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# Artikel – Articles

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# **The WTO's Problematic "Last Resort" Against Noncompliance**

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Ein wesentlicher Unterschied zwischen dem Streitbeilegungssystem der Welthandelsorganisation (WTO) und dem von anderen internationalen Organisationen besteht darin, dass die WTO es einem Mitglied, das Beschwerde eingelegt hat, erlauben darf, den Handel mit einem anderen Mitglied zu beschränken, das Handelsregelungen verletzt und diese Verletzung nicht berichtigt. Beschwerdeführende Regierungen haben diese Grundlage bereits dreimal genutzt, um Strafzölle in Höhe von 100% zu erheben. Wie ist diese Ermächtigung zu erklären? Eine Erklärung ist, dass das beschwerdeführende Mitglied hierdurch in die Lage versetzt werden soll, das Gleichgewicht in den bilateralen Liberalisierungszusagen wieder herzustellen. Die andere ist, dass es sich um Handelssanktionen handelt, die der Durchsetzung der Handelsregeln der WTO dienen. In diesem Artikel werden beide Perspektiven beleuchtet und die Nachteile (und auch einige Vorteile) dieses Mechanismus analysiert. Als Lösungsalternative wird vorgeschlagen, dass die WTO sich verstärkt der öffentlichen Meinung bedienen sollte.

*Keywords:* WTO, Dispute Settlement, Trade Sanctions, Retaliation,  
Compensation

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This article looks at how the World Trade Organization (WTO) addresses noncompliance, and, in particular, at its endorsement of trade-restricting remedies. While the WTO Agreement does not express enthusiasm for such a measure – designating it as the “last resort” – trade rules nonetheless allow an aggrieved government to erect new trade barriers against another country when its government refuses to abide by WTO obligations. So far, the disadvantages of this aggressive approach seem to outweigh the advantages.

The issues discussed here are central to the ongoing WTO negotiations on improving the dispute settlement system. These trade talks are slated to be finished by May 2003. Nonetheless, dispute settlement may get linked to the overall WTO negotiations which are on a longer timetable. As I have

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written previously about the WTO compliance process (e.g., CHARNOVITZ 2001), let me note that this article restructures the analysis, provides more emphasis on economic aspects, and updates the legal developments to include the “Foreign Sales Corporations” case.

This article proceeds in six parts. *Part 1* provides an overview of the WTO’s dispute settlement rules regarding noncompliance. *Part 2* evaluates the experience so far in the authorization and use of trade measures in response to noncompliance. An evaluation requires an understanding of purpose, and *Part 2* points to two purposes – rebalancing and sanction – that could underlie such measures. *Part 3* explores the rebalancing paradigm, and then looks at the impact of the rebalancing remedy for user nations and for the WTO. *Part 4* presents the thesis that the WTO has installed a trade sanction, and then points out the disadvantages of that instrument. Finally, *Part 5* discusses some alternative procedures that the WTO might employ to promote national compliance with trade rules. The conclusion reached is that the WTO needs to better enlist the power of public opinion. A brief *Part 6* concludes.

## **1 Overview of WTO Rules**

Every member of the WTO is directed to “ensure the conformity of its laws, regulations and administrative procedures with its obligations as provided in the annexed Agreements”<sup>1</sup>. Nevertheless, not all governments do so all of the time. One can imagine several reasons why governments might fail to obey WTO rules. For example, a government could be confused as to what the rules are or could lack the capacity to implement them. A government might also make a calculated decision that noncompliance will be more beneficial to it than compliance.

The WTO Understanding on Rules and Procedures Governing the Settlement of Disputes (known as the DSU) was written to deal with disputes arising under the WTO treaty system, and in particular with the problem of non-conformity to trade rules. Private economic actors cannot challenge a violation of WTO rules. The WTO’s compliance system is invocable only by member governments. This limits the flow of complaints, as governments may have many reasons to avoid incurring the political and financial costs of initiating a case. Moreover, a potential complainant is

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1 Marrakesh Agreement Establishing the World Trade Organization, art. XVI:4.

directed by the DSU to “exercise its judgement as to whether action under these procedures would be fruitful” (DSU art. 3.7)<sup>2</sup>.

Given these constraints on challenging noncompliance, it would seem likely that there are more failures to abide by WTO rules than are indicated by counting the cases being brought to the WTO. If the goal of governments was to ferret out all noncompliance, a number of methods could have been used, such as giving the WTO Secretariat or private actors the standing to lodge cases. That those detection methods are not employed shows that governments want to keep the benefits of state-controlled dispute resolution, rather than move to more automatic enforcement.

In the WTO, the settlement of a dispute may be even more important than compliance itself. The DSU states that “a solution mutually acceptable to the parties [...] is clearly to be preferred,” and then notes that “[i]n the absence of a mutually agreed solution, the first objective of the dispute settlement mechanism is usually to secure the withdrawal of the measures concerned if these are found to be inconsistent with the provisions of any of the covered agreements” (DSU art. 3.7). When a dispute arises and a defendant government is found to be violating a WTO obligation, the ideal solution will be for both governments to reach a settlement, or for the scofflaw government to withdraw the offending measure.

If this ideal solution fails to happen, then governments can resort to lower-ranked steps. The first is the “provision of compensation” by the defendant government. This is said to be “a temporary measure pending the withdrawal of the [inconsistent] measure” (DSU art. 3.7). The second is the possibility for the complaining government to suspend WTO concessions or other WTO obligations on a discriminatory basis. The DSU describes that action as the “last resort” (DSU art. 3.7).

The path to this “last resort” has a preliminary phase followed by two discrete steps. In the preliminary phase, the complaining government secures a judgment from a WTO panel or the Appellate Body that the other party is maintaining measures inconsistent with a WTO obligation. This panel or Appellate Body report is then adopted by the WTO Dispute Settlement Body (DSB)<sup>3</sup>. Thereafter, the defending country gets a “reasonable period of time” for implementation as set by agreement or through arbitri-

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2 See MARTHA (2001).

3 The DSB may decide by consensus not to adopt a report, but that has never happened. The DSB is composed of representatives from all of the WTO member countries.

tration (DSU art. 21.3). After expiry of that period, the complaining country may initiate sterner action<sup>4</sup>. The first step is to request authorization to suspend concessions or other obligations at a specified level. The proposed level can be objected to by the defending government, and will then be set through arbitration by the original panel. This arbitral panel is known as the DSU Article 22.6 panel. Following the arbitration, the DSB shall grant authorization to “suspend concessions or other obligations”<sup>5</sup>. To abbreviate this phrase, I call it “SCOO”. The second step is for the complaining government to exercise its option to SCOO which it can do at any time. So far, the governments doing a SCOO have imposed 100% ad valorem tariffs on a list of products from the target country.

