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Dispute Settlement at the WTO and the Dole Commission: USTR Resources and Success

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Dispute Settlement at the WTO and the Dole Commission: USTR Resources and Success*

Gary R. Saxonhouse

I. The Passage of the Uruguay Round Agreements and the Dole Commission

After more than seven years of negotiation the Uruguay Round concluded with an historic agreement on December 15, 1993. Exactly four months later documents implementing this agreement were signed by representatives of the 117 Uruguay Round participants at a ministerial meeting at Marrakesh, Morocco. Even so, this signed agreement required ratification at home by the relevant legislative bodies of the agreement signatories.

Ratification of the Uruguay Round Agreements was viewed as virtually certain in all countries except the United States. While the new World Trade Organization was set to begin operations on January 1, 1995, as late as October, 1994, Senate Finance Committee Chair, Daniel Patrick Moynihan, could claim only 26 committed yes votes.[1] Many senators, including the Republican Minority Leader, Robert Dole, were said to be concerned about the WTO's newly enhanced Dispute Settlement Mechanism (DSM). The critical element of the revised DSM is the absence of the right of any country acting alone to block the formation of a Dispute Settlement panel or the adoption of panel findings. As the DSM had operated under the GATT, veto power was held, effectively, even by the accused party. In fact, this power was used in significant instances by losing parties to block adverse panel findings against them.[2] Under the WTO, however, panels get set up and proceed with their investigations and panel findings are adopted unless the WTO Council decides otherwise by consensus.[3] This is the polar opposite of the older *modus operandi*, and it was the loss of national sovereignty implicit in this new arrangement to which many senators objected.

That there should have been Congressional objections to the new DSM is ironic. In the 1988 Omnibus Trade Act that gave the Reagan Administration fast-track authority for the Uruguay Round, Congress mandated U.S. trade officials "to negotiate for more effective and expeditious dispute settlement mechanism and procedures" that would "enable better enforcement of U.S. rights."[4] Actually, the inclusion of such language in the Trade Act of 1988 should be no surprise. U.S. interest in a revised DSM is of very long standing. Already during the Tokyo Round, the United States pressed both for an end to the single country veto and for expedited procedures.[5]

In Fall 1994, populist fears about the loss of sovereignty to the WTO were such that Senator Dole reported that his office was receiving 2,000 phone calls a day from opponents of the Uruguay Round Agreement.[6] Notwithstanding, on November 23, 1994, he agreed to support the enabling legislation and to encourage all Republican senators to support it in exchange for White House support for a Dole-conceived WTO "escape hatch." The escape hatch would be embodied in legislation to be introduced the following year that would establish a WTO Dispute Settlement Review Commission.[7] Dole intended that

- The Commission would consist of five Federal appellate judges appointed by the President in consultation with the leadership of both Houses and Chairmen and Ranking Members of the Senate Finance Committee and the House Ways and Means Committee.
- It would review all final WTO dispute settlement reports adverse to the United States to determine whether the panel exceeded its authority or acted outside the scope of the agreement. Following issuance of any affirmative determination by the Commission any member of either House would be able to introduce a joint resolution calling on the President to negotiate new dispute settlement rules that would address and correct the problem.
- If there were three affirmative determinations in any five-year period, any member of either House could introduce a joint resolution to disapprove U.S. participation in the WTO – and if the resolution were enacted by Congress and signed by the President, the United States would commence withdrawal from the WTO.

II. The History of the Dole Commission

Despite the wide-spread publicity given the Clinton-Dole WTO agreement and despite the Senate having passed the WTO implementing legislation on December 1, 1994, in the six years that have ensued, the so-called "Dole Commission" has not been set up. As early as January 4, 1995, on the very first day of the new Congress, with Republicans in control of both Houses for the first time in forty years, Senator Dole introduced legislation creating the Commission.[8] The bill was identical with the terms of the late November agreement with the exception of one significant provision. Section 7 of the proposed legislation would have guaranteed participation by private parties in the proceedings before the dispute-settlement panels.

