# Innovative Mechanisms for Resolving or Avoiding Inter-State Trade Disputes in an Asia-Pacific Regional Free Trade Agreement

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## Abstract

This article elaborates upon ideas contributed to a symposium considering the possible shape of an Asia Pacific Community, including future trade arrangements within an Asia Pacific Community. It suggests some innovations in dispute settlement that could be considered for inclusion in such arrangements. The author suggests some innovative mechanisms by focussing on the way in which trade agreements and the dispute settlement mechanisms influence the internal political position of governments. The first mechanism would provide for a pre-quantification of the extent of retaliation that would be permitted should a complaint be successful. This mechanism would encourage respondent governments to focus earlier on weighing the potential loss of political support from exporters with any political support from import competing producers. The second mechanism would provide for free publication of an expert economic report on the economic welfare cost to the respondent of maintaining the protectionist measure subject to the complaint. This mechanism could increase the political weight attributed by the respondent government to the overall economic effects of the controversial measure. The paper further suggests that something similar to the second mechanism could be adopted as a separate transparency mechanism unrelated to dispute settlement. Such a mechanism might make it more likely that governments reform protectionist measures so as to avoiding the possibility of any legal dispute ever arising.

## Introduction

The article in this issue by Micah Burch and Luke Nottage[1] describes some of the regional and bilateral trade initiatives (for example, the Asia-Pacific Economic Cooperation forum[2]) and some of the bilateral and regional trade agreements ('BRTAs') (for example, the Japan

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[1] Micah Burch and Luke Nottage, 'Novel Treaty-Based Approaches to Resolving International Investment and Tax Disputes in the Asia-Pacific Region', (2011) 18 *Australian International Law Journal* 127.

[2] The Asia-Pacific Economic Cooperation ('APEC') forum was established by 12 economies as an informal Ministerial level dialogue group in 1989. Now its membership comprises 21 economies and it facilitates dialogue at various levels. Asia-Pacific Ecomomic Cooperation *Key Apec Milestones* (2012) <http://www.apec.org/About-Us/About-APEC/History.aspx>.

Singapore Free Trade Agreement of 2001,[3] the Australian Singapore Free Trade Agreement of 2003,[4] the ASEAN-China Framework Agreement,[5] the Trans-Pacific Partnership Agreement of 2005 between Brunei Darussalam, Chile, New Zealand and Singapore)[6] in place and under negotiation (the proposed ASEAN plus three — ie China, Japan and Korea — the expansion in membership of the Trans-Pacific Partnership) among nations of the Asia-Pacific region. Burch and Nottage then discuss some novel approaches to mechanisms which could be built into existing agreements or any further agreements in the region to help resolve disputes:

1. the inclusion of investor State arbitration mechanisms for resolving disputes arising when States engage in conduct that detrimentally affects foreign investors; and

2. the inclusion of mandatory arbitration provisions like those in the Organisation for Economic Cooperation and Development ('OECD') model tax treaty for resolution of double tax disputes enabling taxpayers to ensure double tax disputes between different States are resolved.

This article makes some suggestions for novel approaches to resolving disputes between States arising from alleged breaches of the market access commitments contained in any BRTA among Asia-Pacific nations. These mechanisms could be considered in the context of existing BRTAs or in new BRTAs under negotiation or indeed in any wider Asia-Pacific Economic Community should such a thing ever come into existence. The suggested mechanisms are designed to be compatible with any unilateral initiatives in individual countries or to be capable of being multilateralised into World Trade Organization ('WTO') rules should any pair or group of Asia-Pacific countries find the mechanism workable and worthy of a proposal for amendment of WTO dispute resolution procedures.

The suggested mechanisms for resolving trade disputes between States are:

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3    *Agreement between Japan and the Republic of Singapore for a New-Age Economic Partnership*, done Singapore, 13 January 2002; UN registration number I - 48385; in force 30 November 2006. For Japan's various BRTAs, see <http://www.meti.go.jp/english/policy/external_economy/trade/FTA_EPA/index.html>.