The purpose of this article is to consider whether SCOO is an appropriate instrument for WTO dispute settlement. Is it effective? Is it workable for all WTO Members? On the plus side, SCOO is a remedy that complaining governments can single-handedly use when they win WTO cases and the government at fault fails to comply. On the debit side, it seems perverse that the WTO – which was established to promote trade – should encourage new trade restrictions (ALTMAN 2002). Furthermore, insofar as SCOO is perceived as a trade sanction, the ability of the WTO to enforce its rules with sanctions may be destabilizing when other international organizations cannot do so. The next part of the article (*Part 2*) looks at SCOO in practice. An evaluation of SCOO requires a specification of what this action is intended to achieve. Yet SCOO remains enigmatic because of the two different objectives ascribed to it.

## 2 Examining SCOO in Practice

### 2.1 Low Usage and Effectiveness

In the 65 WTO cases that have gone to a final judgment, only six have resulted in the setting of a SCOO level by an Article 22.6 panel<sup>6</sup>. These episodes include the two Bananas cases (the United States and Ecuador

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4 If the defendant government has undertaken any effort at compliance, the parties may go through an additional loop where an “Article 21.5” panel examines the adequacy of measures taken to comply. In one dispute, the WTO Appellate Body held that an Article 21.5 panel determination is a prerequisite to undertaking a suspension of concessions. United States – Import Measures on Certain Products from the European Communities, Report of the Appellate Body, WT/DS165/AB/R, paras. 126–127 (11 December 2000).

5 DSU art. 22.7. The DSB may decide by consensus to reject the request, but that has never happened.

6 Tabulations by the author from data on the WTO website as of 20 September 2002.

complaints against the European Communities), the two Hormones cases (the Canada and United States complaints against the European Communities), the Export Financing for Aircraft case (Canada's complaint against Brazil), and the Foreign Sales Corporations case (the European Communities complaint against the United States). A SCOO has been requested in four other cases which are now in Article 22.6 arbitration over the proper level. Three of those arbitrations have been put on hold (U.S. 1916 Act, U.S. Copyright, and Canada Milk and Dairy), and the other decision is expected this year (Canada – Export Credits for Regional Aircraft). Given the high profile of SCOO in commentary about the WTO, it is striking how few plaintiff governments have sought to use it.

*A priori*, there are two different ways to explain this low usage. One is that the rate of compliance is very high following adjudication, so SCOO is unnecessary (to my knowledge, no study exists of the actual rate of compliance<sup>7</sup>). Such compliance could stem from either law-abiding behavior by governments or a willingness to take corrective action following a threat of a SCOO by the complaining government. In at least one case, the threat to seek a SCOO may have promoted compliance and settlement; this happened in Canada's complaint against Australia on Salmon (PRUZIN 2000). An alternative explanation of the low resort to SCOO is that the complaining governments see little benefit in invoking that remedy.

While it is beyond the scope of this article to test these hypotheses, one can note a few examples where compliance has not occurred, and yet the complaining country did not seek a SCOO. This is what happened in the United States complaint against Mexico on High-Fructose Corn Syrup (ZELAYA-QUESADA 2002). Another example was Bananas, where plaintiff governments Guatemala, Honduras, and Mexico took no further action after winning their cases.

In the five<sup>8</sup> cases where a SCOO was authorized, the complaining government actually performed the act in only three instances. This happened in Bananas when the United States raised tariffs on the European Communities (EC) and in Hormones when the United States and Canada raised tariffs on the EC. For example, in Bananas, the United States imposed 100% tariffs on a list of products that included, among others, hand bags

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7 A former legal adviser in the WTO Secretariat has observed that "many" disputes have "been stranded against the wall of noncompliance" (PAUWELYN 2000, p. 338).

8 Although the Article 22.6 arbitration decision in Foreign Sales Corporations was announced in August 2002, a SCOO has not yet been authorized by the DSB.

and electrothermic coffee and tea makers. In *Hormones*, the United States' list included Roquefort cheese and foie gras among others, and Canada's list included cucumbers and gherkins, among others (MURRAY 1999). Given the high profile of SCO, it is striking that the granted authority went unused in 40% of the episodes.

What might explain this non-utilization? One possible explanation would be that the mere threat of a SCO led to compliance. Yet in the two episodes so far where a SCO grant was not used – Bananas (Ecuador) and Aircraft (Canada) – the compliance achieved was incomplete or non-existent. Perhaps a better explanation of the non-usage of SCO is that the complaining government was dissuaded by the high cost it would entail in carrying out the suspension.

So if a very credible threat to SCO (i.e., after the WTO authorizes it) has not led to compliance, was there a more favorable result from the SCO itself? No such impact can be seen. The first three times that SCO was used failed to elicit compliance. In *Hormones*, the United States and Canada continue to impose 100% tariffs. In Bananas, the SCO was lifted by the United States in 2001 following a settlement in which the EC agreed to attain a WTO-consistent system in 2006, and in the meantime its continued non-conformity with WTO rules was to be sanctified through two waivers<sup>9</sup>.

Of course, promoting compliance is not the only metric by which to evaluate a SCO. One can also look at whether it promotes a positive solution to a bilateral dispute. In Bananas, the EC's eagerness to reach a settlement was probably increased by the nettlesome SCO by the United States for 28 months, and by the threat that Ecuador would SCO.<sup>10</sup> But beyond Bananas and Australia Salmon, the role of SCO in encouraging settlement is not salient.

## 2.2 Rebalancing

Although SCO may not manifest much effectiveness at promoting compliance or settlement, there is one more metric that is relevant. Many observers see SCO as an instrument of self-help that allows the complain-

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9 The two waivers were granted in 2001 at the WTO Ministerial conference in Doha.

10 CHI CARMODY wrote recently that the Bananas settlement "indicates that sanctions have some real value" (CARMODY 2002, p. 320).



ing country to cure the trade injustice it has suffered. In other words, by undoing prior trade concessions or commitments that the complaining government gave to the wrongful government, the complaining government restores the bilateral balance that existed prior to the breach. I call this the “rebalancing” paradigm, although one should note that the term “rebalance” is not in the DSU. Rebalancing is consonant with the bilateral orientation of the DSU in which a complaint is raised by one WTO member about the actions of another. Yet rebalancing does not fit well when trade obligations are viewed as being owed to the entire WTO community.