Guaranteeing participation of private parties in dispute-settlement-panel proceedings, while it did not deter many of the Senate's leading figures on trade policy from co-sponsoring the bill, including Senators Moynihan, Baucus, D'Amato, Grassley, Murkowski, Lott, Pressler, Santorum and Simon, it was as controversial in 1995 as it is today.[9] The hearings held by the Senate Finance Committee on the Dole legislation found wide disagreement on this issue between two former Deputy United State Trade Representatives. Alan Wolff argued such private participation was necessary because

> "… even the best lawyer cannot do a first-rate job if he or she does not have the time or resources to devote to a case. The reality is that these very capable people at USTR are already overworked and if the WTO system spawns even more international trade litigation before panels, they will be stretched even thinner …. The result is that the United States will lose cases it should win."[10]

Alan Holmer countered that

> "… in dispute settlement, the U.S. Government needs to be able to act efficiently and speak with one voice. This is not a mere theoretical issue. Some WTO cases will involve issues that have a direct economic impact on dozens of U.S. industries, trade associations, or companies. Will each of them have the right to represent the interests of the United States before the panel? What if, while supporting the overall U.S. Government position (USG), their view of the law or the facts is different from that of the USG? Moreover, inevitably there will be differences in strategic approaches to cases, particularly where the best U.S. legal argument in one case may have a detrimental interest in another case. The role of the Administration in dispute settlement proceedings is not to represent one company or interest group. Rather, its role is to represent the national interest."[11]

The Clinton Administration took Ambassador Holmer's side in this dispute and refused to support the legislation as Senator Dole had submitted it.[12] It was only in the following November that the original Dole legislation was re-introduced, this time with offending Section 7 removed.[13] In his eagerness to have this legislation passed prior to the beginning of the 1996 presidential primaries in which he would be a candidate and in which he would face protectionist opposition, Senator Dole agreed to allow Robert Byrd, a very senior Democratic member of the Senate, to submit an amendment that would set up two new WTO review commissions in addition to the one comprised of members of the Federal judiciary. One commission would consist of senators whose mandate would be to review all aspects of the WTO's workings and to recommend legislation wherever appropriate. This commission of senators would be advised by a second commission comprised of trade lawyers, former government officials, scholars and labor leaders.[14]

The Byrd Amendment doomed the Dole legislation. Key members of the Senate Finance Committee, led by its Chair, William Roth, changed their views and now opposed the Dole proposal fearing first, that the new commission of senators would be a threat to the Finance Committee's jurisdiction over trade issues, and, second, that the private-sector commission would be prone to domination by special interests.[15] This latter concern was also shared by the Clinton Administration. One last attempt was made to pass this legislation during the last few days before Senator Dole's resignation from the Senate. A compromise was reached to drop the new commission of senators and to refashion the private sector commission so that 1) half the nominees would be appointed by the White House and 2) the new commission would report directly to the Senate Finance Committee and the House Ways & Means Committee.[16]

Notwithstanding this compromise, opposition from protectionist textile interests, who were hostile to anything that might legitimize the WTO in any way, was sufficient to prevent the legislation from coming to a vote at that time.[17] In fact, while periodically re-introduced, the legislation was not voted on in that Congress at all, nor in any subsequent Congress.[18]

