



## Open Plurilateral Agreements, Global Spillovers and the Multilateral Trading System<sup>1</sup>

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National policies can give rise to negative cross-border spillovers. Addressing cross-border policy spillovers requires identifying those that are systemically significant and designing international cooperation 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 international rulemaking initiatives – including by the EU – 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 non-discriminatory 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.

### ***Why consider OPAs as a complement to PTAs?***

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.

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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 about 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).

OPAs among groups of countries are more appropriate instruments to address the trade costs created by regulatory heterogeneity because the issues are more complex than the "terms-of-trade"-cum-commitment problems that trade agreements are appropriate solutions to. 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 what constitutes good practice and balancing the achievement of non-economic 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.

The EU has actively supported efforts by many WTO members to negotiate new OPAs. The associated talks – so-called "joint statement initiatives" – were launched at the end of 2017 at the WTO ministerial conference in Buenos Aires. The subjects being negotiated span e-commerce, domestic regulation of services, investment facilitation, and measures to enhance the ability of micro and small and medium enterprises to utilize the opportunities offered by the rules-based trading system. Much, if not most, of what is on the table concerns coordination failures or entails joint efforts to identify good regulatory practices. To sustain the relevance of the WTO it is critical that at least some of these plurilateral discussions result in agreements. But what matters more for sustaining an open, rules-based multilateral trading system – a core external policy objective of the European Union – is that efforts are extended to use OPAs to manage industrial policy spillovers, regulate the digital economy and govern climate change-motivated trade policies – policy areas that have been, or will become – sources of trade tensions.



### ***Supporting plurilateral engagement***

Hoekman and Sabel (2021) argue the prospects for successfully expanding the scope to negotiate OPAs would be enhanced if efforts are made to agree to a code of conduct for OPAs to address potential concerns of non-participating countries.

A necessary condition for successful OPAs is informed deliberation in a given policy area and substantive, evidence and analysis-based discussion. Without robust information on applied policies across countries and analysis of their effects it is not possible to identify and agree on good practices, whether and which policies create large cross-border 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, 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 and expertise in an area of overlapping interest. On climate change, for example, the Paris Agreement provides 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. Pursuit of plurilateral cooperation by the EU in this area would help to legitimize the use of carbon border adjustments as proposed by the Union and provide a stronger basis to address allegations that the EU is acting unilaterally and in a discriminatory manner.



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 and improve global welfare. 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. Participation can be selective, with a WTO member deciding to join some OPAs but not others. Several non-EU countries have gone down the plurilateral track already. In the Asia Pacific region several APEC economies have concluded digital economy partnerships that are open to other countries to join. Several Asia-Pacific and EFTA countries are negotiating a plurilateral Agreement on Climate Change, Trade and Sustainability. The EU has chosen not to participate in such initiatives, instead limiting its plurilateral engagements to the WTO joint statement initiatives. Implicitly, if not explicitly, it appears that the EU is relying on its purported regulatory market power – the “Brussels effect” to justify a primarily unilateral approach to the pursuit of non-trade policy objectives. Hoekman and Sabel argue this is misconceived and is likely to have avoidable opportunity costs if greater effort was devoted to the conclusion of OPAs with like-minded nations.

### ***A set of principles 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 non-members. Even if – as we assume will be the case – agreements are applied on a non-discriminatory 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 non-members 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 and take the form of a Reference Paper that would be incorporated into each OPA.

Principles for OPAs could include the following elements:

1. Membership is voluntary; WTO Members that decide not to participate initially will not be pressured to join subsequently.



2. Openness to subsequent accession by WTO Members that did not join when an OPA was first agreed, and inclusion of a section laying out the requirements and procedures to be followed for accession by aspiring members.
3. Language stating that accession to an OPA cannot be on terms that are more stringent than those applied to the incumbent parties, adjusted for any changes in substantive disciplines adopted by signatories over time.
4. An obligation to provide reasons to accession-seeking countries for decisions to reject membership applications.
5. The agreement must be implemented on a non-discriminatory basis, with benefits extending to non-signatories. Insofar as benefits are conditional on satisfying requirements pertaining to standards of regulation and regulatory enforcement in a jurisdiction, these should be clearly specified.
6. A provision committing signatories to assist WTO Members that are not yet able to satisfy the institutional/regulatory preconditions for membership in terms of applying specific substantive provisions of the agreement but desire to do so.
7. Wherever it is appropriate 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. Wherever possible, designing agreements to permit 'incremental' accession – adoption of specific disciplines that can be implemented on a separable basis, as is the case under the Trade Facilitation Agreement (TFA) and foreseen in the modular approach taken in recent digital partnership agreements (see below) – can help to encourage participation.
8. Provisions ensuring that non-participants have full information on the implementation and operation of the agreement. These transparency-related requirements should include:
  - a. Compliance with WTO requirements pertaining to publication of information on measures covered by the OPA (along lines of Art. X GATT).
  - b. Simple, robust notification requirements for OPA members regarding the implementation of the agreement, which could draw on recent proposals to develop augmented procedural guidelines for the operation of WTO bodies.
  - c. Creation of a body to oversee implementation of the OPA that is open to observation by non-signatories, including mechanisms to engage 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.
  - 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.
9. Inclusion of consultation and conflict resolution procedures for non-signatories of OPAs in cases where they perceive that incumbents do not live up to the code of conduct adopted by signatories.
10. Provisions indicating whether the OPA envisages recourse to WTO dispute settlement mechanisms to enforce the agreement, and if so, specifying the standard of review as well as the



criteria that will apply in the selection of arbitrators – e.g., to assure arbitrators have the expertise required in the subject matter addressed by the agreement.

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.

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