A major doctrinal problem with the rebalancing paradigm is that under WTO rules, rebalancing alone is not a satisfactory solution to a trade dispute. The DSU makes clear that compensation and SCOO are both “temporary measures”, and that neither is preferred “to full implementation of a recommendation to bring a measure into conformity with the [WTO] covered agreements” (DSU art. 22.1). Furthermore, the DSU underlines that “Prompt compliance with the recommendations and rulings of the DSB is essential” (DSU art. 21.1), and states that the DSB will continue to keep instances of SCOO “under surveillance” if the defending government has not brought the WTO-illegal measure into conformity (DSU art. 22.8). Thus, the problem caused to plaintiff Country P by defendant Country D’s violation of WTO rules cannot be fully corrected by allowing P to do a SCOO on D. Ultimately, under WTO law, D has an obligation to comply<sup>11</sup>.

It is tempting to assert that Countries P and D would both be better off if D complies with WTO rules, yet the reality may be more complex. Country D violates WTO rules because someone in authority has calculated that noncompliance offers more homeland benefits than compliance. A rich literature in game theory exists on why D might defect from an agreement, and how P might respond. Looking only at P’s unitary interest, a tit-for-tat response might be a strategically wise response.

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11 This is my opinion. The issue is not settled in WTO law and has advocates on both sides. For example, CHRISTINE GRAY argues that compensation is not an alternative to performance (GRAY 2000, p. 411–412). ALAN SYKES argues that paying expectation damages is a permitted alternative to specific performance (SYKES 2000, p. 350, 357).

## 2.3 Should the WTO Use SCOO?

This article addresses a different question – viz., whether the WTO treaty should utilize SCOO as the last resort against noncompliance. The answer will depend on the role that SCOO is expected to play.

Two purposes are commonly suggested: First, SCOO can rebalance the trading relationship between the complaining and defending governments in order to restore the economic equilibrium embodied in the original WTO deal (that has been broken)<sup>12</sup>. Second, SCOO can help enforce WTO rules by inducing compliance. Although the term “enforce” is not in the DSU, it does appear in the dispute section of the General Agreement on Trade in Services (GATS), which is titled “Dispute Settlement and Enforcement” (GATS art. XXIII).

The next two parts of the article will examine SCOO in relation to these two distinct purposes. *Part 3* will consider the usefulness of SCOO in rebalancing a trade relationship. The article suggests a need to look beyond the bilateral equilibrium to consider whether SCOO provokes disequilibrium in third countries and in the rule-based trading system. Next, *Part 4* will examine SCOO as an instrument of enforcement, and point out that it may not be coercive enough to induce compliance. For some analysts, this implies that the WTO should be given trade measures with greater bite. This article takes the opposite view and suggests that the WTO abandon the use of trade coercion to enforce its rules.

## 3 SCOO As Rebalancing

On the assumption that the objective of SCOO is to rebalance the bilateral exchange of concessions, *Part 3* looks at two issues. First, is rebalancing good for the plaintiff country doing it? Literal trade rebalancing is presumably not the end, but rather a metaphor for an economic welfare goal. Thus, this inquiry looks at the economic effect of SCOO on the user. Second, is rebalancing good for the WTO system? This inquiry looks at external effects beyond the country doing the SCOO.

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12 ALAN SYKES argues that the key equilibrium is political, not economic. In his schema, a WTO violation in the United States will disappoint foreign stakeholders and lead to a reduction in political support to the foreign government. In response, the foreign politicians will order a SCOO on the United States in order to reap new political support at home (SYKES 2000, p. 354).

The VIENNA CONVENTION ON THE LAW OF TREATIES (art. 60.2) provides that a party “specially affected” by a material breach may invoke it as a ground for suspending the operation of a multilateral treaty in whole or in part in its relations with the defaulting state (SETEAR 1997). The remedy provisions in the General Agreement on Tariffs and Trade (GATT) of 1947 and the remedy provisions in the DSU (which are modeled on GATT Article XXIII) reflect the principle from the law of treaties that a party affected by a breach can suspend its own obligations under a treaty in response. For instance, the DSU employs the term “breach” of the rules (DSU art. 3.8).

In addition to its presence in the DSU, the SCOO also appears in the WTO Agreement on Safeguards. This Agreement allows governments to impose protectionist safeguards against imports in certain situations, but then lets the government of the exporting country respond with a SCOO in the GATT that is substantially equivalent to the lost exports (Safeguards, art. 8.2). The Safeguards SCOO is clearly based on rebalancing (rather than rule enforcement). While I wanted to take note of this provision, I will not discuss Safeguards further.

As pointed out in *Part 1*, the only SCOO implemented so far in the DSU is a 100% tariff. Therefore, the evaluation will start with that remedy, and then in *Part 3.2*, other remedies will be considered. Note that a 100% tariff is unlikely to be achievable merely by a suspension (or snap back) of an actual tariff concession. Tariffs that high were rare even in the days before multilateral trade agreements.

### 3.1 Tariff SCOOs

What should be the benchmark for evaluating the domestic benefit of a 100% tariff in response to noncompliance? One possibility is that the victim country is made whole prospectively<sup>13</sup>.

The problem with this goal is that the DSU sets the level of SCOO to be “equivalent to the level of nullification or impairment” (DSU art. 22.4).

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13 DSU remedies are generally not retrospective. Although some commentators refer to the Article 22.6 arbitration as an award of “damages” (see MOSOTTI 2002), the use of this term is misleading in a WTO context because the DSU remedy is not backdated to the commencement of the breach. Thus, full restitution is not achieved. The forward-looking nature of WTO relief gives governments an incentive to drag out DSU processes (BÜTLER and HAUSER 2000, p. 528; HORLICK 2002, p. 637–640).

In other words, if Country D has impaired its imports from Country P by EUR 100 million, then P can reciprocate by impairing its imports from D by EUR 100 million. This action will achieve a rebalance of two-way trade though at a lower level.<sup>14</sup> Because the EUR 200 million in bilateral trade generated economic gain in P (otherwise the trade would not have occurred in the first place), some portion of that gain is not recovered when P imposes the 100% tariff (ANDERSON 2002, p. 128–129). Thus, SCOO cannot render the victim country whole, even prospectively.

Another benchmark for appraising SCOO is whether it improves the welfare of the plaintiff country *at all* as compared to doing nothing in response to its loss of trade benefits. The possibility that a SCOO might make the country employing it worse off seems to be contemplated in DSU rules which permit, but do not require, the country gaining SCOO authority to actually invoke it. In effect, the WTO is saying, “we will grant you authority to SCOO the scofflaw country, but it is up to you to decide whether that is worthwhile”. Prohibitive tariffs could cause net harm to the country using them for several reasons (BARFIELD 2001, p. 130). Such tariffs can raise prices for consumers and distort choices. Tariffs can also weaken the competitive fiber of the newly protected domestic industries and can encourage rent-seeking political behavior.

