



Working Paper

# Open Plurilateral Agreements, Global Spillovers and the Multilateral Trading System

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## Abstract

Problems involving regulatory design and cooperation to respond to climate change, the rise of the digital economy and managing industrial policy conflicts call for cooperation to identify good practice and balancing the achievement of noneconomic objectives against competitive spillovers. Contrary to arguments that small group cooperation is second best in a world where consensus is not obtainable, open plurilateral agreements (OPAs) can be a first-best response to international collective action problems as it does not require all WTO members to participate or for the package deals that characterize trade negotiations. Sustaining an open, rules-based multilateral trading system calls for greater use of OPAs. The prospects for this would be enhanced if the trade policy community would build bridges to other organizations and epistemic communities and agree to a code of conduct for OPAs to ensure they support the open multilateral trade regime.

Keywords: Open plurilateral agreements; WTO; trade agreements; WTO; cross-border spillovers

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## Bertelsmann Stiftung and WTO Reform

If international trade is not governed by rules, mere might dictates what is right. The World Trade Organization (WTO) serves as a place where trade policy issues are addressed, disputes arbitrated, legal frameworks derived and enforced. Through these functions, the WTO ensures that the rules of trade policy are inspired by fairness and reciprocity rather than national interest. It is more important than ever to vitalise the global public good that it represents against various threats that have been undermining it.

The Global Economic Dynamics project of Bertelsmann Stiftung is a firm believer in rules-based international trade and the WTO. In 2018, we published an extensive report with propositions on how to revitalise the WTO, based on the deliberations of our High-Level Board of Experts on the Future of Global Trade Governance. In 2019 and 2020, we follow up on this report with a series of policy contributions, providing fresh ideas and elaborating on concepts already introduced in the report. These contributions cover the areas of the Appellate Body crisis, dealing with the competitive distortions caused by industrial subsidies, enabling Open Plurilateral Agreements within the WTO while providing reassurance to concerns of the membership at large with such forms of flexible cooperation and, finally, improving working practices in WTO Committees.

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## Executive Summary

National policies can give rise to negative cross-border spillovers. Addressing cross-border policy spillovers requires identifying those that are systemically significant and international cooperating to attenuate negative effects. Insofar as the policies impact on trade, in principle this is the task of the WTO, the international apex forum for cooperation on trade policy and the negotiation and implementation of multilaterally agreed rules. The WTO has been unable to fulfill this role, reflecting differences in priorities across the membership, an erosion in trust, and deep-seated working practices that have impeded efforts to revise and update the rulebook. The result has been that since 1995 most new rulemaking has been through preferential trade agreements (PTAs), not the WTO.

There is growing recognition that reforms are needed to improve the functioning of the WTO, including a willingness to pursue agreements pertaining to only a subset of WTO members but that are open to all WTO members and where benefits in principle extend to all countries on a nondiscriminatory basis. Open plurilateral agreements (OPAs) on specific policy areas or sectors of economic activity can complement discriminatory, closed PTAs, in the process supporting the multilateral trading system.

Contrary to arguments that plurilateral initiatives are second best in a world where consensus is not obtainable, OPAs can be a first-best response. Cooperation aimed at identifying good regulatory practice and processes to determine whether different regulatory regimes are equivalent does not require all WTO members to participate. Nor does it call for the package deals that characterize trade negotiations.

PTAs are inherently limited in their country coverage and are discriminatory by design – liberalization only applies among signatories. One consequence is that PTAs do relatively little to address global policy spillovers. Trade agreements are designed to address a specific problem: reducing the aggregate welfare cost associated with national trade-restricting measures. If countries are large (enough) such policies impose negative externalities on trading partners. Often such policies are also costly to the countries imposing them. They will reduce aggregate real income if countries are small (cannot affect their terms of trade). Efforts by large(r) countries to shift the terms of trade in their favor may have the same result if other countries in turn impose barriers on imports.

This terms-of-trade prisoner's dilemma rationale for trade cooperation is complemented by a corollary role that trade agreements can play. The structure of trade policy in a nation is determined by political economy forces. Trade agreements permit governments to “mutually disarm” by changing the domestic political equilibrium that underpins the use of welfare-reducing restrictive trade policies. They do so by offering exporters better access to partner markets, creating incentives for exporters to provide domestic political support for liberalization. Moreover, because trade agreements are self-enforcing, they can help governments make credible commitments to sustain liberalization over time.

These two conventional rationales for trade agreements ignore an increasingly important motivation for international cooperation. Changes in the structure and consequences of economic activity call for domestic regulatory measures to address associated market failures. Governments confront significant uncertainty how best to design such regulation to attain underlying objectives. Moreover, differences in regulatory regimes for a sector, product or activity give rise to transactions costs for firms operating internationally. Experience with WTO negotiations and the Paris Agreement make clear that common approaches reflected in binding multilateral agreements are unlikely to be feasible given the difficulty of attaining consensus. Instead, workable global solutions are more likely to emerge through encouragement of plurilateral initiatives (clubs) and efforts to ensure that over time these become the basis of a revamped rules-based multilateral trade regime.

OPAs among groups of countries are more appropriate instruments to address international collective action problems and the trade costs of regulatory heterogeneity because the problems are more complex than the “terms-of-trade”-cum-commitment problems trade agreements are appropriate for. Problems involving regulatory design and cooperation to respond to climate change, the rise of the digital economy and managing high-tech industrial policy conflicts call for cooperation to identify good practice and balancing the achievement of noneconomic objectives against competitive spillovers.

OPAs can help parties understand and learn about the effectiveness of alternative policy options and their effects on trade, and to identify approaches that are more effective as well as more efficient in terms of attenuating negative spillovers. International coordination and learning about good regulatory practice do not require a trade agreement because the problem is not internalizing terms-of-trade spillovers or addressing commitment problems.

Of the so-called “joint statement initiatives” that are now being pursued in the WTO – spanning e-commerce, domestic regulation of services, investment facilitation, and measures to enhance the ability of micro and small and medium enterprises (MSMEs) to utilize the opportunities offered by the rules-based trading system – most address coordination failures or entail joint efforts to identify good regulatory practices. The subjects of discussion are all areas where there are potential gains from cooperation. However, apart from the e-commerce talks, they do not address fundamental sources of recent trade tensions and conflicts. Nor do they deal with matters that will become increasingly prominent soon, such as the use of trade policies to combat climate change.

For the credibility of the WTO it is critical that at least some of the ongoing plurilateral discussions result in agreements. But what matters more for sustaining an open, rules-based multilateral trading system is to use OPAs to manage industrial policy spillovers, regulate the digital economy and govern climate change-motivated trade policies.

The prospects for successfully using OPAs to do so would be enhanced if engagement extends beyond the trade community and efforts are made to agree to a code of conduct for OPAs to address potential concerns of non-participating countries.

### Supporting plurilateral engagement

Successful international agreements addressing regulatory policies such as the WTO agreements on sanitary and phytosanitary measures, technical barriers to trade and trade facilitation are all associated with a body of agreed technical knowledge and accumulated good will among the relevant national regulatory agencies. The same is true for all successful examples of international regulatory cooperation.

A necessary condition for successful OPAs is to create mechanisms that support informed deliberation in a given policy area and fosters substantive, evidence and analysis-based discussion. Without robust information on applied policies across countries and experience in implementing them it is not possible to identify either good practices, what policies create large spillovers that are systemically important, or efficient approaches to attenuate such spillovers in ways that reflect and respond to local capabilities and priorities. Integrating the relevant stakeholders, regulators, and sources of expertise (e.g., international organizations) in efforts to address such questions is necessary.

Different models can be envisaged to prepare the ground for new OPAs. One is to work through the G20 Trade and Investment Working Group, which spans G20 governments and the major international agencies. Another approach is to create a sector-specific platform serviced by one specialized agency, as was done by the G20 through the 2016 Global Forum on Steel Excess Capacity (GFSEC), which was tasked with producing reliable statistics on steel production capacity and identifying policies that affect steel production. Yet another option is to bring together a group of independent policy research institutes and provide them with a mandate and the resources to collect and analyze information to support engagement by countries to cooperate on a critical mass basis.

In practice effective OPAs are likely to be policy and/or sector-specific, bringing together the WTO (trade community) with other organizations that have a mandate in an area of overlapping interest. On climate change, for example, the Paris Agreement and the WTO provide a basis for the formation of linked OPAs to support domain-specific decarbonization regimes. The Paris Agreement authorizes countries to set national decarbonization targets and to form sector-specific ‘climate clubs’ for joint pursuit of national targets outside Paris and to count progress achieved there towards their voluntary goals. An implication of the voluntary nature of national commitments under Paris is that any penalty defaults defined by climate clubs involving trade restrictions fall outside the Paris Agreement. Although countries can invoke the general exceptions provision of the WTO to justify the use of

trade measures as part of decarbonization initiatives, an OPA can make explicit how trade sanctions will be applied among members of the OPA to attain decarbonization targets they have agreed.