4    *Singapore-Australia Free Trade Agreement*, done Singapore, 17 February 2003; in force 28 July 2003; 2257 UNTS 103 (UN No 40211); [2003] ATS 16. For Australia's various BRTAs, see: Australian Government Department of Foreign Affairs and Trade, *Australia's Trade Agreements*, <http://www.dfat.gov.au/fta/index.html>.

5    *Framework Agreement on Comprehensive Economic Co-operation between ASEAN and the People's Republic of China*, done Phnom Penh, 4 November 2002; <http://www.aseansec.org/20164.htm> (not recorded in UN database of Depositary Notifications <http://treaties.un.org/pages/CNs.aspx>; not published in UNTS) Pursuant to the Framework agreement, the parties have entered into the *Agreement on Trade in Goods of the Framework Agreement on Comprehensive Economic Co-operation between Association of South East Asian Nations and the People's Republic of China*, done Ventianne, 29 November 2004, in force 1 January 2005 and the *Agreement on Trade in Services of the Framework Agreement on Comprehensive Economic Co-operation between Association of South East Asian Nations and the People's Republic of China*, done Cebu, 14 January 2007, in force 1 July 2007 (not recorded in UN Treaty Collection <http://treaties.un.org/Home.aspx?lang=en>). The WTO website <http://rtais.wto.org/UI/PublicShowMember RTAIDCard.aspx?rtaid=42> records these two treaties as having been notified to the WTO on 21 September 2005 and 26 June 2008 respectively (neither are recorded in UN Treaty Collection <http://treaties.un.org/Home.aspx?lang=en>). For BRTAs entered between ASEAN countries and other countries see Association of Southeast Asian Nations *External Relations* <http://www.aseansec.org/20164.htm>.

6    Trans-Pacific Strategic Economic Partnership Agreement between Brunei Darussalam, Chile, New Zealand, and Singapore, done Wellington 18 July 2005; in force for NZ and Singapore 28 May 2006 (frequently described as 'TPP4') The author is not aware of any hard copy publication but see New Zealand Ministry for Foreign Affairs and Trade, *Trans-Pacific Strategic Economic Partnership Agreement* (30 September 2011) <http://www.mfat.govt.nz/Trade-and-Economic-Relations/2-Trade-Relationships-and-Agreements/Trans-Pacific/3-Understanding-P4.php>.

1.  a mechanism for pre-quantifying the extent of permissible retaliation, that is: provision for an early estimation of the possible retaliation that could be imposed should a complaint be successful; and

2.  a mechanism for making the economic welfare costs of measures allegedly in breach of market access commitments transparent and widely known.

Both suggested mechanisms are based on the same theoretical approach to trade agreements and their dispute settlement provisions. The approach to explaining the function of trade agreements relies on a variation of a model called the Trading Nations Dilemma as set out in the 1985 article by Kenneth Abbott.[7] The approach of that model and this explanation of it in describing the pressures within governments is sometimes called the 'public choice' or 'political economy' approach.[8] It is not the only model used to explain behaviour of States or the functions of trade agreements.[9] However, this article does not attempt to critique the model, or assess the merits of the different models of trade agreements.

## The theoretical background

The decisions of governments of any States about trade policy can be seen as being a function of political pressures. The trade policy measures that a government implements may affect the level of political support and political opposition that it faces. Successful models of government behaviour in the area have incorporated various sources of political pressures.[10] The simplified matrix below (Table 1) is representative of the typical political economy approach to explaining the political pressures (and it approximates the political factors set out in Abbott's article referred to above).

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[7]  Kenneth Abbott, 'The Trading Nations Dilemma: The Function of the Law of International Trade' (1985) 26 *Harvard International Law Journal* 501–32.

[8]  Abbott's model sets out the payoffs in terms of political support to trading nation governments not the payoffs in terms of economic consequences to the trading nations. He relies on public choice theory as it then stood based on some early works which concentrated on voting behaviour (see Abbott, above n 7, 514–16 and footnotes 68–77) Although there have been further developments in public choice theory, the essence of the Trading Nations Dilemma model is still relevant.