III. Congressional Review of WTO Treatment of U.S. Interests

While the WTO Dispute Settlement Review Act has never been passed by Congress and does not have any immediate prospect of passage, the sovereignty issues raised at the time that it was under active consideration remain politically salient. There may be no federal judiciary review of WTO decisions adverse to U.S. interests, but the Uruguay Round Agreements Act does require a five year review for the Congress by the USTR of U.S. participation in the WTO.[19] This report appeared in late February 2000. At that time, by USTR's count, 32 WTO cases in which the United States had been involved in a significant way had been completed. Of these cases, the United States prevailed in 24, either as a result of a Dispute Settlement panel finding or because of a settlement highly favorable to U.S. interests prior to a formal panel report being issued. The USTR, emphasizing both the large number of cases in which the United States prevailed, particularly as a plaintiff, and the overall high win-rate, concluded that the DSM is operating in a way highly beneficial to U.S. interests.[20] By implication, by these indices, the USTR suggests that the fears that spawned the original interest in the Dole Commission were unwarranted. Indeed, the U.S. rate of success with the DSM since the WTO commenced is slightly better than it was during the 1980s when the DSM first came to be used intensively as means of resolving trade disputes.[21]

Whatever the views of the USTR, and irregardless of the non-existence of the Dole Commission, the same section of the Uruguay Round Agreements Act that provides for a five-year review of U.S. participation in the WTO, also provides that within 90 days of Congress receiving this report, just as with the Dole Commission bill, any member may introduce a joint resolution of both Houses calling for U.S. withdrawal from the WTO.[22] Such a resolution must be placed on the calendar for action no later than 45 days after being introduced. If passed by the Congress and signed by the President, it would trigger U.S. withdrawal subject to the six months advance notification required by the WTO's Article XV. In response to the USTR's five-year report and citing the eight decisions that have gone against the United States, a joint resolution calling for U.S. withdrawal from the WTO was introduced within a matter of days of the report's release.[23] Because of the expedited schedule required by the Uruguay Round Agreements Act, hearings were held on the resolution within a month of its filing. A little more than two months after hearings were held, the resolution was voted down on the House floor by a margin of 363 to 56, a margin of victory much wider than the 288-146 vote on whether to join the WTO in November, 1994.[24] Notwithstanding the December 1999 turmoil at the failed WTO Summit in Seattle, Congressional support for the WTO was stronger than it had been five years earlier. Significantly, during the floor debate on the joint resolution, the USTR's high rate of success at the WTO was raised repeatedly by opponents of the resolution.[25]

IV. Resources and U.S. Performance at the WTO

It is possible that the absence of a review commission composed of respected jurists may actually increase the political sensitivity of each adverse WTO outcome for the United States and lead to undue focus on quantitative indicators of success at the DSM. In this connection, the resources that the USTR has at its disposal to pursue litigation at the WTO does become an issue. It may be as Alan Wolff forecast in his testimony before the Senate Finance Committee that the USTR is losing cases it should win at the WTO because its lawyers are "overworked."[26] While it may seem obvious that more resources should strengthen the position of the United States in international economic disputes, senior U.S. trade officials have often taken the opposite view. Ambassador Mickey Kantor, when he was USTR, argued that his agency's great virtue was its small size, and that this small size was the key to its success.[27] Whether because of Ambassador Kantor's views, or because of the constraints imposed by the large Federal budget deficits that Congress faced during much of the 1990s, despite the creation of the WTO, NAFTA, and APEC, to mention just a few new responsibilities, until the very last months of the Clinton Administration, USTR was no

larger than it was in 1993 when the Clinton Administration took office.[28] USTR had 203 full-time equivalent authorized positions in both fiscal year 1993 and in fiscal year 2000. In recent years, USTR Charlene Barshefsky regularly asked for, but was denied large increases in her staff.[29] Finally, only a few months before her departure from public life, Congress did approve Ambassador Barshefsky's request for 25 new full-time, career positions within USTR.[30]

V. Resources, Success and Success Rates

Now that the USTR's size is changing, what can be expected to happen to U.S. performance at the WTO? To analyze this issue, and leaving aside until Section VII of this paper all questions of strategic behavior including reactions of trading partners,[31] assume that the USTR has the utility function:[32]

$$U\Big(a(X,\delta),b(X,\delta)\Big) \quad ,$$

where

a(X, δ) is the proportion of cases won at the WTO

b(X, δ) is the number of cases won at the WTO

X is the number of cases brought before the WTO

δ is the resources the USTR will use above the minimum K required per case

The utility function posited here reflects USTR interest, as evident in its recent report on U.S. performance at the WTO, and in the Congressional debate on continued U.S. participation in the WTO, in its success-rate as well as in its total number of wins. Note further that f(y) is the 'base' probability that case number 'y' is won by the US, with f '(y)<0, that is, potential WTO cases can be ordered according to their probability of success on the assumption that only K resources are used per case. The probability of success can be affected by δ g(δ) is the increased likelihood that any particular case is won due to 'extra' resources (independent of which case):