Reconciling sectoral differences in domestic regulatory requirements pertaining to decarbonization of economic activity is just one, albeit very important example where OPAs can reduce the costs of regulatory heterogeneity. The concept can be applied as well to other policy domains, with clubs of countries, without the consent of other WTO members, defining regulatory standards for themselves, but committing that cooperation be open to participation by any WTO member. As a result, participation would be selective, with a WTO member deciding to join some OPAs but not others.

### **A governance framework for OPAs in the WTO**

While not a panacea, OPAs are a good path forward for countries desiring to deepen cooperation in a given policy area or sector of economic activity. Although OPAs cannot alter the rights and obligations of WTO members that do not sign them, they do raise potential concerns for nonmembers. Even if – as we assume will be the case – agreements are applied on a nondiscriminatory basis, countries that decide not to participate may have an interest in what is discussed and agreed to constitute good practice.

Agreeing to a set of binding principles that OPA signatories commit to abide by can help recognize valid concerns of nonmembers that OPAs be fully consistent with multilateralism. Ensuring that agreements are truly open to any country wishing to join, are fully transparent, and include mechanisms to assist countries not able to participate because of weaknesses in institutional capabilities would do much to ensure OPAs support the goals of the multilateral trading system.

More broadly, developing a framework of general rules for registering OPA commitments, monitoring and evaluating results, establishing penalty defaults and establishment of financial facilities to support expanded participation over time can help facilitate coordination among governments, specialized international agencies and international business organizations.

A governance framework for OPAs can build on WTO precedent in the area of telecom regulation and take the form of a binding Reference Paper that would be incorporated into each OPA.

A Reference Paper on OPAs could include the following elements:

1. A provision making explicit that membership of an OPA is voluntary and that WTO members that decide not to participate cannot be obliged to join at a later date;
2. The OPA is open to subsequent membership by WTO Members that did not join when it was first agreed;
3. A section laying out the requirements and procedures to be followed for accession by aspiring members;
4. A commitment that accession to an OPA cannot be on terms that are more stringent than those that applied to the incumbent parties, adjusted for any changes in substantive disciplines adopted by signatories over time;
5. Where feasible and in instances where capacities must be built for a country to meet OPA requirements, consideration be given to establish a stepwise schedule of compliance;
6. A binding and enforceable provision committing signatories to provide assistance to WTO members that are not in a position to satisfy the preconditions for membership in terms of applying the substantive provisions of the agreement but desire to do so;
7. Inclusion of consultation and binding conflict resolution procedures that may be invoked by non-signatories of OPAs if they perceive that incumbents impose more stringent conditions to accede to an agreement than apply to extant parties to the OPA, or if parties to an OPA do not live up to the commitment to respond to requests to provide assistance to nonmembers;
8. Provisions that ensure the OPA is open in the sense of including transparency mechanisms to ensure that nonparticipants have full information on the implementation and operation of the agreement. These should include:
  - a. Compliance with WTO requirements pertaining to publication of information on measures covered by the OPA;
  - b. Simple, robust notification requirements for OPA members;



- c. Regular engagement of stakeholders in an ongoing conversation about how the agreement is working and future needs;
- d. Annual reporting to the WTO General Council by the OPA on its activities.

These principles do not include a requirement to provide 'special and differential treatment' (SDT) of the type currently embodied in the WTO which permits developing countries to offer 'less than full reciprocity'. Instead, the focus is to assist countries to achieve the common regulatory objectives of OPA members. Including mechanisms to assist countries improve their regulatory regimes to be able to benefit from OPA is important for inclusiveness and enhancing their relevance to low-income countries.

## Introduction

Since the early 1990s, sustained economic growth in many parts of the world has led to a great increase in the global trade share of developing countries, driven by a rapid expansion in global value chains (GVCs), in turn reflecting adoption of outward-oriented trade policies. The associated rebalancing of global output and income shares has helped lead to a “backlash against globalization” in many high-income countries, driven by the adjustment pressures and perceptions that the success of emerging economies is based in part on policies that unfairly advantage their firms. Further complicating matters, ongoing technological change and innovation is changing the composition of global trade flows towards services, e-commerce and cross-border digital transactions, generating new sources of economic adjustment pressures as well as opportunities.

These developments call for revisiting and updating international trade cooperation. In principle this is the task of the World Trade Organization (WTO), the international apex forum for negotiation and implementation of multilaterally agreed trade rules. The WTO has been unable to fulfill this role, reflecting differences in priorities across the membership, an erosion in trust, and deep-seated working practices that have impeded efforts to agree on changes to the rulebook. Consequently, most new rulemaking has been occurring in preferential trade agreements (PTAs), not the WTO.

Abstracting from regional integration arrangements that go far beyond reciprocal trade liberalization and reflect political goals to foster deep integration through creation of an economic union – such as the European Union – trade agreements and the negotiating processes used to conclude them are designed to address a specific problem: reducing the aggregate welfare cost associated with nationally adopted trade-restricting policies. If countries are large (enough) such policies impose negative externalities on trading partners. Often such policies are also costly to the countries imposing them. They will reduce aggregate real income if countries are small (cannot affect their terms of trade). Efforts by large(r) countries to shift the terms of trade in their favor may have the same result if other countries in turn impose barriers to their exports.

Addressing this terms-of-trade prisoner’s dilemma rationale for trade cooperation is complemented by a corollary potential role for trade agreements. The structure of trade policy in a nation is determined by political economy forces. Trade agreements permit governments to “mutually disarm” by changing the domestic political equilibrium that underpins the use of welfare-reducing restrictive trade policies. They do so by offering exporters better access to partner markets, creating incentives for exporters to provide political support for liberalization. Moreover, because trade agreements are self-enforcing, they help governments make credible commitments to sustain liberalization commitments over time because reversal of liberalization will be met by retaliation by trading partners, hurting export industries and firms.

These two conventional rationales for trade agreements<sup>1</sup> ignore another motivation for international cooperation: to reduce the transactions costs of international regulatory heterogeneity for a given sector or product, and to identify how best to regulate economic activities to attain common economic or noneconomic objectives. The trade costs of regulatory heterogeneity may be reduced through coordination and learning, leading to adoption of common norms and gradual adoption of what has been determined to constitute good regulatory practices. Such cooperation does not require a trade agreement because the problem is not internalizing terms-of-trade spillovers or addressing time inconsistency problems by creating a credible commitment mechanism. Instead, what we call open plurilateral agreements (OPAs) can be used to support mutually beneficial cooperation. Because regulatory heterogeneity is increasingly rising to the fore as a factor creating trade costs, reflecting the steady rise in economic interdependency, OPAs can complement trade agreements as devices to support and sustain international cooperation. Moreover, OPAs offer a tool for countries to cooperate in addressing international collective action problems and for countries learn about and adapt policies to address market failures more efficiently. Climate change-related policies are a particularly important example. Finally, OPAs may also be a means to address the

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<sup>1</sup> See, e.g., Maggi (2014) and Limão (2016).

international spillovers of policies that cannot be addressed through PTAs because of free rider concerns. Industrial subsidies are an example: agreement of rules of the game in this area require all of the large trade powers to participate.

Open plurilateral agreements (OPAs) offer both the prospect of reducing regulatory compliance costs for firms operating internationally and acting as a platform for large players to cooperate in attenuating negative spillovers from national policies. Contrary to arguments that plurilateral initiatives are second best in a world where consensus is not obtainable, OPAs can be a first-best response. Cooperation aimed at identifying good regulatory practice and processes to determine whether different regulatory regimes are equivalent does not require all WTO members to participate. Nor does it call for the package deals that characterize trade negotiations. OPAs can be sector-specific, bringing together the associated stakeholders and leverage the expertise and experience that is salient to a given activity and the spillovers it generates.<sup>2</sup>

The international rules of the game were last revised in the early 1990s. They have not kept up with a rapidly changing world economy in which emerging economies account for a large share of global output and where cross-border flows of data, digital products and technologies are expanding rapidly. Competition between governments to stimulate domestic economic activity through 'make it here' policies is growing, often reflecting an implicit if not explicit questioning of the distribution of the gains from trade. The US has reverted to "aggressive unilateralism" including negotiation of bilateral 'voluntary' export restraints and import expansion commitments – i.e., managed trade of the type last seen in the 1980s (Bhagwati, 1987; Bhagwati and Patrick, 1991). Globally, rising use of trade-distorting policies is occurring in conjunction with a rapid shift towards an ever more globally interconnected digital economy. These developments call for multilateral cooperation to revisit the rules of the game in a variety of policy areas, including industrial policies and the regulation of cross-border data flows and digital products.

National policies can give rise to negative cross-border spillovers. Policies restricting trade and investment are designed to do so, while policies of a fiscal nature (tax exemptions, subsidies and related industrial policies) or measures to combat climate change may do so. Addressing cross-border policy spillovers requires cooperation to identify those that are systemically significant and negotiating rules that attenuate negative side effects. Insofar as the policies impact on trade, in principle this is the task of the WTO. The WTO is the apex international forum for the negotiation and enforcement of trade policy disciplines and commitments. The WTO has been unable to fulfill this role, reflecting differences in priorities across the membership, an erosion in trust, and deep-seated working practices that have impeded efforts to address both old and new policy externalities.