The experience discussed in *Part 2* shows that SCOO will sometimes look uninviting. Ecuador did not use a SCOO against the EC, and Canada did not use a SCOO against Brazil. Perhaps what happened is that Ecuador and Canada calculated that the potential gains from SCOO were less than the overall political and economic costs. Or perhaps Ecuador and Canada saw no economic benefit to the SCOO.<sup>15</sup> In the first Article 22.6 arbitration in Bananas, the panel disclosed that it had encouraged the two parties to negotiate, “as the suspension of concessions is not in the economic interest of either of them” (WT/DS27/ARB, para. 2.13). This is a sober assessment of what some analysts consider the most impressive feature of the DSU.

Does the fact that two large states (Canada and the United States) have used the SCOO necessarily show that it was beneficial to them? Nor-

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14 This is a rebalance by definition ignoring second order effects.

15 It is interesting to note that Ecuador did not specifically seek to include trade in goods within its SCOO. In response, the arbitral panel reminded Ecuador to consider more carefully the option of suspending tariff concessions on consumer goods. See WTO WT/DS27/ARB/ECU, 24 March 2000, paras. 100–101. Thus, it is possible that even when a plaintiff country doubts that raising its tariffs would be in its interest, the WTO would insist that it do so, if it wants to SCOO.

mally, one might assume that a state would act in line with its self-interest. Yet in trade policy, that assumption is unwarranted. Indeed, the WTO is based on the notion of discouraging countries from using self-defeating trade restrictions (TUMLIR 1985, p. 12–13; KRUGMAN 1997, p. 113; FINGER and WINTERS 2002). In instances of SCO, it could be that the plaintiff Country P's decision-making is flawed due to public choice biases. In other words, P may act at the behest of frustrated exporters who want revenge even though the imposition of 100% tariffs ends up hurting P's economy more than helping it.

The other issue in evaluation looks at the external effect of SCO on other countries and the WTO system. Even while endorsing SCO, the DSU directs governments to “take into account [...] the broader economic consequences” of the requested SCO (DSU art. 22.3(d)). Certainly, the SCO can hurt third countries. For example, if Country P imposes a prohibitive tariff on widgets from Country D, then a supplier of widget components in third Country T could get hurt. Under DSU rules, P owes no duty to T to avoid harming it. Because P may choose any product it wants to bar from D, the T countries will (at the very least) bear costs of insecurity and unpredictability. Yet one of the purposes of the DSU is “providing security and predictability to the multilateral trading system” (DSU art. 3.2). Recently, the EC evinced candor in admitting to the WTO that “the authorization to suspend concessions runs against a basic principle of the WTO, i.e., predictability of the trading system” (EUROPEAN COMMUNITIES 2002, p. 4).

In the WTO rebalancing paradigm, the purpose is not to punish or coerce the country at fault, but rather to enable the victim country to recover by re-leveling its trade. Since there is no intent to punish, the possibility that a SCO may hurt victims in the receiving country could count as a disadvantage. Under DSU rules, the government using a SCO lacks any duty to mitigate the economic or social consequences to private economic actors. Many of these persons will be innocent of any responsibility for the WTO violation that underlies the case.

It is interesting to note that the VIENNA CONVENTION provisions for suspending a treaty in response to a breach “do not apply to provisions relating to the protection of the human person contained in treaties of a humanitarian character [...]” (VIENNA CONVENTION, art. 60.5). Thus, the law of treaties recognizes the deontological problem of suspending treaties

when that action will cause collateral damage to human persons. So far, the law of trade does not.

Another issue is the fairness of SCOO among countries of different size. It is sometimes suggested that a SCOO to rebalance is not workable for smaller economies (e.g., BISHOP 2002, p. 17). As a generality, this seems false. There would probably be few circumstances when the country doing the SCOO is dependent on the defendant country as the only possible source of its imports. Of course, substituting suppliers will generate costs for the plaintiff country. Furthermore, a smaller country would be handicapped in levying a non-prohibitive tariff increase in the hope of shifting the costs to the exporter.

Consider also the issue of how SCOO affects public support for freer trade. The traditional disinterest of GATT/WTO in public opinion was shattered by the fiasco at the Seattle Ministerial Conference in 1999. Today, few would deny that increasing public understanding of the benefits of trade is an appropriate objective for the WTO. Indeed, the WTO Doha Declaration states a commitment “to communicate the benefits of a liberal, rules-based multilateral trading system” (WTO 2001b, para. 10).

What is being communicated to the public when the WTO authorizes a 100% tariff SCOO? Seemingly, the message is that a country can improve its welfare by barring imports, and that the WTO is oblivious to whatever collateral damage is suffered as a result. Such messages cannot possibly strengthen public support for a liberal trading system.

In summary, the value of a tariff-based SCOO is far from clear. Yet even if it does have advantages for the user, it has significant disadvantages for the WTO. The SCOO can hurt third countries and innocent individuals. It can also confuse the public as to what the WTO stands for. As GARY HORLICK has pungently put it, “Simply stated, the purpose of the WTO is not to impose 100 percent duties on importers of Roquefort cheese, or other innocent bystanders” (HORLICK 2002, p. 641).

### **3.2 Non-tariff SCOOs**

Although the prohibitive tariff is the only SCOO used to date, the plaintiff government winning a case is free to propose a plan to suspend any of its WTO obligations. For example, in the Bananas case, Ecuador sought

authorization to suspend its GATS commitments on wholesale trade services and to suspend several rules in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). In the “Export Credits for Regional Aircraft” case, Brazil is seeking a SCO in the WTO Agreements on Customs Valuation and Import Licensing Procedures. The SCO proposal from the complaining government is reviewed by the Article 22.6 arbitral panel. In addition to reviewing the level requested, the panel considers whether the sectors chosen are justified under the principles and procedures (for so-called cross retaliation) in DSU Article 22.3.

Non-tariff SCOs can have an assortment of effects. On the positive side, such a SCO may make it easier for a complaining country to avoid shooting itself in the foot. Furthermore, smaller countries may find non-tariff remedies easier to impose (SUBRAMANIAN and WATAL 2000). On the negative side, the non-tariff SCO may cause even more unpredictability than the prohibitive tariff. Furthermore, such a SCO undermines the normative value of the WTO discipline being suspended. For example, if intellectual property rights warrant societal protection, then how can the WTO be so cavalier in permitting Ecuador to flout them? The WTO cannot pretend to be a rule-based trading system when every rule is potentially erasable through a SCO.