[9]  A terms-of-trade approach is popular. Leading works describing a terms-of-trade approach are: K Bagwell and R W Staiger, 'An Economic Theory of GATT' *American Economic Review* 89(1), 215–48 and K Bagwell and RW Staiger, *The Economics of the World Trading System* (MIT Press, 2002). There is some controversy as to the utility of the terms of trade approach to explaining trade behaviour and trade agreements. For example, Wilfred Ethier argues that the terms of trade approach is certainly inferior to a public choice or political economy approach: see, eg, Wilfred J Ethier, 'Political Externalities, Non-discrimination, and a Multilateral World', Penn Institute for Economic Research, PIER Working Paper 02-030, 5 September 2002; <http://www.econ.upenn.edu/pier> or <http://ssrn.com/abstract_id=333006>, and Wilfred J Ethier, 'Trade Policies Based on Political Externalties: An Exploration' PIER Working Paper 04-006, 2 February 2004; <www.econ.upenn.edu/pier> or <http://ssrn.com/abstract=498464>.

[10]  Some models are based on calculating the outcomes of voting and others focus more on calculating the incentive to donate political contributions. In the latter category, the leading work is Gene M Grossman, and Elhanan Helpman, 'Protection for Sale' (1994) 84 *American Economic Review* 833–50.

**Table 1:   Political support and opposition to a government reducing protection
against imports**

| Key factors | Political influence |
|---|---|
| Import competing producers | Against reducing protection (significant weight) |
| Consumers | In favour of reducing protection, but negligible weight in most circumstances |
| Importance placed on national welfare | In favour of reducing protection/ Against protection, but negligible weight in most circumstances |
| Exporters | In favour of reducing protection because protection to another sector is equal to a tax on the export sector, but negligible weight in most circumstances because exporters are not engaged in the decision or do not understand its effects |
| *In aggregate: Which decision will maximise political support and minimise opposition?* | *Likely political decision: Not to reduce protection/ to grant protection* |

Import competing producers have a clear and significant financial interest in supporting a government which grants them protection. Though there are other groups which have an interest in supporting a reduction in protection, they are likely to have a negligible influence on political decision making in most circumstances:

- consumers gains are usually dispersed among a large group (with some exceptions) so that, for any individual, the cost of engaging in political activity is larger than the gain from reducing protection;[11]

- the influence upon politicians of the value of enhancing national welfare will be diminished by the fact that political gains from enhancing national welfare would accrue much further into the future than the immediate political gains and losses from sectors directly and immediately affected by a political decision;[12] and

- exporting producers do lose indirectly from a decision to grant protection to other producers but they may not understand that and, even if they do, their loss is quite dispersed so that the cost of influencing political decision may exceed their gain from being successful in influencing the relevant political decisions.

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[11]   See Abbott, above n 7, 514–15 for further elaboration on why consumer interests tend to have small political weight.

[12]   Abbott, above n 7, 516.

Therefore, in many (though not all) circumstances, the only significant political pressure affecting a government will be the pressure from import competing producers. This means that a government interested in maximising political support would choose to grant protection in many, even if not all, circumstances.

If we construct a trade agreement in which two trading nations, TN1 and TN2, exchange tariff reductions, then the exporters in each nation would gain from the implementation of the agreement so they would have an incentive to provide political support to their government to enter into the agreement. Once a draft agreement specifies market access to the other country which would provide gains to exporters, then those exporters have an incentive to provide political support for entering into the agreement. As a political group, the exporting producers have many of the same characteristics as groups of import competing producers so they are likely to exert political influence of a comparable magnitude.

Therefore, by bringing the possible trade agreement into consideration, the political situation affecting a decision to reduce protection changes to that set out in the second column of Table 2.