Many countries have responded to recent US unilateralism by ramping up efforts to conclude trade agreements with each other. In parallel, plurilateral cooperation outside the narrow area of trade policy is pursued by many countries, ranging from health and safety standards to taxation and regulation of financial service providers (Hoekman and Sabel, 2018).<sup>3</sup> This illustrates that many countries continue to pursue international cooperation to deepen economic integration. The multidimensional nature of the policies that influence investment and operational decisions of international firms suggests a multidimensional response is in order. Part of that response should center on revisiting the design and content of trade and investment agreements. In the WTO setting there is a growing recognition that reforms are needed to improve the functioning of the organization, including a willingness to explore plurilateral forms of cooperation under the umbrella of the multilateral agreements. The challenge – and opportunity – is to ensure that any agreements that emerge are open as opposed to the closed nature of most PTAs, in the process supporting gradual multilateralization (Hoekman and Sabel, 2019).

Our premise is that many critical mass initiatives, where the benefits extend on a nondiscriminatory basis to all countries, should be feasible if they involve the key players in the G20. In practice, specific initiatives need not

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<sup>2</sup> For example, Hoekman and Inama (2018) propose an OPA on rules of origin.

<sup>3</sup> The term plurilateral is used to describe different types of arrangements in the literature. In this paper the term "discriminatory plurilateral agreement" (DPA) is used for so-called Annex 4 WTO agreements that allow for discrimination against non-signatories. In contrast, the term "open plurilateral agreement" (OPA) is used to describe cooperation where benefits are applied on a nondiscriminatory basis to non-signatories.

necessarily include all G20 member countries. Indeed, imposing that constraint would greatly limit the scope for action given the wide divergences within the G20 as regards desirable trade policies. The critical mass needed to internalize a large share of the total benefits associated with rules for policies such as industrial subsidies is very small, essentially encompassing China, the EU (and UK), Japan and the US.

The situation confronting the trading system today has parallels with the 1980s, which saw extensive recourse to trade-distorting measures in response to a rapid rise in exports from East Asian economies. This motivated the launch of a preparatory process by countries that informed the design of the Uruguay Round negotiation agenda. A similar effort is needed today, aimed at resolving the trade conflicts that are of greatest relevance from a systemic perspective. Two areas are particularly important: (i) rulemaking to address major international spillovers from national industrial policies; and (ii) improving the functioning of the WTO, including more effective approaches to address disparities in capacity and economic development. Open plurilateral agreements (OPAs) can help on both fronts.

The plan of this paper is as follows. Section 1 describes briefly some of the drivers of the turn to plurilateral cooperation and away from fully multilateral initiatives spanning all 164 WTO members. Section 2 discusses rationales for – and tradeoffs associated with – embedding cooperation in discriminatory, closed, trade agreements (PTAs). Section 3 makes a case for open plurilateral agreements (OPAs) as a complementary, desirable, instrument to further deepen cooperation on a nondiscriminatory basis and briefly discusses ongoing plurilateral talks in the WTO. Section 4 presents some suggestions for governance principles that could be applied by participating WTO members to ensure that OPAs support the multilateral trading system. Section 5 concludes.

## 1 Deadlock in the WTO as a driver of regionalism

Many policy areas can generate spillovers for other countries, both negative and positive. Examples are export restrictions, which are detrimental to net importing countries but may benefit competing exporters and “green” subsidies (ranging from minimum feed-in prices for electricity generated from renewable resources to subsidies for the development or use of specific technologies) that help to address global climate change even though they may have adverse consequences for competing firms from other countries. Similarly, policies constraining digital trade, e-commerce and data flows may not have the goal of restricting trade but do so as a side-effect of the pursuit of specific domestic regulatory objectives such as consumer protection and privacy.

Support for trade is strong in most countries. Indeed, post-Trump support has been increasing in countries where surveys suggested a trend towards increasing critical views of globalization. In the EU, for example, Eurobarometer data indicate that 60% of Europeans consider free trade as positive.<sup>4</sup> This provides political support for one response of governments to the Trump administration’s unilateral decision to adopt an explicitly mercantilist trade policy: negotiation of trade agreements. The decision by the TPP-11 countries to move forward with the CPTPP, without the US, exemplifies that these nations continue to believe that opening markets and cooperating on trade policies is in their interest. The CPTPP includes provisions on policies that give rise to negative spillovers and that go beyond what is embodied in the WTO, including on digital trade and data flows. Similarly, post-2016 the EU has been active in pursuit of new PTAs that include provisions dealing with domestic regulatory policies, and many countries in Asia and Africa ramped up longer-standing efforts to negotiate PTAs, notably, the African Continental Free Trade Area (AfCFTA) and the Regional Comprehensive Economic Partnership (RCEP).

Such a dynamic is not observed in the WTO. Reasons for this include shifts in the power balance among its members, the legacy of the failed Doha Development Agenda (DDA) and the organization’s working practices. The core negotiation, transparency, and conflict resolution functions of the organization are not functioning effectively, undermining the WTO’s ability to fulfill its mandate. The failure of the Doha round in turn has precluded discussion of a new work program that includes the regulatory subjects that increasingly are of central concern to politics and international businesses.

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<sup>4</sup> Between 2010 and 2019, there was a 16-percentage point increase in positive responses to the question whether respondents benefited from international trade. At: <https://ec.europa.eu/commfrontoffice/publicopinion/index.cfm/survey/getsurveydetail/instruments/special/surveyky/2246>

Deadlock in the WTO has prevailed in part because of consensus-based decision-making. This permitted WTO members to veto initiatives and block efforts to go beyond the issues on the DDA. A complementary factor in this regard is that the WTO embodies special and differential treatment (SDT) provisions for developing countries which entail a right to offer less than full reciprocity in trade negotiations and to delay or be exempted from the application of certain WTO rules. The invocation of SDT by large and/or more advanced emerging economies is increasingly opposed by many higher-income countries, first and foremost the US. Conversely, many developing countries take the position that SDT is a core feature of the balance of rights and obligations associated with WTO membership.

While consensus is primarily a practice and not a formal rule – voting is possible in principle – voting does not occur, reflecting a widely held view this would undermine the legitimacy of WTO decisions.<sup>5</sup> Countries large and small rely on the consensus practice as a guarantee that the results of negotiations are acceptable to them, ensuring political ‘ownership’ of the WTO by members and their polities. This positive aspect of consensus decision-making is offset by the possibility of blocking activities that may have nothing to do with rule-making negotiations, such as setting the agenda of committee meetings or proposals to discuss trade policy-related matters that are not covered by a WTO agreement or the DDA. The result has been that since the WTO was created in 1995 most new rulemaking has been occurring in PTAs, not the WTO (Dür, Baccini and Elsig, 2014; Hofman et al. 2018).

In January 2020 there were 303 PTAs in force according to the WTO.<sup>6</sup> They often have a regional focus: the EU and its PTAs with neighboring countries; the AfCFTA in Africa; ASEAN and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in Asia; and a variety of shallower agreements around the world. Many countries have concluded multiple PTAs both with regional partners and across regions. While PTAs can help reduce trade costs they are inherently limited in the coverage of the countries involved and are by design discriminatory – market access liberalization is on a preferential basis. Most do not have an accession provision – one reason why there is such a plethora of PTAs. The CPTPP is an outlier in having a provision that permits other countries to join. The CPTPP includes provisions on e-commerce, regulatory matters, investment, and competition policy (including state-owned enterprises). If China and the EU were to join or link to the CPTPP, this would reduce the fragmentation associated with bilateral PTAs and further expand trade cooperation to areas not or partially covered by the WTO. In such a scenario, it is likely that the US would have incentives to consider joining such a greatly expanded CPTPP to avoid associated trade and investment diversion costs.

The prospects for this appear rather dim. Major emerging economies such as China and India have not signed deep PTAs. One consequence is that to date PTAs have done relatively little to address major sources of policy spillovers – such as the use of subsidies – because of collective action (free riding) problems. China, the EU, Japan and the US all engage in bilateral discussions with each other on trade-related matters. In addition, the EU, Japan and the US have launched in a trilateral process to identify ways to strengthen disciplines on subsidies, state-owned enterprises, and industrial development policies more broadly. A necessary condition for meaningful outcomes is that all the major trading powers are involved in the associated deliberations-cum-negotiations. There is no magic bullet: progress on rulemaking to resolve sources of policy conflicts and systemic spillovers requires agreement between the large players.

A key question – both practical and analytical – is how to design trade agreements to incentivize engagement by a sufficiently large number of significant countries. A corollary question is whether cooperation on policies such as subsidies or digital economy regulation requires embedding in agreements that encompass market access liberalization commitments or can be pursued on a policy-specific basis. The latter is currently being pursued in the WTO through plurilateral discussions on e-commerce and domestic regulation of services.