#### **4 SCO as Trade Sanction**

Because the DSU does not state an explicit purpose for SCO, uncertainty exists regarding the role of that instrument. In contrast to *Part 3*, which considered SCO as a trade re-balancer, *Part 4* characterizes SCO as an instrument of enforcement used to persuade scofflaw governments to bring their WTO-inconsistent measures into compliance. In a recent speech, the Chairman of the Appellate Body explained that “Our judgments are enforced, not by us, but by the Members of the WTO themselves through the power of economic suasion” (BACCHUS 2002, p. 4). The usual term for such an economic instrument is a “sanction”.

Of course, sanction has another meaning: it can be a punishment (NOSSAL 1989). The punitive connotation of “sanction” is not what is intended here. Moreover, no one argues that punishment is the goal of the DSU. At the international level, sanctions are typically used for persuasion, rather than for punishment. Sanctions approved by the United Nations Security Council do not have punishment as the ostensible goal.

All of the Article 22.6 arbitrators through 2001 have stated that the purpose of SCOOP is to induce compliance. In the first Bananas arbitration, the panel declared that the temporary nature of the SCOOP “indicates that it is the purpose of countermeasures to induce compliance” (WT/DS27/ARB, para. 6.3). In the Hormones arbitrations, the panel declared that it agreed with the Bananas panel that the purpose of countermeasures is to induce compliance (WT/DS26/ARB, para. 40). In the second Bananas arbitration, the panel posited that an “effective” SCOOP should ensure the desired result, “namely to induce compliance [...]” (WT/DS27/ARB/ECU, para. 72)<sup>16</sup>. In the Aircraft arbitration, the panel declared that an appropriate countermeasure “effectively induces compliance” (WT/DS46/ARB, para. 3.44)<sup>17</sup>.

## 4.1 Criticism of WTO

This line of decisions has been criticized by DAVID PALMETER and STANIMIR A. ALEXANDROV. In their view, “The purpose of countermeasures in the WTO is not to induce compliance, but to maintain the balance of reciprocal trade concessions negotiated in the WTO agreements” (PALMETER and ALEXANDROV 2002, p. 647). The authors argue that the arbitrators’ statements (above) are unsupported by the text of the WTO agreement, and that the “induce compliance” standard has “evolved into something the negotiators might not recognize” (PALMETER and ALEXANDROV 2002, pp. 651, 654).

PALMETER and ALEXANDROV are on solid ground in some of their criticism. They are right to question the authoritativeness of Article 22.6 arbitral decisions. Such decisions are unreviewable by the Appellate Body and are not the proper process for an official interpretation of the DSU.<sup>18</sup> The authors are also correct in surmising that some governments may not intend Article 22 to operate as a sanction. For example in February 2001, Brazil’s delegate to the DSB contrasted SCOOP with U.N. Security Coun-

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16 The relevance of the word “effective” is that the DSU limits SCOOP to the same sector and same WTO agreement of the violation unless the winning complaining country considers that such a limited SCOOP would not be “practicable or effective” (DSU art. 22.3).

17 The term “countermeasures” is used in the WTO Agreement on Subsidies and Countervailing Measures (SCM). If the defending government does not withdraw its prohibited export subsidy, the complaining government may seek authorization from the DSB to impose appropriate “countermeasures” (SCM arts. 4.7, 4.10).

18 In my opinion, the DSU ought to be changed to assign the Article 22.6 function to special arbitrators. The original panel does not necessarily have the expertise to carry out this task.



cil sanctions, and denied that the objective of a DSU Article 22 measure is to induce compliance (WT/DSB/M/94, para. 94).

Nevertheless, PALMETER and ALEXANDROV are wrong in their underlying thesis.<sup>19</sup> In analyzing the text of the DSU, the Article 22.6 arbitrators have correctly grasped that SCOO operates as a sanction. The intent to sanction is confirmed in the practice of the most active sender, the United States. In both instances when it utilized a SCOO, the United States did selective targeting across EC countries. For example in the Hormones dispute, the United Kingdom was reportedly kept off the hit list because it had voted against the hormone ban (INSIDE U.S. TRADE 1999, p. 9–10). Such political considerations would not come into play if the only purpose of SCOO were rebalancing. Furthermore, PALMETER and ALEXANDROV put too much weight on the rebalancing tradition inherited from the GATT, and do not fully appreciate the legal transformation toward enforcement that has occurred in the WTO.

## 4.2 Recent Developments

The most recent Article 22.6 arbitration decision confirms that the WTO utilizes trade measures to induce compliance.<sup>20</sup> This is the Foreign Sales Corporations (FSC) case, a complaint by the EC against the United States. Because the United States had failed to withdraw a prohibited export subsidy, the EC was seeking appropriate “countermeasures” pursuant to Article 4 of the Agreement on Subsidies and Countervailing Measures. The arbitral panel awarded the EC the right to block \$4 billion in exports from the United States. In determining its award, the panel concluded that an authorized countermeasure does not have to be equivalent to the U.S. export subsidy’s trade impact on the EC (WT/DS108/ARB, para. 5.30). Since countermeasures are taken against non-compliance, the FSC panel reasoned, such countermeasures are “aimed at inducing or securing compliance with the DSB’s recommendation” (WT/DS108/ARB, para. 5.52). Moreover, the panel stated that “the balance of rights and obligations between Members will only ultimately be properly redressed through

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19 The authors (PALMETER and ALEXANDROV 2002, p. 654–655) cite PAUWELYN’s article in the *American Journal of International Law* in support of their thesis, but apparently overlook PAUWELYN’s statement that the arbitrators were correct in ruling that the purpose of countermeasures is to induce compliance (PAUWELYN 2000, p. 343).

20 World Trade Organization; United States – Tax Treatment for “Foreign Sales Corporations”, Recourse to Arbitration by the United States under Article 22.6 of the DSU and Article 4.11 of the SCM Agreement, Decision of the Arbitrator, WT/DS108/ARB (30 August 2002).

full compliance with the DSB's recommendations [...]” (WT/DS108/ARB, para. 6.9 n. 72). In addition, the panel held that the United States' obligation to comply was owed to every WTO Member and cannot be considered to be “allocatable” across the membership (WT/DS108/ARB, paras. 6.10, 6.28). The panel's logic suggests that if other WTO Members lodge and win an identical case against the United States, they too could receive a \$4 billion SCOO authorization should the violation continue. For all of these reasons, this decision is difficult to reconcile with the rebalancing paradigm.