**Table 2:  Impact of a trade agreement on political support**

| In the absence of any trade agreement | In the presence of a trade agreement |
|---|---|
| *Supporting protection* | *Supporting protection* |
| Import competing producers (significant weight) | Import competing producers (significant weight) |
| *Opposing protection* | *Opposing protection* |
| Consumers (but negligible weight) | Consumers (but negligible weight) |
| Value of national welfare (but negligible weight) | Value of national welfare (but negligible weight) |
| Exporters because opposed to indirect tax arising from protection of others (but negligible weight) | Exporters because opposed to indirect tax arising from protection of others (but negligible weight) |
|  | Exporters' support based on benefitting from negotiated market access (significant weight) |

The critical thing is that in the absence of a trade agreement, there is frequently only one significant influence on the government, whereas when decisions on trade policy are made in the context of a trade agreement, there are two groups that have a significant

bearing on the political support or opposition accruing to the government making the trade policy decision: the import competing producers ('ICPs') and the exporters ('Es').

In the presence of a trade agreement, the way that these internal political pressures influence the interaction between different countries can be illustrated by the following matrix showing interaction between the governments of two trading nations. The matrix is based on the political pressures described above, and an important element is that it is based on the assumption that all of the political influences other than ICPs and exporters gaining from market access are of trivial magnitude justifying leaving them out of the matrix.

For the government of Trading Nation 1, ('TN1'), maintaining or increasing protection leads to a gain in political support from ICPs (represented by a payoff of '+ICP') but reducing protection leads to opposition from ICPs (represented by a payoff of '-ICP'). Trading Nation 2 ('TN2') receives the same payoffs from ICPs for either maintaining or reducing protection.

Next, consider the exporting producers. Whenever the government of TN1 succeeds in encouraging TN2 to reduce protection, it receives political support from some of its own exporters (represented by a payoff of '+E') but whenever it fails and TN2 maintains (or increases) protection, then the government of TN1 receives political opposition from exporters (or at least fails to gain any support from them) (represented by a payoff of '-E').

## Figure 1: The simplified trading nations' governments' dilemma

| | | Trading Nation | Government no 2 |
|---|---|---|---|
| | | Reduce protection | Maintain protection |
| Trading Nation | Reduce protection | quadrant 1 <br> For 1 (-ICP +E) <br> For 2: (-ICP +E) | quadrant 3 <br> For 1 (-ICP -E) <br> For 2 (+ICP + E) |
| Government no 1 | Maintain protection | quadrant 2 <br> For 1 (+ICP +E) <br> For 2: (-ICP -E) | quadrant 4 <br> For 1 (+ICP -E) <br> For 2 (+ICP -E) |

When the two nations' governments have negotiated a possible trade agreement, then their decision to bring it into force is a decision to move from quadrant 4 to quadrant 1. This means that they are prepared to reduce the import restrictions knowing that they will arouse some political opposition from ICPs but also knowing that there are some groups of exporters which will provide political support to them for entering into the trade agreement.

Whether they are prepared to move to quadrant 1 depends on their perceptions as to the size of the gains and losses of political support involved and how significant these are relative to other factors affecting their ability to maintain a desirable level of political support. Their preparedness to move to quadrant 1 also depends on the rules contained in the agreement and on their expectations about the other nation's behaviour. Once the agreement is in force, TN1 may be tempted to reverse the reduction in protection in order to gain some political support from ICPs. This would move TN1 to quadrant 2. In a quadrant 2 outcome, exporters in TN2 would lose their market access into TN1 and, hence, lose their reason for providing political support to the government of TN2. For as long as the situation remains in quadrant 2, the government of TN2 is receiving a net level of political support which is lower than the level of political support it would have received by deciding not to enter into the trade agreement and staying in quadrant 4. The same thing would happen to TN1 if TN2 granted protection and moved the outcome to quadrant 3, an outcome which for TN1 is worse than the outcome from either having the agreement complied with or not having the agreement at all. Therefore, in negotiating the content of the trade agreement, both parties have in interest in ensuring that they do not get stuck for a prolonged time in the worst quadrant (which is quadrant 2 for TN2 and is quadrant 3 for TN1).