$g'(\delta)>0,\ g''(\delta)<0$ with $\lim_{\delta\to\infty} g(\delta) < 1-\lim_{X\to 0} f(X)$

(Impossible to guarantee any win).

The problem for the USTR is:

$$Max_{X,\delta} U\Big(\underset{+}{a(X,\delta)},\underset{+}{b(X,\delta)}\Big) subject\ to\ (K+\delta)X \le m,$$

where m is the total resources available to the USTR.

VI. The Comparative Statics of the USTR's Problem

The total number of U.S. wins at the WTO is clearly increasing in USTR resources[33]

$$\frac{db}{dm} = \frac{\overset{+}{db}}{dX}\frac{\overset{+}{dX}}{dm} + \frac{\overset{+}{db}}{d\delta}\frac{\overset{+}{d\delta}}{dm} \quad .$$

This presumably is the relationship that Ambassador Wolff had in mind. Once again, as in the USTR report on the WTO, Congressional debate on continued U.S. participation in the WTO, and Ambassador Barshefsky's own Congressional testimony makes clear, however, there is also interest in a, the rate of success. Here the results are ambiguous:

$$\frac{da}{dm} = \frac{\overset{-}{da}}{dX}\frac{\overset{+}{dX}}{dm} + \frac{\overset{+}{da}}{d\delta}\frac{\overset{+}{d\delta}}{dm}$$, which can be positive or negative.

This can be restated as the effect that marginal resources have on the marginal success rate depends on the effect of marginal resources on the impact of each of the USTR's two possible uses of these resources

Resources per U.S. case at the WTO

Number of U.S. cases at the WTO

Using the results from Appendices 1 and 2, decreasing (increasing) g"(δ^*), that is a lessening (increasing) of the effect of above-minimum resources K per case, decreases (increases) the denominator of $\frac{d\delta}{dm}$, and therefore $\frac{d\delta}{dm}$ is increased (decreased) while $\frac{dX}{dm}$ is decreased (increased), thereby increasing (decreasing) $\frac{da}{dm}$. In other words, the less (more) rapidly the effectiveness of marginal resources used per case (g"(δ^*)) is falling (from the equilibrium amount of resources per case, $K+\delta^*$), the greater (smaller) the share of any increase in marginal resources will be used to increase resources per case. Because resources per case is what is assumed to increase WTO success rates, less (more) rapid marginal decline in the effect of resources used per case correspond with greater resources increasing (lowering) success rates.

Decreasing (increasing) f"(X^*), that is, increasing (decreasing) the rate at which the 'base' success rate is falling at X^*, decreases (increases) $\frac{d^2a}{dX^2}$ (guaranteeing the Hessian given in Appendix 1 is negative semi-definite) and decreases (increases) the denominator of $\frac{d\delta}{dm}$. Once again $\frac{d\delta}{dm}$ is increased (decreased), $\frac{dX}{dm}$ is decreased (increased) and $\frac{da}{dm}$ is increased. This means the more rapidly (slowly) the probability of success with a new case at the WTO (f '(X)) is falling (from the marginal U.S. WTO case, X^*, in equilibrium), the lower (higher) the share of any marginal increases in resources that will go towards bringing additional U.S. cases at the WTO. Instead, more of these marginal increases in resources will go towards increasing resources per case (starting new cases) and therefore to higher (lower) success rates.