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<sup>5</sup> Art. IX WTO specifies that if voting occurs, unanimity is required for amendments relating to general principles such as non-discrimination; a three-quarters majority for Interpretations of provisions of the WTO agreements and decisions on waivers; and a two-thirds majority for amendments relating to issues other than general principles. Where not otherwise specified and consensus cannot be reached a simple majority vote is sufficient. Art. X provides that a member cannot be bound by a vote on an amendment that alters its rights or obligations and that it opposes. In such instances, the Ministerial Conference may decide to request that the member concerned withdraw from the WTO or to grant it a waiver.

<sup>6</sup> [https://www.wto.org/english/tratop\\_e/region\\_e/region\\_e.htm](https://www.wto.org/english/tratop_e/region_e/region_e.htm).

## 2 Why cooperate through trade agreements

Conceptually, trade agreements deal with two specific problems: reducing the negative spillovers generated by foreign trade policies – a ‘terms of trade’ externality; and/or an inability of a government to make a credible commitment to sustain a desired more liberal trade policy (Maggi, 2014). Both dimensions are potentially relevant as a motivation for including provisions on domestic regulation in a trade agreement as well as a focus on liberalization of discriminatory market access barriers. Regulation can affect the terms of trade by raising costs for foreign firms – even if regulations apply on a nondiscriminatory basis to foreign and home firms (Kox and Lejour, 2005). Moreover, desirable types of regulation may confront implementation difficulties because of political economy forces that a government might be able to overcome through binding treaty commitments. Even if commitment is the aim, improving market access remains the primary focus of trade agreements, as this is the mechanism through which credibility is obtained: it is market access that incentivizes the trading partner to enforce the commitment.

Trade agreements have four salient characteristics that are relevant from the perspective of considering how they may support – or impede – deeper forms of market integration. First, they liberalize access to markets through a process of reciprocal exchange of trade policy concessions. The need for reciprocity on market access liberalization is well understood and reflects a mix of terms of trade considerations (for large enough countries) and political economy forces. Internalizing the benefits of liberalization can be achieved if the liberalization is reciprocal. Second, they rely on the national treatment principle to prevent ‘concession erosion’ using domestic policies that may be designed to substitute for trade policies, while leaving parties free to define their domestic regulations as they wish. What matters here is that such regulation is applied equally to domestic and foreign agents. Third, and related to the previous characteristic, provisions on nontariff measures reflect a desire to facilitate trade (reduce trade costs), not change or improve national regulation. Fourth, they are self-enforcing: the threat of withdrawal of market access commitments is the mechanism to sustain cooperation.

Most PTAs are shallow integration instruments in the sense that signatories retain national regulatory sovereignty: they are free to regulate as they wish as long as measures apply on a nondiscriminatory basis to domestic and foreign products (firms) – i.e., satisfy the national treatment and most-favored-nation (MFN) principles.<sup>7</sup> National treatment is effective in preventing the use of domestic regulation to undercut negotiated trade liberalization commitments, but it does nothing to help move countries to improve regulatory outcomes over time. “Deeper” PTAs go beyond the four basic characteristics by including provisions on the substance of domestic regulation. Differences in regulation across jurisdictions for tangible and intangible products may impede trade by generating redundant transactions costs or segmenting markets. Governments have responded to demands from businesses and citizens to bolster the governance of cross-border exchanges by (re-)designing trade agreements to go beyond traditional liberalization of trade in goods to encompass disciplines on policies affecting trade in services, protection of intellectual property rights, dimensions of foreign investment and regulation of product and factor markets more broadly. This may reflect concerns that trading partners adopt certain health, safety, labor or environmental regulations, often centered around alignment with international norms.

There may also be efficiency rationales for pursuing cooperation on regulatory policies on a small group basis. One reason is that a uniform rule for a given policy may be inefficient; another is that even if there is agreement that a given regulatory rule is desirable, not all countries will satisfy the preconditions for implementing it.

The great diversity in circumstances and priorities across the WTO membership implies “variable geometry” is and will be an inherent feature of regulatory cooperation. The challenge for the multilateral trading system is to do so in a way that supports rather than undercuts the WTO and recognizes that an exclusive focus on mini-lateral outcomes is suboptimal systemically as well as in terms of aggregate welfare gains. Large players such as the EU or the US may seek to “export” their preferred regulatory norms to trading partners (Lavenex, 2014) and do so in part by linking preferential access to markets to commitments by partner countries to change domestic regulatory policies. Linkage to market access may be soft in the sense of not being enforceable, but what matters is that

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<sup>7</sup> The WTO encourages members to adopt international product standards if these exist, but national requirements that differ from international norms – if these exist – are permitted if they are not more trade restrictive than necessary to attain the underlying policy objective. See Mavroidis (2016) for an in-depth treatment of the genesis and substance of WTO rules.

this is a core feature of trade agreements. Market access is the carrot to induce a country to change its domestic regulation or to do more to enforce specific regulations. An example is conditioning preferential access to the market on reform and enforcement of labor standards, environmental policies or protection of human rights.<sup>8</sup>

Both PTAs and multilateral WTO negotiating rounds involve bundling multiple issues into packages and embody a complex mix of within- and cross-issue linkages. Cross-issue linkages are needed when policies are not separable, i.e., policies either can substitute for each other or they are complements so that addressing one area enhances the payoffs of cooperation in another. Issue linkage in international agreements involves the parties connecting two or more policy areas in some way. If there are structural interactions between issue areas, linkage may be both needed and beneficial (Spagnolo, 2001; Conconi and Perroni, 2002; Limão, 2005). If there are not, issue linkage is not needed and may undermine cooperation.<sup>9</sup>

Maggi (2016) identifies three types of issue linkage in international agreements: negotiation linkage; enforcement linkage and participation linkage. The first of these involves negotiating two or more issues in one agreement, with the possibility of trade-offs across issues, the goal being to conclude one agreement – a package deal. Given agreement, enforcement linkage involves action in one issue area to enforce compliance with commitments in another (cross-retaliation). Participation linkage comprise situations where the threat of sanctions in one area induces participation in an agreement addressing another policy area. All three types of linkage fall under the broader concept of conditionality – making cooperation in one area a condition for cooperation in another. Conconi and Perroni (2005) contrast this notion of conditionality with a separation rule, in which there are explicit prohibitions on using sanctions in one area to induce (enforce) cooperation in another.

In principle, issue linkage increases potential overall gains, but as demonstrated by the Doha round, crafting a negotiating agenda that delivers large enough net gains to all parties is difficult. If policies are separable, cross-issue linkage is not needed – the payoffs of cooperation are independent of what governments may or may not do in other policy areas. There is no rationale for considering cross-issue linkage. There may also be no need to tie cooperation to market access – i.e., to engage in what Maggi (2016) calls enforcement linkage. The potential value of enforceability depends on the type of commitment that is undertaken. Binding dispute settlement enforced by the (threat of) withdrawal of market access is unlikely to be useful for encouraging cooperation on regulatory matters. It is more likely to have a chilling effect on the willingness to consider cooperation – due to fear of uncertain contingent liability or views by regulators that market access considerations will have adverse effects on the realization of regulatory goals.<sup>10</sup> Different systems are needed, based on transparency mechanisms (information collection, incident reporting, sharing of data, dialogue) and, as Hoekman and Sabel (2019) argue, severability. The latter is a feature of the CPTPP chapter on regulatory coherence which is not subject to binding dispute resolution. This was also taken off the table by the EU in the aborted TTIP talks.

‘Enforcement linkage’ may be a motivation to include regulatory provisions in trade agreements, but the desirability of such mechanisms needs careful analysis. A PTA-centered approach may make it more difficult to sustain regulatory cooperation. PTAs are conditional on acceptance of engaging in preferential liberalization of market access. This is a requirement of WTO rules: ‘substantially all trade’ must be covered by a trade agreement for it to be WTO-consistent. Thus, countries that are interested in deepening cooperation on domestic regulation and non-trade areas of economic policy will need to be willing to engage on market access. In turn, existing PTA members must accept extending access to their markets to new countries insofar as their PTAs have provisions permitting accession. Incumbents may not be willing to do so for many reasons. Thus, the PTA route is an inflexible one, even for PTAs that have an accession provision – such as the CPTPP – given the need for far-reaching

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<sup>8</sup> A feature of so-called nonreciprocal trade preference programs in which richer countries grant poorer countries better access to their markets without requiring the latter to offer reciprocity in terms of market opening is that conditionality may be imposed in other policy areas – i.e., there is cross-issue linkage.

<sup>9</sup> India’s failed attempt to link final adoption of the WTO Trade Facilitation Agreement (TFA) to concessions on agricultural support is an example. See Hoekman (2016).

<sup>10</sup> Such concerns were an important factor in the demise of talks in the WTO on competition policy in the late 1990s and early 2000s. Competition authorities held the view that their mandate was to safeguard consumer interests, the contestability of markets and national welfare. In doing so, they do not distinguish between the behavior of domestic and foreign firms on the market, as opposed to the focus of trade negotiators on improving conditions of competition for national firms.

market access commitments that have nothing to do with regulatory cooperation. This applies to multilateral trade agreements as well.