### 4.3 Recognition of the Sanction

SCOO operates as a sanction because most of the WTO policy community perceives it as such. Consider the following statements which show a common use of the term “sanction” in connection with the WTO:

*Trade sanctions are allowed in cases where compliance isn't there.*  
PASCAL LAMY (2002)<sup>21</sup>

*Either the offending Member can offer “compensation” for the harm done to the trade interests of another Member or the DSB can authorize a level of retaliatory sanctions.*  
WORLD TRADE ORGANIZATION (2001a, p. 10)

*For us, it is clear from the evidence that the United States was trying to impose trade sanctions – the ultimate remedy under WTO law – against listed imports from the European Communities.*  
WTO PANEL REPORT (2000, para. 5.13)<sup>22</sup>

*Four years of US sanctions have failed to get the EU beef ban lifted. If anything, the measures have caused European attitudes to harden.*  
FINANCIAL TIMES [editorial] (2002)<sup>23</sup>

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21 YERKEY (2002, A-12).

22 United States – Import Measures on Certain Products from the European Communities, Report of the Panel, WT/DS165/R (17 July 2000). This was a complaint by the EC regarding the U.S. government's SCOO in the Bananas dispute.

23 “Retaliation and Trade”, FINANCIAL TIMES, 3 April 2002: 14.

*[...] [C]ountries held to have broken WTO rules must either change their policies so as to comply, or pay compensation to the injured party, or face trade sanctions.*

THE ECONOMIST (2001)<sup>24</sup>

*The WTO's TRIPS agreement can be enforced through the integrated dispute settlement system. This effectively means that if a country does not fulfil its intellectual property rights obligations, trade sanctions can be applied against it—a serious threat.*

U.N. DEVELOPMENT PROGRAMME (1999, p. 67)

*Governments and others perceive that the WTO is particularly important as an institution for establishing trade rules which are binding. This is because of the generality of its scope and the fact that it has the power to impose sanctions that may significantly affect national policy.*

COMMISSION ON INTELLECTUAL PROPERTY RIGHTS (2002, p. 157)

*Finally, the WTO has teeth. Through its dispute-settlement system, countries can challenge each other's policies and, in the event of non-compliance with WTO rules, demand compensation or impose trade sanctions.*

OXFAM (2002, p. 251)

*The Dispute Settlement Body [...] adopts the rulings of the panels and the Appellate Body, and authorizes sanctions for noncompliance.*

FRIEDER ROESSLER (2001, p. 323)

*In this respect, an interesting lesson may be learned from another case of “collateral damage” from interstate trade sanctions, the losses incurred by European exporters on the U.S. market as an indirect consequence of the Bananas and Hormones disputes [...].*

AUGUST REINISCH (2001, p. 869)

While demonstrating the widespread view that SCOO is a “sanction”, the above quotations do not clearly state that the purpose of SCOO is to induce compliance, rather than to rebalance. Of course, those using the term “sanction” are surely aware of its connotations.<sup>25</sup>

24 “Who Elected the WTO?”, THE ECONOMIST, 29 Sept. 2001: 26.

25 Nevertheless, some proponents of the rebalancing paradigm, such as ALAN SYKES, refer to a SCOO as a “sanction” (SYKES 2000, p. 351–352).

Increasingly, analysts are drawing an explicit conclusion that the goal of a WTO sanction is to induce compliance. Consider the following:

*[The Ecuador Article 22.6 arbitration decision] can be viewed as a formal recognition of the post-WTO tendency to view retaliation as a sanction designed to induce compliance by economic pain, rather than the original view of retaliation as a form of temporary compensation for an imbalance of benefits.*

ROBERT E. HUDEC (2002, p. 89)

*Under the GATT, one of the primary purposes of retaliation was to allow for a restoration of the “balance of concessions” between the complaining and defending parties under the Agreement. [...] Under the WTO, however, it is clear that the main objective of the complaining party is not a restoration of the balance of concessions, but is rather to induce the defending party to comply with its obligations.*

BRENDAN P. MCGIVERN (2002, p. 144)

*Under the WTO regime, the losing party remains under multilateral surveillance and induced to ensure WTO-compliance under authorized sanctions.*

NORIO KOMURO (2000, p. 56)

*Within the proper ambit of the WTO system, such as the trade in goods, retaliation should be considered as forcing Member States to comply with the panel or Appellate Body’s judgment.<sup>26</sup>*

AKIRA KOTERA (2002, p. 920–921)

These statements point to the conclusion that SCOO has become a trade sanction, even if that result was not intended by all of the Uruguay Round negotiators.

#### 4.4 Evaluating the Sanction

The effect of SCOO on the country doing it is the same regardless of whether the purpose is rebalancing or sanction. Purpose matters, however, in assessing the external effects on other countries. When viewed as

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26 KOTERA goes on to say that “outside this ambit, retaliation can be a final measure to restore the balance of trade benefits among Member States”. In KOTERA’s view, the proper ambit of the WTO is trade in goods, trade in services, and intellectual property rights.

a sanction, the sending country wants SCOO to change the behavior of the defendant country by getting it to withdraw the measure that is at issue in the trade dispute. Is that a viable strategy?

ADAM SMITH was perhaps the first economist to examine this situation, and his analysis remains relevant. In *Wealth of Nations*, SMITH looked at the policy of “revenge” or “retaliation” against a foreign nation (that restrains importation) using the instrument of “like duties and prohibitions”. SMITH advised that “There may be good policy in retaliations of this kind, when there is a probability that they will procure the repeal of the high duties or prohibitions complained of”. Then he went on to warn that “When there is no probability that any such repeal can be procured, it seems a bad method of compensating the injury done to certain classes of our people, to do another injury ourselves [...]” (SMITH 1776, Book 4, Chap. 2).

Based on SMITH’s analysis, the key variable is the probability that SCOO will procure the repeal of the WTO-illegal measure. As *Part 2* indicates, the success rate of the three instances of SCOO was zero. This low rate of success can perhaps be attributed to the fact that the DSU limits the size of the SCOO to the “level of nullification or impairment” (DSU art. 22.4), and that level cannot cause enough pain to induce compliance (PAUWELYN 2000, p. 344)<sup>27</sup>. So SMITH and anyone else would have good reason to doubt the merits of SCOO.