In the rules of the WTO and the rules of virtually all trade agreements, TN2 can request a ruling on whether TN1 has violated the agreement.[13] If the panel or arbitral body finds that TN1 is in violation then TN2 can withdraw substantially equivalent obligations owed to TN1, meaning that TN2 can grant some import protection that would adversely affect exporters in TN1.[14] Virtually all trade agreements have a mechanism for resolving disagreements about whether the impact of the proposed or actual retaliation is equivalent to the impact of the original violation, by having third-party adjudication.[15] When TN2 announces its intended retaliatory measures, then the government of TN1 has to decide whether it would prefer:

- to comply with the ruling and receive the political payoff in quadrant 1 by removing the violation and foregoing the gain in political support from ICPs that flowed from the violation but avoiding the political loss that would flow from its own Exporters blaming it for their loss of market access to TN2's market.

- not to comply with the ruling and receive the political payoff in quadrant 4 in which the government of TN1 would continue to receive the political support of the ICPs benefitting from the violation but would incur a political loss from its own exporters blaming it for their loss of market access to TN2's market.

Observation of the behaviour of governments in trade agreements indicates that, most of the time, the respondent government chooses to comply with the agreement and to move back to quadrant 1 rather than let the outcome shift to quadrant 4.[16] Sometimes

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[13]   See arts 4 to 7 of 'Understanding on Rules and Procedures Governing the Settlement of Disputes, which is annex 2 to *Agreement Establishing the World Trade Organization* 1867 UNTS (1995) 3; Aust TS [1995] No 8; 33 ILM 1144 ('WTO DSU').

[14]   See WTO DSU art 22.6 and for example, *ASEAN – Australia – NZ FTA* art 17(3).

[15]   See WTO DSU arts 21.4 and 21.6.

[16]   See the study of compliance with GATT rulings between 1948 and 1991 in Robert E Hudec, *Enforcing International Trade Law: the evolution of the modern GATT legal system* (Butterworths, 1993), and the study of compliance under the

however, there is a very prolonged stay in quadrant 4. Sometimes the parties need to renegotiate new commitments and reach a compromise that leaves them somewhere in between quadrants 1 and 4. Sometimes, though rarely, the parties do revert to quadrant 4 and remain there with both the breach and the consequent retaliation remaining indefinitely. However, the operation of the rules does give any injured party an opportunity to ensure that it does not get stuck in the worst case outcome (quadrant 2 for TN2, and quadrant 3 for TN1). This assurance helps the parties decide to enter into the trade agreement in the first place. Therefore, apart from the obvious function of helping members to convince other parties to comply with their agreements, the dispute settlement clause is also important as a mechanism for helping trading nations' governments to bring trade liberalisation agreements into existence and for helping parties to include politically difficult liberalisation in trade agreements.

## Mechanism to pre-quantify permissible retaliation — to prompt political decision-makers to focus earlier on '– E', the cost of retaliation

Dispute settlement mechanisms in trade agreements are criticised for a number of reasons: for not ensuring compliance, for taking too long, and for costing too much. Among these criticisms is the important point that when dispute resolution takes a long time, the system, in effect, leaves TN2 in quadrant 2 for that period of time. Given the complexity of the rules of the agreement, the domestic measures and the questions of consistency between the two, there are limits to how quick and easy an adjudication system can be. Nevertheless, it is suggested that even without adjusting the normal processes of the dispute settlement system, it may be possible to supplement the rules with a mechanism to bring the respondent government to focus earlier on the choice between:

- keeping the additional political support of the group of ICPs (arising from the measure allegedly in breach) but losing the political support of a group of exporters; or

- letting go of the additional political support from ICPs (gained from the measures allegedly in breach) but avoiding the loss of political support from a group of exporters who would be affected by the retaliation.

The problem is that the size of the potential loss of political support from a group of exporters is very uncertain since it depends on the finding, not just of a breach, but of a specific breach, and on the finding of the trade impact of that breach, and the choice by the complainant as to the sectors which will be the subject of retaliatory measures.

Is it possible to narrow the range of those uncertainties to a point where it might reduce the time that a party may be stuck in the worst outcome quadrant? What if, at any stage of the dispute proceedings, the complainant could request an independent arbitrator to make a hypothetical finding on this question:

WTO in: Bruce Wilson, 'Compliance by WTO Members with Adverse WTO Dispute Settlement Rulings: The Record to Date' (2007) 10 *Journal of International Economic Law* 397–403.