PTAs are also not a panacea as instruments to address concerns of citizens regarding non-trade policy dimensions. Many citizens of high-income countries consider globalization a threat to employment and a source of rising inequalities. These include the implications of trade agreements for regulatory powers and the desire that trade be conditioned on protecting the environment and social standards. As noted, such policy areas are increasingly addressed explicitly in trade agreements, e.g., through the inclusion of provisions that require action by signatory governments on social and environmental policies. PTAs permit market access to be used as a carrot (and a stick) to encourage adoption of commitments pertaining to these areas. Such linkage strategies can work when trade relations are asymmetric but are less feasible to implement when it comes to large countries such as China or India.

Some foreign trade practices generating negative spillover effects cannot be addressed effectively through regional agreements that only include a subset of the major countries. PTAs offer only partial solutions to companies seeking a reduction in trade uncertainty and a level playing field. The same is true for citizens concerned with ensuring that trade supports societal goals and sustainable development. What is needed is to complement PTAs with forms of cooperation that are more open and inclusive. In some areas deeper cooperation on contested policies require all of the major traders to agree. In others cooperation may be feasible among subsets of countries without necessarily encompassing all major players.

### 3 Open plurilateral agreements

At the December 2017 Ministerial Conference, WTO members abandoned the long-standing view that the WTO should pursue agreements spanning all 164 members. This development offers a path for international cooperation that does not require all WTO members participate, and thus a potential alternative to what has been the primary alternative for countries seeking to deepen trade governance: discriminatory PTAs. Open plurilateral agreements (OPAs) involving groups of WTO members offer both the prospect of reducing regulatory compliance costs for firms operating internationally while enhancing the ability of regulatory agencies to attain societal objectives more efficiently.<sup>11</sup>

Contrary to arguments that plurilateral initiatives are second best in a world where consensus is not obtainable, OPAs can be a first-best response to resolving problems associated with regulatory heterogeneity. Cooperation on regulatory matters does not require large-N participation or cross-issue linkage or the type of first difference reciprocity (Bhagwati, 1988) that is a basic feature of trade negotiations. Attempting to integrate regulatory cooperation into the framework of 'single undertaking' type package deals that characterize trade negotiations is neither necessary nor desirable. Nor is the secrecy that is part of the trade negotiations process. Indeed, when pursuing regulatory cooperation secrecy is counterproductive. This is not to deny the close link that may exist between market access and regulation, or that in some instances this link must be explicit in international cooperation between countries. What is feasible will depend of the type of issues involved.

#### 3.1 Beyond reciprocity

In addition to formation of discriminatory PTAs that remove barriers of substantially all trade between signatories, the WTO offers two alternative mechanisms for Members to make trade policy commitments on a small group basis. One is to conclude a discriminatory plurilateral agreement (DPA) under Art. II.3 WTO; the other is a so-

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<sup>11</sup> Hoekman and Sabel (2019). Open plurilateralism as an organizing concept is an element of the Government of New Zealand's trade policy strategy. See Vitalis (2018). New Zealand launched an initiative with Costa Rica, Fiji, Iceland, Norway and Switzerland on an open plurilateral Agreement on Climate Change, Trade and Sustainability, with a view to demonstrating how trade policy and trade rules can play a critical role in helping to drive the transformation of the economy to become more sustainable and inclusive. See <https://www.mfat.govt.nz/en/media-and-resources/ministry-statements-and-speeches/trade-ministers-express-support-for-the-agreement-on-climate-change-trade-and-sustainability-at-the-world-economic-forum-davos-2020/>.



called critical mass agreement (CMA). Both involve negotiated disciplines that apply only to signatories. They differ in that the benefits of a CMA apply on a nondiscriminatory basis to all countries, including non-participating nations, whereas in a DPA they do not. Examples of CMAs include the Information Technology Agreement (ITA) and agreements on basic telecommunications and financial services (Hoekman and Mavroidis, 2015b). The main example of a DPA is the WTO Agreement on Government Procurement (GPA). In considering different types of trade cooperation, countries must determine the need for cross-issue linkages, whether free-riding constraints apply and, if so, what constitutes a critical mass of participation that internalizes enough of the benefits within the participating group of countries.

Table 1 characterizes different types of trade agreements—multilateral package deals, PTAs, CMAs and DPAs. All involve policy commitments and international cooperation among signatories. They differ in design and implementation. Types of cooperation included in the top part of Table 1 address policies that by design impede market access. Multilateral package deals and CMAs that reduce market access barriers are only feasible if most of the associated benefits is internalized by participants. Free riding concerns will otherwise preclude agreement. This is a problem for trade liberalization because the WTO requires border trade policies to be applied on a most-favored-basis to all WTO members. This constraint can easily bind, as shown by negotiations on an Environmental Goods Agreement (EGA) to reduce tariffs on products salient for reducing carbon emissions, which have not been concluded because of free-riding concerns. Similar concerns arose in the now aborted negotiations on a Trade in Services Agreement (TiSA). The ITA demonstrates that CMAs can be negotiated, but also that a necessary condition is that a large enough set of countries participate.

The bottom part of Table 1 presents alternative types of cooperation where the primary focus is not on removing market access barriers but on agreement to cooperate on domestic regulation. Such agreements can take the form of harmonization (e.g., a commitment to develop and adopt common standards), implementing agreed good regulatory practices, and mutual recognition of equivalence of standards or regulatory regimes. Agreement on regulatory standards and regimes may be associated with improving access to markets insofar as regulatory standards must be satisfied as a condition for supplying a product. What and how much can be done will depend on whether free riding is a constraint. This will be a factor for narrow market access liberalization negotiations but may be much less pertinent for regulatory cooperation given that countries can decide not to extend cooperate if local circumstances or social preferences differ too much, and exclude countries that do not satisfy the negotiated preconditions for cooperation to occur.

The benefits of cooperation may apply unconditionally to all countries on a nondiscriminatory basis or on a conditional basis. Examples of the former include the WTO TFA which defines a set of good regulatory practices to facilitate trade that all WTO members have agreed to implement, with countries determining for themselves the timeline for implementation and having the ability to request technical assistance if needed. Other examples are collaborative efforts in fora such as the OECD and APEC to define good regulatory practices and agreement by countries to adopt these. They also include international collaboration to develop product and process standards in inter-governmental bodies such as the ISO. Cooperation involving identification and agreement on good regulatory practices can be applied on an MFN basis as it is insensitive to free riding considerations: the policies are in the self-interest of countries independent of whether other countries do so.

In practice, regulatory cooperation may need to be conditional on joint action by the parties. Such conditionality will vary in intensity, ranging from low forms such as mutual recognition agreements that require satisfying minimum standards, to very high (e.g., regulatory equivalence regimes). Countries that do not have adequate regulatory institutions will not be able to benefit from mutual recognition, let alone equivalence arrangements. Cooperation in such cases may require a focus on complementary measures such as development aid and related measures to bolster regulatory capacity. Inclusion of technical or financial assistance was an important element of the 2013 Trade Facilitation Agreement (Hoekman, 2016).

One type of OPA that falls into the category of a conditional agreement in the bottom right party of Table 1 is what Mattoo (2018) calls destination-specific exporter regulatory commitments where a regulator (government) accepts to look after the interests of consumers in countries to which firms under its jurisdiction export. Foreign consumer interests would be defined by the regulatory objectives that have been established by the importing country, with the exporting country regulator/government committing to attain these goals without necessarily adopting an identical regulatory regime. This is a form of regulatory cooperation that is more closely linked to market access

objectives than equivalence or adequacy regimes in that the importing country would agree to allow the associated products to be offered on its market.

Another example where trade (market access) may be used as a default penalty to enforce cooperation are domain-specific climate clubs where countries agree on joint decarbonization targets for a sector or type of activity and include trade as a part of the enforcement mechanism (Nordhaus, 2015; Sabel and Victor, 2019).