Yet the question is not that easy. SMITH wrote in the context of an anarchic international system, but today there is a law-based WTO. Just because the EC refused compliance in Bananas and Hormones is no reason to conclude that SCOO (or the threat of SCOO) lacks any capacity to correct governmental misbehavior. As PETROS MAVROIDIS has explained, a legal system needs to possess means to enforce what has been agreed, and in the WTO, “implementation will depend on the persuasive power of counter-measures” (MAVROIDIS 2002, p. 168). This persuasive power is not just on the nations being hit with the sanction, but also on the rest of the WTO governments, which are constantly assessing the incentives and disincentives to comply. Thus the sanction, merely by being available, may

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27 Assuming that a country benefits from violating WTO rules, the SCOO is sized to take away that benefit. The scofflaw country is now even. It will be indifferent to maintaining the status quo versus complying and having SCOO lifted. That is why many commentators have suggested that the SCOO needs to be more costly in order to be an effective sanction.

provide systemic benefits to the WTO as governments bargain in the shadow of the SCOO.

The theory of the SCOO seems to be that threats directed at exporting companies in the country violating WTO law will catalyze those companies (and associated stakeholders) to demand that the domestic government come into compliance with the provision of the WTO being violated. To date, such private sector coalitions for compliance have not noticeably materialized. Yet the potential for their emergence is clear.

Although sufficient data points are lacking for an evaluation of the impact of SCOO on compliance generally, some negative features of SCOO can be seen now. One problem is that the goal of inducing compliance is nearly impossible for small and perhaps medium size economies (SPEYER 2001, p. 277; STEINBERG 2002, p. 347)<sup>28</sup>. Ecuador cannot effectively sanction the EC. Recognizing this inequity, a coalition of nongovernmental organizations, led by SAVE THE CHILDREN, is calling for WTO negotiators to “explore the possibility of a system which is not ultimately based on the threat of trade sanctions [...] given that this system is of no practical relevance to the majority of developing countries” (SAVE THE CHILDREN 2002, para. 11).

The SCOO is also problematic because it has a destabilizing effect on the WTO and other international organizations. The problem is twofold: First, because the WTO is the only global institution to use trade sanctions for enforcement (aside from the Security Council)<sup>29</sup>, there is pressure to take issues from other fora and insert them into the WTO. Indeed, intellectual property came into the WTO because the World Intellectual Property Organization did not have a potent enforcement tool (FELGUEROSO 2002, p. 172). Second, the lack of sanctions in other regimes makes them feel inferior to the WTO and leads to resentment. JOEL TRACHTMAN has wryly called this “penance envy” (ALVAREZ 2002, p. 2).

The urge to add new WTO issues – like labor standards or human rights – springs from the view that the WTO has teeth that other treaties lack. As

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28 A new draft study by SIMON J. EVENETT introduces the concept of bilateral “enforcers”, that is, nations which import enough of a WTO defendant country’s exports so that there is a potential for trade sanctions to induce adherence to commitments. EVENETT views his analysis as “casting doubt on any sweeping claims that developing countries as a rule are more exposed to sanctions from WTO dispute settlement than industrialized economies” (EVENETT 2002).

29 Many treaties employ trade controls (e.g., environment, narcotics, and fisheries), but only the WTO authorizes discretionary trade measures against unrelated products.

MARTIN WOLF explains: “Nowadays, however, commercial interests are no longer alone in recognizing what they can gain by employing WTO-authorized sanctions against imports. A rich assortment of activists have realized the potential value of the WTO’s enforcement mechanisms for their own varied purposes” (WOLF 2001, p. 195). A similar argument is offered by WILLIAM A. KERR who explains that the “WTO, with its ability to impose trade sanctions, is a coveted prize that may be open to capture” (KERR 2000, p. 103). Another study notes the phenomenon of international “venue shopping”, and concludes that “Because of its ability to levy trade sanctions, the WTO frequently has been the venue of choice” (SUTHERLAND ET AL. 2001, p. 105).

If SCOO is viewed as a sanction, then there is no principled reason why the WTO Agreement should have trade sanctions for enforcement when other treaties do not. For example, the Kyoto Protocol on Climate Change will have enormous problems of compliance, at least as difficult as those in the WTO. Should trade sanctions be added to it? Some environmentalists have learned a lesson from the WTO and are already suggesting that environmental treaties could be given “sanctioning powers similar to WTO’s” (FRENCH 2002, p. 181). The response that civil society groups think they are hearing is that only the WTO is important enough to have trade sanctions. This attitude that the trading system stands above other international law is unlikely to generate public support for the WTO.

## **5 Improving the WTO Compliance System**

Any treaty with numerous and complex obligations needs a compliance system. As compared to the GATT, the WTO was designed to be more judicial in the determination of noncompliance and in the automatic imposition of a remedy. On the whole, the DSU has much to commend.

Nevertheless, the enforcement approach in the DSU is flawed. It lets scoff-law governments avoid liability for too long and has little deterrent effect. It provides insufficient relief to injured countries and to the injured economic actors within. It promotes the SCOO remedy that hurts innocent individuals and confounds the public. SCOO also destabilizes the WTO’s relationship with other agencies of global governance.

Many analysts have examined the problems of DSU enforcement and have offered varying prescriptions. Let me briefly note a few here: JOOST

PAUWELYN agrees that the purpose of SCOO is to induce compliance, but laments that the DSU has “not been paired with a strong enough enforcement mechanism” (PAUWELYN 2000, pp. 338, 343–344). PAUWELYN points to procedural changes that would (1) allow all injured WTO Members to implement a collective SCOO against the defendant country, (2) require the defendant government to give trade-liberalizing compensation to the plaintiff government, or (3) require pecuniary (i.e., monetary) compensation (PAUWELYN 2000, p. 345–46). DANI RODRIK would require all WTO Members to join in the SCOO if the winning plaintiff is a developing country (RODRIK 2001, p. 33). KYM ANDERSON suggests that “a greater dose of retaliation could speed up the process of becoming compliant [...]” (ANDERSON 2002, p. 133). CLAUDE BARFIELD would have the WTO impose a monetary fine on the losing defendant (for distribution to the injured domestic industry) or require the defendant government to institute trade liberalization of value to the complaining country. BARFIELD explains that “Either method is feasible and would be superior to the use of trade sanctions” (BARFIELD 2001, p. 131). JAGDISH BHAGWATI suggests that the WTO “encourage the payment of monetary damages that reflect not the value of trade affected but the gains from trade lost (which is only a small fraction of the sales)” (BHAGWATI 2002, p. 17). PALMETER and ALEXANDROV would not change the DSU, but rather call for an epiphany that SCOO is not a sanction.