> If the respondent's measure is found to be a violation, what is the change in value of trade that is caused by the violation measure and what would be the level of retaliation that the complainant could ultimately be allowed to impose?

The complainant could then announce details about how it would choose the sectors that might be the subject of the retaliation measures or could even identify the particular products (or if applicable the services sectors or intellectual property obligations).

This would help to quantify for the respondent government the loss of political support that it might face if it did lose the case and the complainant did impose the retaliation.

The effect of such a quantification would be stronger in some cases than others, since the impact on the respondent would be affected by the respondent's chance of being found not to be in violation or having only some part of the claims against it established. The final outcome of the case might involve findings of a violation which would lead to a different measurement of the change in trade caused by the violation measure. Nevertheless, it seems likely that there would be cases in which the early quantification of retaliation contained in a reasoned opinion would focus the government of the respondent country on the choice between quadrant 1 and quadrant 4 so as to encourage the respondent to withdraw or modify the challenged measure earlier than it otherwise would.

This pre-quantification of possible retaliation:

- could run parallel to the main proceedings;
- would not affect the duration of the main proceedings;
- need not be binding on the parties; and
- would not affect the rights of the parties under the main dispute resolution mechanism for monitoring compliance and imposing retaliation.

There would be some practical issues to be agreed upon, such as procedures for selecting the arbitrator including tie-breaker provisions. There would need to be agreement on who bears the cost of the arbitrator. Given that the complainant would be the one invoking the mechanism, it would seem fair to place the cost on the complainant.

Of course, there is no reason why a party to a dispute cannot seek its own expert report on the quantitative impact of another party's measures allegedly in violation and then make the report public. However, inserting the procedure into the trade agreement would be more effective than the ad hoc publication of expert studies. The procedure for selection of the arbitrator, the official role and the terms of reference would give to the arbitrator's report considerable weight as an indication of what the eventual outcome of the dispute settlement process could be.

## Mechanism to make economic welfare costs more transparent — to prompt political decision-makers to put more weight on considerations related to national economic welfare

The matrix above took into account only two factors: the influence on government decisions of ICPs and of exporters ('E'). There is an implicit assumption that other factors are trivial. One of the factors assumed to be trivial is the influence upon politicians of considerations of national economic welfare. There are good reasons which indicate that

making this assumption will be consistent with predicting real world outcomes in many situations:

- it may be true that there are very few people allocating votes, donations or political support on the basis of considerations of national economic welfare;
- the political support that does accrue to politicians because of constituents' views about the impact of policies on national economic welfare may accrue only after a significant time delay so politicians may regard any political support as being so far in the future that it should be discounted to a very small present value compared to more immediate political pressures.

However, if we took the view that sometimes politicians are influenced by a desire to have a positive impact on national welfare, then we would need to incorporate this into the matrix. If the impact of trade policy decisions were assessed using the standard economics of protection, then (with limited exceptions):

- decisions to reduce protection would contribute positively to national economic welfare; and
- decisions to maintain or increase protection would contribute negatively to national economic welfare.

Incorporating this factor would modify the matrix as indicated in Figure 2 below. The governments of TN1 or TN2 would:

- gain some political support on the basis of their positive contribution to national economic welfare whenever they choose to reduce protection (represented by a payoff of '+NW'); and
- lose some political support on the basis of their negative contribution to national economic welfare whenever they choose to maintain or increase protection (represented by a payoff of '-NW').

Under this revised matrix, the bigger the quantitative evaluation of the impact on governments of national economic welfare, the more likely it is that a rational government maximising political support would choose quadrant 1 instead of quadrant 4.

The respondent government faced with a complaint may ultimately be faced with a choice between:

- keeping the additional political support of the group of ICPs (arising from the measure allegedly in breach) but losing the political support of a group of exporters *and* losing political support from those valuing national economic welfare (quadrant 4); or
- letting go of the additional political support of the ICPs gained from the measure allegedly in breach but avoiding the loss of political support from a group of Exporters who would be affected by the retaliation *and* avoiding the loss of political support from those valuing national economic welfare (quadrant 1).