Table 1: **Alternative Instruments for Cooperation**

Type of cooperation	Main issue	Type of spillover	Characteristics of cooperation	
			Nondiscrimination	Discrimination
Trade agreements: Binding State-to-State treaties with fixed terms and binding, self-enforcing dispute resolution	Market access	„Terms of trade“ effects of trade/industrial policies	Multi-issue multilateral agreements (Uruguay Round; DDA)	Reciprocal PTAs
		Pecuniary spillovers	Issue-specific critical mass agreements (CMAs) (e.g. Information Technology Agreement)	Issue-specific, discriminatory plurilateral agreements (DPAs) (e.g. WTO Government Procurement Agreement)
Open plurilateral agreement (OPA): Open, severable, issue-specific	Regulatory heterogeneity (e.g. product market regulation; climate policy)	Cross border effects of domestic regulatory policies	International product or process standards (e.g., Codex Alimentarius)	Mutual recognition agreements Regulatory equivalence regimes (e.g., EU data adequacy findings)
		Non-pecuniary spillovers	Good regulatory practices (e.g., OECD; APEC; WTO Trade Facilitation Agreement)	Exporter commitments to apply importer country standards (e.g., EU Forest Law Enforcement, Governance and Trade regime)  Climate clubs including trade penalty defaults

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### 3.2 OPAs vs. PTAs

OPAs differ from PTAs in three ways (Hoekman and Mavroidis, 2015b; Hoekman and Sabel, 2018; 2019). First, PTAs are comprehensive trade deals and thus entail cross issue linkages. A weakening of standards in domain A may, as part of an encompassing bargain, be compensated by concessions in domain B. OPAs are domain specific: standards in one domain are not bargaining chips in negotiations about standards in others. Second, PTAs are enduring, detailed agreements, fixing the terms of trade for the foreseeable future, subject only to presumably marginal adjustments. OPAs establish frameworks for continuing reciprocal review of existing regulatory standards and their implementation, and joint evaluation of potential alternatives and adaptations to new developments. Put another way, OPAs can entrench particular values more deeply than PTAs, but treat the precise expression of those values in regulatory rules as more easily contestable and corrigible. Because they treat standards as values in themselves, expressive of deep and abiding social and political commitments, rather than counters in periodic rounds of trade bargaining, and because they institutionalize ongoing review of the interpretations and elaboration of those commitments, OPAs make it easier than PTAs for nations to assert distinctive aspects of their sovereignty, and easier for polities, wary of elites that have proven inattentive to repercussions of globalization, to hold regulatory authorities and their political overseers to account. Third, as mentioned, WTO rules require PTAs to be comprehensive, covering “substantially all trade” between the parties and to accede to a PTA – if this

is possible at all – a prospective member must agree to all the terms of the elaborate compromise struck by the original signatories. PTAs are therefore closed instruments de facto, even if some are not de jure.<sup>12</sup>

Because they are domain specific, accession to an OPA requires a narrower and more limited commitment. A candidate member must only undertake to meet the regulatory requirements of the members as these apply to the particular class of goods and services for which it seeks market access. As members of an OPA require only equivalent performance—not identical procedures or institutions—in conformance testing, standard setting and enforcement in each domain, they permit candidate members to produce the required regulatory outcome by the process best suited to their own traditions and conditions. Finally, accession to an OPA can be achieved step wise, with candidate members establishing the equivalence of their methods in one phase of the regulatory process, or one or another product of a particular class, then another, and another, so that trade expands and collaboration deepens even when full equivalence of regulatory systems is a distant goal.

OPAs centered on good regulatory practices to facilitate trade can be applied on a MFN basis as this is insensitive to free riding considerations. Because the primary focus is on identifying policies that are in the self-interest of countries to implement, there is no need for cross-issue linkages. Indeed, efforts to link different issues may impede agreement by shifting the focus away from defining good practices towards quid pro quo bargaining that characterizes negotiations on subjects where changes in policies give rise to political costs for governments. Nor is it necessary that all major trading powers are part of an agreement. While broad membership increases overall benefits, all that is necessary for cooperation is that enough countries are part of the process to justify participation costs.

Good regulatory practice OPAs do not need binding dispute settlement procedures where the ultimate sanction is the threat of withdrawal of trade concessions (retaliation). If a country no longer applies what was agreed to be good practice it makes no sense to respond by doing the same – both because this will at most have only a small effect on the trading partner and, more important, doing so will be costly as the practice by assumption is beneficial to apply – otherwise it would not have been adopted in the first place. In situations where a party to an agreement decides no longer to apply an agreed practice the appropriate response is to assess the reasons for this decision. If it reflects political economy forces in the partner country driven by rent-seeking behavior by vested interests, this is not a reason to change one's own policy. Alternatively, if the change can be justified as enhancing national welfare, there may be reason to revisit the presumption that the policy constitutes good practice. In principle, however, situations where a party comes to believe there is a better way of regulating should give rise to discussion between parties to an agreement.

Doing more to accept OPAs as a WTO-conforming device through which countries can reduce the international trade costs of regulatory heterogeneity may help regenerate the WTO as a forum for mutually beneficial cooperation on trade-related policies. To the extent that addressing regulatory differences becomes increasingly important for trade and investment OPAs can provide platforms to enhance the relevance of the WTO as a clearing house for registering, comparing and diffusing their results, complemented by facilities for technical support services to candidate OPA members. Through the formation of OPAs with different geographic scope and substantive reach, groups of WTO member countries can both test and re-elaborate alternative regulatory standards and designs for institutional cooperation. The growth or decline of OPAs would demonstrate the attractiveness to newcomers of those that survived this winnowing. In this way OPAs, operating under auspices of the WTO would be dynamic and flexible vehicles by which member states come to reconsider their particular regulatory commitments and institutional habits in light of the experience of like-minded others. The most successful approaches could serve as the starting points for generalization and codification in international standards or framework international agreements of various kinds. A WTO hospitable to OPAs would no longer be hostage to the consensus of its members but be a partner in articulating it.

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<sup>12</sup> The closed nature of PTAs is demonstrated by the UK's difficulty in withdrawing from the EU: all the commercially feasible alternatives to membership entail continuing, deep engagement with the EU regulatory regime, at odds with the reassertion of national sovereignty that motivated Brexit.

### 3.3 Current plurilateral deliberations in the WTO

As noted, several so-called “joint statement initiatives” are being pursued in the WTO – spanning e-commerce, domestic regulation of services, investment facilitation, and measures to enhance the ability of micro and small and medium enterprises (MSMEs) to utilize the trade opportunities. Much of the focus of these talks center on good regulator practices in their areas of concern.<sup>13</sup>

The E-commerce (include 70+ WTO Members) focus on (i) restrictive policies and (ii) digital trade facilitation.<sup>14</sup> Rules on digital trade restrictions policies will be difficult to agree given differences between EU, China and US on issues such as data privacy, the necessary regulatory conditions that must be satisfied for freedom of cross-border data flows, or the need for data localization requirements. Agreement more likely to be feasible on provisions to facilitate digital trade: e.g., use of electronic signatures, e-invoicing; facilitating electronic payment for cross-border transactions; policy transparency or measures in the area of consumer protection (e.g., relating to fraud).

Domestic regulation talks involve 50+ WTO Members and center on matters associated with authorization and certification of foreign services providers (licensing, qualification, and technical standards), not on substance of regulations. While some WTO members would prefer to include a substantive commitments that reduce the trade-impeding effects of domestic regulation, such as a “necessity test” or language calling for countries to adopt regulations that minimize trade restrictive effects (“least trade restrictiveness” language), the experience of previous efforts in the WTO to get agreement on such principles suggests the main outcome will involve trade facilitation measures, e.g., agreement to publish information; create enquiry points; establish good practice timeframes for processing of applications; acceptance of electronic applications, use of objective criteria, and ensuring authorizing bodies are independent and/or impartial and decisions can be appealed.

The investment facilitation group was launched by 70 WTO Members and at the time of writing encompasses some 90 WTO members.<sup>15</sup> The agenda does not include liberalization of inward FDI policies or measures related to protection of foreign investors. The focus is solely on facilitation. All investment is covered, including services, i.e., facilitation of mode 3 is part of the discussion. Talks center on “good regulatory practices” such as transparency and predictability of investment-related policy measures; streamlining administrative procedures and requirements; international cooperation, information sharing, and exchange of best practices (learning) by bringing together stakeholders within countries concerned with FDI; soliciting feedback on proposed regulatory measures; ensuring transparency of regulatory processes and use of ex post monitoring and evaluation of implementation impacts.

For much if not most of the agenda pursued in these groups free riding is not a serious concern in that the goal is not to reduce discrimination against foreign providers but to improve regulatory processes. Insofar as this is the case, a corollary is that OPAs on such subjects need not include all the majors. Participation by just one of two of the majors in addition to like-minded small and medium-sized economies may be enough to reduce the trade-cum-transaction costs effects of regulatory heterogeneity by more than the associated negotiation costs, while providing a mechanism that helps countries achieve their regulatory goals more efficiently.

Matters are less clear cut when it comes to policy areas where cooperation spanning the major trade powers is needed to internalize negative spillovers. This is the case for e-commerce-related policies affecting cross-border data flows and digital transactions. It also applies to policy areas such as subsidies and state-owned enterprises (SOEs) and the use of trade policy as a component of programs to combat climate change. In all these instances, policies give rise to potentially significant international spillovers. Importantly, however, in all these areas the matter is not simply one of dealing with competitive effects of policies. Account must be taken that policies may – and

<sup>13</sup> [https://www.wto.org/english/news\\_e/news17\\_e/minis\\_13dec17\\_e.htm](https://www.wto.org/english/news_e/news17_e/minis_13dec17_e.htm). Participation in these groups spans a broad cross-section of the membership. The EU participates in all four groups. The US is part of one (e-commerce). China was a sponsor of three of the four groups – initially it decided not to join the group on e-commerce but joined subsequently. Independent of whether a WTO member is a sponsor/supporter of a group, deliberations of the groups are open to all.

