules or procedures embodied in the DSU, the action represents a direct attack on the functioning of the WTO enforcement system. Unless disputing parties agree to a process, without Appellate Body members, the DSU cannot function because it cannot provide the appeal to which WTO countries are entitled under the DSU framework. This means that the dispute cannot be resolved because the case cannot be forwarded to the Dispute Settlement Body, the entire WTO membership sitting in its dispute settlement role, for adoption.<sup>16</sup> The United States thereby

<sup>12</sup> See Chad P. Bown et al., *Trump and China Formalize Tariffs on \$260 Billion of Imports and Look Ahead to Next Phase*, PETERSON INST. FOR INT'L ECON. (Sept. 20, 2018).

<sup>13</sup> See Bown & Kolb, *supra* note 1.

<sup>14</sup> *Id.* Like the United States, China has filed a case but did not wait for WTO adjudication to counterretaliate.

<sup>15</sup> Jennifer A. Hillman, *Trump Tariffs Threaten National Security*, N.Y. TIMES (June 1, 2018).

<sup>16</sup> The Dispute Settlement Body adopts Appellate Body reports by reverse consensus: the report is adopted unless there is a consensus against adoption. This has never happened in practice. Instead of going through the DSU process, WTO members could alternatively agree to arbitration or to waive appeals on an ad hoc basis, but respondent states are unlikely to accept these alternatives.

effectively is forcing other WTO members out of the multilateral adjudication system as well—in most cases, with no alternative dispute settlement system. As former WTO Appellate Body member Jennifer Hillman has noted:

[W]hat everyone expects is that no one will wait for an appeals decision if there is not an appellate body division that can hear the appeal . . . . No country is likely to wait like that. So they start then to take a unilateral action—to go ahead to retaliate or other unilateral action against the country with whom they had the dispute. And the concern is that then that country says, “that action was not lawful” . . . and you end up with the possibility of a mini-trade war in each and every dispute that comes before the WTO dispute settlement system.<sup>17</sup>

These three trade actions have significantly undermined enforcement norms. The United States and other WTO members have eschewed multilateral dispute settlement, have engaged in counterretaliation, and have imposed escalating trade sanctions. Together with the block on Appellate Body member appointments, these actions represent a rejection of the existing enforcement system.

### *Are We Heading Toward a Power-Based Future?*

The departure of WTO member countries *en masse* from WTO dispute resolution does not bode well for the return to near perfect compliance with WTO enforcement norms. Until 2016, the system functioned as a mandatory and binding legal system, even though the WTO never had the power to prevent unilateralism. Nonetheless, member countries abided by the WTO’s enforcement norms and created one of the most effective rule-based legal systems in international law.

Going forward, it will be hard for countries to credibly commit to returning to a mandatory rule-of-law system in good times and bad. First, the precedent of widespread departures from WTO enforcement norms provides national leaders with more freedom in crafting strategies to allegations of WTO breaches. Many complaining countries may no longer wait for the WTO adjudicative process to play out and may respond immediately to other countries’ alleged breaches. In addition, respondent countries may resist dispute settlement and start threatening counterretaliation if complaining countries impose sanctions. The events of the last two years also change the optics of such actions: these strategies seem less like an egregious violation of international law and more like a reasonably available policy option. Furthermore, domestic constituencies may now have less sympathy for claims that WTO rules pose a real constraint on national leaders, thus raising the already high political costs of abiding by WTO rules and procedures.

Second, emerging economies, which have greater long-term concerns about whether the WTO rules are in their national interests, may use the precedent of recent events to resist the application of WTO rules. Countries such as China, Brazil, and India may wish to push back on WTO intellectual property rules or rules that limit a country’s ability to use subsidies broadly. These countries can use the recent precedent to justify departures from WTO enforcement norms and force a return to power-based negotiations on these issues.<sup>18</sup> Such threats may materialize more in future years as the economic power of emerging economies grows.

If the WTO system is not able to return to a rule-of-law system, then the value of the WTO agreements and, perhaps more importantly, the value of the WTO as a forum to resolve trade issues without threats will be notably weakened. The meaning of WTO rules will depend on the disputing countries’ interpretations and the relative power of each country to enforce its view. This creates uncertainty for countries trying to maintain the maximum

<sup>17</sup> See Trade Talks, *America May Be Doing Away with Dispute Settlement*, Episode 60 (Oct. 28, 2018).

<sup>18</sup> Rachel Brewster, *The Trump Administration and the Future of Trade Agreements*, 44 YALE J. INT’L L. ONLINE (Nov. 25, 2018).

level of regulatory discretion in trade policy and yet comply with WTO rules, as well as for private industry trying to make investments for the next decade. More importantly, it will make WTO law apply only to those who do not have the power to resist other country's interpretations.

The path ahead seems like a much rockier road than the last two decades, with the prospect of protracted trade wars and uncertain trade law. The WTO's ability to be an important constraint on states will be substantially weakened. Although the WTO will continue to operate, its influence is most likely to wane as the international trade system returns to more unilateral adjudication and remedies.