**Figure 2: Simplified trading nations governments dilemma incorporating national welfare**

|  |  | Trading Nation | Government no 2 |
|  |  | Maintain protection | Reduce protection |
| --- | --- | --- | --- |
| Trading Nation | Maintain protection | quadrant 1 For 1 (-ICP + E + NW) For 2: (-ICP + E + NW) | quadrant 3 For 1 (-ICP – E + NW) For 2 (+ICP + E + NW) |
| Government no 1 | Reduce protection | quadrant 2 For 1 (+ICP + E - NW) For 2: (-ICP – E - NW) | quadrant 4 For 1 (+ICP -E - NW) For 2 (+ICP -E - NW) |

How could we modify the dispute system to increase the weight that the respondent government places on the gain or loss of national economic welfare? What if the complainant could request an independent arbitrator to make an estimation of the economic cost to the respondent of maintaining the protectionist measure subject to the complaint and to publish that estimation in a freely available form?

In the presence of the additional report, citizens in the respondent country would be more likely to be aware of the costs and benefits of the respondent's measure and its likely net cost. The citizens in the respondent country might be more likely to make decisions about whether to support or oppose the government upon the basis of the impact of the policy on national economic welfare. That might make politicians put greater weight on this factor in deciding whether to maintain the measure which is the subject of the litigation.

Like the mechanism for pre-estimation of retaliation, this mechanism for quantification of impact on the respondent country's national economic welfare:

- could run parallel to the main proceedings;
- would not affect the duration of the main proceedings;
- need not be binding on the parties; and
- would not affect the rights of the parties under the main dispute resolution mechanism for monitoring compliance and imposing retaliation.

The same practical issues mentioned above in the context of the mechanism for pre-estimation of retaliation would also apply to this mechanism for quantification of impact on the respondent's country's national economic welfare.

There are advantages of institutionalising this mechanism through the trade agreement. Of course, there is no reason why a party to a trade agreement cannot commission an expert economist report on the national economic welfare cost of another member's policy measure. However, the insertion of the mechanism for obtaining an expert economic assessment into the trade agreement would be more effective than the ad hoc publication of economic studies of particular measures. Since the objective is to increase the political impact upon political decision-makers in the respondent country, then the critical thing is that economic report is publicly available in the respondent country to influence public opinion in that country. The insertion of the mechanism into the trade agreement means:

1. that the respondent government's own endorsement of the process of appointing the expert and obtaining the report agreement enhances the authority of the conclusions of the report; and

2. that the respondent government consents in advance to the report being publicly available and uncensored in the respondent country.

## Transparency mechanism

A further point is that something like the second mechanism could be adopted without it being confined to situations in which there has been a complaint about a particular measure in formal dispute settlement. Parties could incorporate into a trade agreement a mechanism under which any party can instigate the preparation of an expert economic report into the economic welfare cost of another member's measure. For example, the Closer Economic Relations treaty between Australia and New Zealand[17] could be amended to add a mechanism under which Australia could initiate the appointment of an expert economist or group of expert economists to report on the national economic welfare cost to New Zealand of a New Zealand measure protecting a particular product or service sector. In the context of a broader Asia Pacific Community agreement, it could be possible for any member to trigger the production of an economic report on another member's measure. The availability of the report might influence public debate about the measure within the country imposing it and in due course might influence a process of reform.

This suggestion is consistent with the views of the Tasman Transparency Group[18] which argues that it is domestic reform processes and transparent debate about reform options that are the key to economic gains. The Group argues that trade agreements are useful drivers of economic reform only when domestic processes cannot work effectively and that the focus should be on generating sufficient transparency in public debate so that

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17  *Australia New Zealand Closer Economic Relations Trade Agreement* done Canberra, 28 March 1983, (on its terms deemed to be in force from 1 January 1983) Australian Treaty Series [1983] No 2; also available at <http://www.dfat.gov.au/fta/anzcerta/index.html>. The same website makes available a number of protocols and other instruments that have amended the treaty.