<sup>14</sup> For a summary of the issues that have been tabled by different participants, see <https://etradeforall.org/wto-members-submit-proposals-aimed-at-advancing-exploratory-e-commerce-work/>.

<sup>15</sup> [https://www.wto.org/english/news\\_e/news19\\_e/infac\\_05nov19\\_e.htm](https://www.wto.org/english/news_e/news19_e/infac_05nov19_e.htm). See Echandi and Sauve (2019) for an assessment of the issues being discussed.

often will – be used to deal with international collective action problems and market failures. Cooperation then calls for considering underlying goals and how to attain these most efficiently. Doing so requires policy dialogue with a view to identifying the magnitude of negative effects of specific policies and approaches that reduce potential adverse impacts on foreign producers and distortions to competition (Hoekman and Nelson, 2020a,b). The same need arises for digital economy policies and governing the use of trade policies (e.g., border carbon adjustments) as an element of programs aiming to reduce national carbon footprints as envisaged by the EU (von der Leyen, 2019).

## 4 Preparing the ground for OPAs

Whether the large trading powers will be able (willing) to pursue cooperation on a plurilateral basis to agree on rules of the game for contested policy areas like industrial subsidies is very much an open question. In part, this will depend on the experience that emerges from the plurilateral talks launched after the December 2017 WTO Ministerial meeting in Buenos Aires and whether agreements that emerge are implemented on a nondiscriminatory basis. The point we would stress here is that there are many additional issues that need to be addressed and that lend themselves to OPAs, and that WTO members would benefit from seeking to cooperate on these matters through OPAs. The prospects for success of efforts to do so will be enhanced if they are based on a solid evidence base, and if proponents of OPAs would agree to a code of conduct to address potential concerns of non-participating countries. We discuss each of these in turn.

### 4.1 Informed plurilateral engagements and deliberation

Successful international agreements addressing regulatory policies such as the WTO agreements on sanitary and phytosanitary measures, technical barriers to trade and trade facilitation are all associated with a body of agreed technical knowledge and accumulated good will among the relevant national regulatory agencies. Haas (1992) refers to a group of stakeholders and experts linked in this way as an epistemic community. Specifically, he defines an epistemic community as a group of professionals who share:

- a set of normative and principled beliefs, which provide a value-based rationale for the social action of community members;
- causal beliefs, derived from their analysis of practices to address problems in their domain, that serve as the basis for understanding linkages between possible policy actions and desired outcomes;
- notions of validity—criteria for weighing and validating knowledge in the domain of their expertise; and
- a set of common practices—associated with the problems to which their professional competence is directed with a view to enhance welfare.

There are a wide variety of policy domains in which such epistemic communities help support international cooperation, including trade facilitation, competition policy (Kovacic and Hollman, 2011); environmental policy (Abbott, 2012) and product safety (Livermore, 2006). A necessary condition for successful OPAs is a community that has an interest in international regulatory cooperation and a mechanism that supports informed deliberation in each policy area (Hoekman and Sabel, 2019; Hoekman and Nelson, 2020a,b). Such mechanisms can include what is sometimes called a knowledge platform, a forum aimed at fostering a substantive, evidence and analysis-based discussion of the impacts of sector specific regulatory policies. Such fora can generate information on applied policies across countries, facilitate sharing experiences and help to identify good practices that reflect and respond to local capabilities and priorities. APEC, the OECD and the World Bank are examples of entities that provide institutional homes for this type of engagement.

A common denominator underpinning the launch of several of the new plurilateral deliberations in the WTO is that they benefitted from joint engagement by international organizations working through the G20 Trade and Investment Working Group. This is the case most clearly for investment facilitation discussions but also applies to e-commerce and talks on MSMEs. As discussed below, the G20 also created the Global Forum on Steel Excess Capacity in 2016, a forum that has many of the characteristics of a potential OPA. G20 summits bring together

Leaders have the ability to cut across prevailing silos in government to bring together the key actors at national level in ways that sectoral ministers (e.g., trade ministries) cannot. Insofar as the source of cross-border spillovers is associated with national tax/subsidy measures, these will be under the purview of Finance Ministries—who play a prominent role in G20 deliberations. Many of the contentious potentially spillover-creating policies put in place by governments since 2009 are tax and subsidy related (Evenett, 2019). This makes the G20 a particularly relevant forum to discuss and address the cross-border effects of domestic regulatory measures. More broadly, given differences in national priorities and capacity sustaining cooperation may require transfers – technical and/or financial assistance. Trade ministries do not have such instruments and may find it difficult to orchestrate them when needed to support international agreements. The fact that the major international organizations are part of the G20 process (i.e., participate in the TIWG) is another positive feature of seeking a G20 mandate for the pursuit of OPAs on specific policy areas of common interest to a plurality of G20 countries. The agencies that are part of the TIWG are not at the table in WTO negotiations.

A prominent example where the G20 has played a role in establishing a forum for dialogue and deliberation is the G20 Global Forum on Steel Excess Capacity (GFSEC), established at the 2016 G20 summit in China.<sup>16</sup> The three-year mandate of this forum, which ran from 2017-2019, included producing and sharing reliable statistics on production, capacity and excess capacity across major steel producers, and identifying measures to reduce global production. It was managed/supported by the OECD secretariat. The forum provided a platform for the exchange of data on steel capacity, subsidies and other support measures, thus improving the information base and the transparency of the relevant policies implemented by major steel producing countries. The forum reported to G20 Ministers annually during 2017-2019 and met at least three times a year during this period. The forum included both governments and industry. The latter were a key source of information on production and investment trends but did not participate in discussions relating to steel sector policies. The forum reported to G20 Ministers annually during 2017-2019 and met at least three times a year during this period.

The GFSEC focused on just one sector, steel, and could draw on expertise at the OECD, an international organization with deep knowledge of the sector, based on the operation a Steel Committee that has been in place since 1978. The exercise had high level political support because it was both a G20 initiative and was launched while China held the presidency. Such high-level support is likely to be a necessary condition for success in any effort to increase transparency and develop rules of the game for policies that generate international spillovers. This is certainly a lesson that can be drawn from the experience of developing the Producer Support Estimate (PSE) for agriculture, where demand from OECD Ministers of Finance was an important factor in creating the political space for the OECD secretariat to sustain the effort to measure and analyze the effects of agricultural support policies (Wolfe, 2020c). The agriculture/PSE example also suggests the importance of a sense of crisis – that a matter is of sufficiently great economic and political salience to generate a common view that action is required.

A distinct feature of the GFSEC was the obligation imposed on the OECD secretariat to maintain confidentiality of data provided – including within the organization. The OECD was required to agree to nondisclosure agreements prohibiting publication of data provided by participating governments and limits on what it was permitted to do in the way of analysis or putting information on the table – including data that had already been compiled by and for the OECD Steel Committee. One reason for this was that some of the major global players in the steel sector are not OECD members. Members defined the contours of the policy focus of GFSEC activities – measures deemed to result in or sustain excess capacity – as opposed to a broader view of policies. The GFSEC did not seek to establish a comprehensive baseline dataset spanning all steel-related policy support provided by different levels of governments in a country. A consequence was an inability to assess the effects of policies, even if the OECD had been mandated to so, which it was not. The type of analysis done by the OECD on aluminum and semiconductors for its Trade Committee was not done for steel because of the circumscribed mandate given to and by the GFSEC. Although the GFSEC helped governments to better understand their own national policies and those of other countries, the experience suggests careful consideration be given to trade-offs associated with seeking a mandate from the G20 to establish a platform to consider subsidies. An open initiative centered around a small number of high quality policy research institutes working with former senior officials who are respected and

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<sup>16</sup> What follows draws on Hoekman and Nelson (2020b),

trusted by their peers in the international policy community would be less constrained by political factors in implementing a knowledge platform to support deliberations and eventual negotiations on new rules among a critical mass of countries.

In practice effective OPAs are likely to be policy and/or sector-specific, bringing together the WTO (trade community) with other organizations that have a mandate in an area of overlapping interest. On climate change, for example, the Paris Agreement and the WTO provide a basis for the formation of linked OPAs to support domain-specific decarbonization regimes. The Paris Agreement authorizes countries to set national decarbonization targets and to form sector-specific ‘climate clubs’ for joint pursuit of national targets outside Paris and to count progress achieved there towards their voluntary goals. An implication of the voluntary nature of national commitments under Paris is that any penalty defaults defined by climate clubs involving trade restrictions fall outside Paris. Although countries can invoke the general exceptions provision of the WTO to justify the use of trade measures as part of decarbonization initiatives, an OPA can make explicit how trade sanctions will be applied among members of the OPA to attain decarbonization targets they have agreed.<sup>17</sup>

## 4.2 Governance of OPAs: Towards a Code of Conduct

As noted, plurilateral initiatives offer a way to attenuate the need for consensus, but are not a panacea, as free riding concerns can block cooperation by all the major powers. OPAs, even if open, raise potential concerns for nonmembers. First, if free riding considerations induce signatories to exclude non-participants from benefitting from whatever they have agreed to do. Second, even if – as we assume will be the case – agreements do not discriminate, countries that decide not to participate will not have obligations but nonetheless may have an interest in what is agreed to constitute good practice by a plurilateral group. In part this is because they may want to participate later, and in part because their firms may have to comply with whatever policies are adopted by a club of WTO members.