Much can be said about each of these recommendations, but in the limited space here, let me make a few brief observations. Replacing SCOO with trade liberalizing compensation is a good idea, yet none of its proponents has explained how to operationalize it. Just as the WTO has no power to compel compliance, it has no power to compel compensation. (The SCOO works because it is self-implementing by the plaintiff government.) A monetary fine is another good idea, either paid to the WTO or to the complaining government. In contrast to SCOO, the fine gets the equities right, and makes the defendant transfer a true benefit. In principle, the payment of a fine could be enforced through a domestic court under longstanding treaties dealing with the collection of arbitral awards. Nevertheless, it is doubtful that governments are willing to agree to such a process. The United States is probably not willing, particularly in view of the controversy over the possibility of financial compensation being awarded in arbitrations pursuant to Chapter 11 (Investment) of the North



American Free Trade Agreement (see LERNER 2001)<sup>30</sup>. PALMETER and ALEXANDROV's approach of denying that there is a sanction could eliminate the problems with SCOO discussed in *Part 4* above, but would do nothing about the problems with rebalancing discussed in *Part 3*.

In my view, SCOO is an unwise remedy whether implemented as a tariff or as a suspension of a WTO rule. I would eliminate it as the WTO's "last resort". And yet I recognize that this will not happen over the next decade.

It would be possible, however, for governments to add another resort in the DSU. Specifically, the WTO could improve its implementation process in order to put greater pressure on governments to comply or settle. While one source of this pressure could be other WTO Members, I contend that a more important source of influence is public opinion within the defendant country to encourage more self-responsibility for compliance.

In a democratic country, convincing the public that its government should honor WTO legal obligations may help to secure implementation. Over many years, ROBERT E. HUDEC has called attention to the nexus between domestic politics and international agencies. For example, in 1993, HUDEC wrote that "The existence of an international legal institution provides a focus for the continual education, expansion, and refinement of the domestic political forces who favor it, and growing domestic political support in turn makes the institution more effective" (HUDEC 1993, p. 359). Recently, EDITH BROWN WEISS has pointed to the constructive role that the public could play in WTO enforcement. Drawing a lesson from the environment regime, WEISS calls for "strengthening a culture of compliance in the public with trade agreements" (WEISS 2000, p. 471). On some trade issues, she states that "efforts need to be made to build public support for the dispute settlement process and for compliance with the decisions" (WEISS 2000, p. 471). WEISS recommends techniques of transparency and sunshine.

Certainly, the WTO could use more transparency and sunshine. At present, WTO panel and Appellate Body hearings are held out of the view of the public. When the DSB debates a panel report and examines compliance efforts at monthly sessions, these sessions are closed to the private

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30 It is interesting to note that the new U.S. Trade Act of 2002 authorizes a \$50 million monetary fund for the payment of settlements in WTO disputes. PUBLIC LAW 107-210, Section 5201.

sector and civic society. Thus, the potential power of public opinion within the outlaw country is left untapped. Instead of the current practice where WTO disputes are considered in closed rooms with only government delegates and WTO staff observers, all of the DSU bodies should hold most of their sessions in public as national courts do.<sup>31</sup> Whenever a government fails to comply, the DSB should convene a public hearing where the government would be asked to explain its delay, and other governments and concerned private economic and social actors could respond to those excuses. The public likes this sort of adversarial theatre, and the ensuing embarrassment could elicit compliance.

Such a discursive process might have helped in the Bananas case where the European public was probably not aware of the numerous harms being caused by the noncompliance. It is interesting to note that the value of a public hearing in trade was pointed to as early as 1947 during the drafting of the Charter of the International Trade Organization. When the governments were debating whether to provide recourse to an advisory opinion from the International Court of Justice, one delegate noted that the “light thrown on a case by a public hearing and opinion of the Court” could promote diplomatic compromise (HUDEC 1971, p. 1313–1314).

Another procedural improvement would be to encourage WTO Member governments to commit to a detailed domestic procedure for implementing an adverse panel decision. Already, governments are informing the WTO about their domestic legislative and rulemaking processes as they seek an allotment of time to implement panel rulings (MONNIER 2001). This DSU Article 21.3 arbitration (of the reasonable period of time) could be expanded to ask governments to supply a timeline for effectuating compliance. National parliaments or administrative agencies could be encouraged to hold public hearings on modalities for compliance.

It might also be useful for the compliance process to invite informal participation of national courts. For example, a defendant government could ask a panel of national judges (or retired judges) to give their opinion on the holding in the Appellate Body or WTO panel decision. Such independent judicial opinion might help the government revise national law or regulation in order to comply.

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31 Indeed, it might help the public to better understand the DSU function by acknowledging the Appellate Body as a “Court” and calling it that. JOHN JACKSON may have been the first to refer to WTO dispute system as “the International Trade Court of Justice” (JACKSON 1996, p. 175).

Although public proceedings by WTO panels and the Appellate Body would require a change in DSU rules, all of the other transparency proposals discussed above could be accomplished under existing rules. To be sure, a heightened public awareness is not a panacea for achieving WTO compliance. Indeed, a danger exists of a popular backlash against the WTO's intrusion into national democratic processes. Nevertheless, working to enlighten the public is the most morally tenable way for peaceful democracies to improve each other's behavior in trade policy.

## 6 Conclusion

As ADAM SMITH pointed out over 200 years ago, we should approach with caution the idea of blocking trade in order to promote it. Nevertheless, the WTO enforcement system institutionalizes a suspension of trade rights as a response to a continued violation of WTO law. The DSU calls this action a "last resort" and to date it has been done only three times. Yet more such interventions may occur in the near future.

Before reaching the last resort, the WTO should beef up its intermediate responses to a persistent failure to comply with WTO rules. The way to turn up the pressure is to draw on the power of domestic parliaments, courts, interest groups, and public opinion to influence a government to meet its WTO obligations. Because of its state-centric orientation, the WTO has done little so far to strengthen the culture of compliance.

Although the DSU was meant to enshrine the rule of law in trade relations, the use and threat of economic sanctions reinforces the primacy of power. In principle, the non-tariff SCOOP might be equally available to small countries. But those non-tariff remedies are problematic because they vitiate WTO norms (like intellectual property rights) and hence undermine the rule of law.

The availability of trade sanctions in the WTO but not in other multilateral treaties is inherently destabilizing. It will invite pressure to add issues to the WTO. It will feed resentment of the WTO which will undermine support for freer trade.

One response to this problem is to try to turn back the clock to the GATT era and thereby envision SCOOP as rebalancing rather than sanction. This tack would not be useful however. Although it provides an answer to why

the WTO alone has trade sanctioning ability, it leaves the more difficult task of explaining why we should compensate one economic injury to ourselves by doing another. This basic conundrum identified by ADAM SMITH may be a key reason why Article 22 arbitrators have invested SCOO with the purpose of inducing compliance.

Either way, the SCOO is a bad idea for the WTO.

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