18  The Tasman Transparency Group is a group comprised of a number of Australian and New Zealand NGOs. Its website describes the group as 'a private, not-for-profit group dedicated to strengthening the World Trade Organisation (WTO) multilateral trading system through better transparency of trade policy at home' (< http://tasmantransparencygroup.com/about>) and indicates that the members are the Australian Services Roundtable, Evian Group, Federated Farmers of New Zealand, International Chamber of Commerce (Australia), New Zealand Business Roundtable, New Zealand Services Group and Wellington Regional Chamber of Commerce (New Zealand).

domestic reform processes can work effectively.[19] I will not debate here the respective roles of achieving reform unilaterally and achieving reform in the context of trade agreements. However, there are no disadvantages from incorporating into trade agreements mechanisms that might make unilateral reforms more likely.

Such process for making economic impacts transparent has some parallels with the way in which economic studies of OECD members policies are produced by the OECD Secretariat, though in that context, the OECD has to take a decision to write a report on a particular issue.[20] Anything contentious can be kept off the work programme. There is also a limited parallel with the WTO's Trade Policy Review Mechanism under which members can ensure that reports set out a Members restrictive laws and policies.[21] However, the Trade Policy Review Mechanism does not have a mandate to investigate the economic welfare costs of members' policies.

There is of course nothing to prevent any country from establishing its own domestic processes for analysing existing policies and publishing reports on their economic welfare costs. There are advantages of incorporating such a process into a trade agreement:

- each party agrees in advance to the process so that no consensus is necessary on initiating the study or releasing or publishing the report;

- no party can prevent initiation of a study, interrupt progress of a study or prevent release of an unfavourable report; and

- each party agrees in advance to the mechanism for publishing the reports so the problem of parties declining to publish a report would not arise.

As mentioned above in relation in discussing the insertion of such a mechanism into the dispute settlement process, the critical thing is that the economic report is publicly available in the country in which the measure is in force so as to influence public opinion in that country. The country whose measure is studied in the report consents in advance to the report being publicly available and uncensored within its own borders. That the country itself has endorsed the process of appointing the expert and obtaining the report enhances the authority of the conclusions in the report.

## Conclusion

No doubt there are some situations where none of the mechanisms above will bring to bear sufficient pressure for a particular government to remove a measure which is diminishing the economic welfare of its own citizens. However, surely, there could be a range of situations in which the abovementioned mechanisms might be sufficient to tip the scale so that a government decision to remove a protectionist measure can be made earlier than it otherwise would be.

The key is to consider the political pressures that weigh on governments that seek to maximise their political support and minimise opposition:

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[19]    Tasman Transparency Group, *An Assessment of the Government's Review of Trade Policy* (17 November 2011) <http://tasmantransparencygroup.com/ttg-publications>.

[20]    On the OECD website <www.oecd.org> , see the Country Reviews and the various working paper series.

[21]    The WTO Trade Policy Review Mechanism operates under *Trade Policy Review Mechanism,* which is Annex 3 to the WTO DSU. Documents relating to the operation of the Trade Policy Review Mechanism are available from the WTO website at <http://www.wto.org/english/tratop_e/tpr_e/tpr_e.htm>.

- the first mechanism may help resolve disputes in a trade liberalising way by encouraging respondent governments to focus earlier on the potential loss of political support from exporters that they will need to weigh against any political support from import competing producers;

- the second mechanism may help resolve disputes in a trade liberalising way by increasing the political weight attributed by the respondent government to the overall economic effects of the controversial measure and, therefore, reduce the extent to which liberalising the measure subject to the litigation may cause the government to lose political support;

- the third mechanism may avoid disputes about existing commitments completely or may facilitate further liberalisation commitments, either unilaterally or through exchanges under the trade agreement, by increasing the political weight attributed by a government to the overall economic effects of its measures and, therefore, reduce the extent to which liberalising a protectionist measure may cause the government to lose political support.

Ultimately, the success of a trade agreement depends on how it influences the internal decision making of each government. These mechanisms, aimed squarely at internal political decisions, may help.