In practice not all countries will be able to engage on an equal footing in the negotiation of an OPA. There are major differences in capacities to engage on regulatory matters and the ability to participate in a fully informed way. Some governments may find it difficult to determine the ‘return’ to applying a proposed rule (e.g., the direct administrative costs or the size – and perhaps even the sign – of the net economic impact of implementing a proposed set of disciplines). This suggests that any OPA should include an aid for trade component—mechanisms to assist countries improve their standards, regulation, etc. to the level that is required to benefit from the OPA. Including an operational aid for trade dimension in OPAs could enhance their relevance to low-income countries and enhance their inclusiveness.

Ensuring that agreements are truly open to any country wishing to join, are fully transparent, and encourage participation by international and sectoral organizations with relevant expertise could help address potential concerns of nonmembers. Particularly important are to put in place mechanisms to assist countries not able to participate despite being interested in doing so because of weaknesses in institutional capacity and capabilities. Addressing these types of concerns is important. One way to do so is through establishment of a code of conduct that signatories of plurilateral agreements commit to apply (Lawrence, 2006, WEF, 2010, Draper and Dube, 2013 and Hoekman and Mavroidis, 2015a). Providing a governance framework for new plurilateral agreements that ensures they are consistent with multilateralism would help to recognize valid concerns of nonmembers.

Such a framework can take the form of binding code of conduct that is incorporated in the schedules of commitments of WTO members that decide to apply them. There is a precedent for this in the General Agreement on Trade in Services (GATS), where a so-called Reference Paper on basic telecommunications sets out specific obligations on the behavior of telecom operators that control access to the network. These disciplines become binding on signatories, and thus enforceable, through inclusion of the Reference Paper into their schedule of GATS commitments. Such inclusion cannot be blocked by any country as WTO members are free to make additional commitments if they wish to (Hoekman and Mavroidis, 2017). A Reference Paper on OPAs could be

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<sup>17</sup> See Sabel and Victor (2019) for an extended discussion of how the trade and climate regimes can be brought together to support climate clubs.

incorporated in the schedules of members who drafted it, with any WTO member interested in participating in an OPA negotiation or acceding to an OPA accepting to incorporate the paper into their schedules. As amendment of the WTO to include new provisions to govern the design elements of OPAs will be difficult if not impossible given the need for consensus, a pragmatic approach to incorporating a code of conduct is for a common Reference Paper to be incorporated into each new OPA that is negotiated.

A Reference Paper on OPAs could include the following elements:

1. A provision making explicit that membership of an OPA is voluntary and that WTO members that decide not to participate cannot be obliged to join at a later date;
2. The OPA is open to subsequent membership by WTO Members that did not join when it was first agreed;<sup>18</sup>
3. A section laying out the requirements and procedures to be followed for accession by aspiring members;
4. A commitment that accession to an OPA cannot be on terms that are more stringent than those that applied to the incumbent parties, adjusted for any changes in substantive disciplines adopted by signatories over time;<sup>19</sup>
5. Where feasible and in instances where capacities must be built for a country to meet OPA requirements, consideration be given to establish a stepwise schedule of compliance;
6. A binding and enforceable provision committing signatories to provide assistance to WTO members that are not in a position to satisfy the preconditions for membership in terms of applying the substantive provisions of the agreement but desire to do so;<sup>20</sup>
7. Inclusion of consultation and binding conflict resolution procedures to be used by non-signatories of OPAs in cases where they perceive that incumbents impose more stringent conditions to accede to an agreement than apply to extant parties to the OPA, or if parties to an OPA do not live up to the commitment to respond to requests to provide assistance to nonmembers;
8. Provisions that ensure the OPA is open in the sense of including transparency mechanisms to ensure that nonparticipants have full information on the implementation and operation of the agreement. These should include:
  - a. Compliance with WTO requirements pertaining to publication of information on measures covered by the OPA;
  - b. Simple, robust notification requirements for OPA members, which could draw on recent proposals to develop augmented procedural guidelines for the operation of WTO bodies;<sup>21</sup>
  - c. Regular thematic sessions of the body overseeing implementation of the OPA to engage stakeholders in an ongoing conversation about how the agreement is working and future needs;<sup>22</sup>
  - d. Annual reporting to the WTO General Council by the OPA on its activities;
  - e. A mandate for the WTO Secretariat to assess the effects of implementing OPAs on the functioning of the trading system as part of the Director-General's annual monitoring report of developments in the trading system.

These principles do not include a requirement to provide 'special and differential treatment' (SDT) of the type currently embodied in the WTO which permits developing countries to offer 'less than full reciprocity'. One reason is that this bring back a major reason for current deadlock in the WTO: insistence by some WTO members that more advanced emerging economies should participate on an equal basis. More substantively, this traditional notion of SDT would defeat a major rationale for pursuing many OPAs: to permit subset of countries to cooperate in areas not covered by WTO rules or to go beyond them by adopting what all agree are good policy practices.

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<sup>18</sup> Open access in the sense that once negotiated any OPA allow for accession by any WTO Member is not explicitly required in Art. X.9 WTO. Instead, accession provisions will be defined in each OPA. It would be desirable to agree explicitly that 'open access' ex post be a precondition for any OPA under the WTO.

<sup>19</sup> This leaves open the possibility that parties to an OPA can offer accession on less demanding terms for developing countries if they agree to do so.

<sup>20</sup> Such provisions can draw on the approach embodied in the TFA – see e.g., Hoekman (2016).

<sup>21</sup> See Wolfe (2020a) for an extended discussion.

<sup>22</sup> Wolfe (2020b) discusses how WTO bodies could do more to organize periodic sessions that focus on learning and engagement with stakeholders.



Insofar as OPAs deal with regulatory matters it makes no sense to consider that some countries should only partially implement whatever standards and processes are agreed, as this would undercut the achievement of common regulatory objectives of OPA members. The requirement that parties to OPAs must assist non-members desiring to participate but unable to do so because of capacity weaknesses addresses development differences more effectively than traditional SDT. How to ensure that this is a credible commitment is something to be determined by OPA members. One option is to include a provision establishing an earmarked trust fund to finance assistance when this is requested.

## 5 Conclusion

The success of the multilateral trade regime in the post-Second World War period was attributable in large part to US leadership and the fact that the organization was dominated by broadly like-minded countries. Today the WTO is much more inclusive with 164 members, and as a result much more heterogeneous. This was a factor impeding successful conclusion of the Doha round and the increase in trade tensions. PTAs have partially filled the gap but are not well suited to address the sources of current global trade tensions or to reduce the costs of regulatory heterogeneity. Trade agreements are designed to deal with specific problems: internalizing terms-of-trade spillovers and addressing the potential time inconsistency of policy commitments. Problems involving the appropriate design of regulatory responses to market failures, monitoring and evaluation systems to support learning and adaptation of policies over time, and reducing the transactions costs for international business from differences in regulation for a given sector or activity call for a different form of cooperation.

What is needed are initiatives among like-minded jurisdictions to identify and agree on good practices in a domain or sector and balancing the achievement of noneconomic objectives against competitive spillovers. Both the WTO and most PTAs do little to help countries learn how best to attain regulatory objectives and improve regulatory efficiency and effectiveness over time. OPAs offer a potentially superior vehicle to do so. Contrary to arguments that plurilateral initiatives are second best in a world where consensus is not obtainable, depending on the type of issue, OPAs can be a first-best response, especially where the problem is to reduce the trade costs of regulatory heterogeneity. Cooperation on regulatory matters does not necessarily require large-N participation, cross-issue linkages or the type of reciprocity that is a basic feature of market access negotiations. Indeed, OPAs may also be a path forward in addressing some of the sources of current trade conflicts such as industrial subsidies that are perceived to distort the competitive landscape and international collective action problems, most urgently and importantly, decarbonization of economic activity.

Of the so-called “joint statement initiatives” that are now being pursued in the WTO – spanning e-commerce, domestic regulation of services, investment facilitation, and measures to enhance the ability of micro and small and medium enterprises (MSMEs) to utilize the opportunities offered by the rules-based trading system – most address coordination failures or entail joint efforts to identify good regulatory practices. This is valuable. The subjects of discussion are all areas where there are potential gains from cooperation and policy coordination. However, apart from the e-commerce talks, they do not address fundamental sources of recent trade tensions and conflicts. Nor do they deal with matters that are likely to become increasingly prominent, notably the use of trade policies as an element of regulatory regimes designed to decarbonize the economy and combat climate change. For the credibility of the WTO it is critical that most of the ongoing plurilateral discussions result in OPAs. What matters even more looking forward for sustaining an open, rules-based multilateral trading system is greater use of OPAs to manage industrial policy spillovers, regulate the digital economy and govern the use of climate change-motivated trade policies.

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