The impact that USTR preferences have on the allocation of its resources can be seen with the use of the first-order conditions:

$(K+\delta)X = m$, and therefore $X = \frac{m}{K+\delta}$

Substituting this into $U_a g'(\delta) + XU_b g'(\delta) = X\lambda$ gives:

$((K+\delta)U_a + mU_b)g'(\delta) = m\lambda$.

Suppose there is an increase (decrease) in importance to the USTR of the success rate. Because utility is homogeneous in degree zero the comparative statics for such a change are the same sign as if U_a is increased (decreased) and U_b decreased (increased) in the ratio necessary to leave λ unchanged. Since g"(δ)<0 and the above condition must hold for all utility functions, δ must increase (decrease). Given $X = \frac{m}{K+\delta}$, this means that X must decrease (increase). Because the USTR success rate at the WTO is increasing in δ and decreasing in X, the success rate increases (decreases).

The results in this section are also presented in figure 1.[34] m^o is the original resource constraint, m' is the new resource constraint, and w_{USTR} is the USTR iso-welfare curve through the original equilibrium. a^o is the locus of points with a^o proportion of wins, and b^o is the locus of points with b^o wins. Points to the left (right) and below (above) a^o represent a higher (lower) proportion of wins than a^o. Points to the right (left) and above (below) b^o represent a higher (lower) number of wins. With the new resource constraint m', if the new equilibrium is to the left (right) and above (below) a^o, this will be the outcome most consistent with Ambassador Wolff's (Kantor's) 1995 Congressional testimony. Where this new equilibrium will be depends critically (though not exclusively) on the shape of a^o, which, in turn, depends on g"(δ) and f"(y).

It does appear that the view implicit in Congressional appropriations for USTR until last year, and explicit in Ambassador Kantor's remarks, under some conditions, can be correct. Less resources for the USTR can mean a higher success rate. In thinking about this issue, it is important to keep in mind that it is the USTR itself that ultimately controls the number of U.S. cases that go before the WTO. The more cases the USTR allows to go before a dispute settlement panel, the more cases it will win. But assuming the cases with the highest chance of success at the WTO are taken there first, the more cases it will also lose.[35] To the extent that both the number of successes and the rate of success are politically salient, there is a trade-off here. The trade-off will depend on how quickly the probability of success in an additional case taken to the WTO declines by comparison with how much investing additional resources on cases already at the WTO raises the probability of success with them. Depending on how much the USTR values the number of successes versus success rates will determine together with these two factors how its resources are allocated. If additional cases bring with them very low probability of success by comparison with investing additional resources in existing cases, new resources for the USTR will raise both the success rate and the number of wins. Paradoxically, if there remain promising cases that are not being brought to the WTO because of a lack of resources, new resources for the USTR can lower its rate of success at the WTO even while it increases the number of wins.

VII. USTR Behavior and MITI Reactions

The preceding analysis assumes that the USTR values all cases equally. It also does not discuss reactions that U.S. trading partners might make in response to an increase in USTR resources. Suppose instead these possibilities are now allowed for in a simple example.[36] Assume that USTR and MITI are contesting two cases before the WTO Dispute Settlement Mechanism. The issue is how USTR and MITI will split their resources. Suppose USTR's utility function is

$U = \alpha a + \beta b^*$,

a special case of the utility function used in the preceding sections. While a is still the win rate with wins unweighted, b* now weights wins according to their importance to USTR. When b* is calculated, the first case is weighted more significantly than the second. USTR gives Case 1 a weighting of 1, while Case 2 is given a weighting of w.

$1 > w > 0$

is the amount USTR weights a win in Case 2. As before, the more resources USTR uses per case, the greater the chance of winning that case. Once again, K resources are the 'base' resources used per case (here set exogenously to 0). τ are the additional resources the USTR will use for the first case. n represents total USTR resources (set exogenously to 1).

MITI is assumed to have a utility function of the same form as USTR.

$U' = \rho c + \theta d^*$

c is MITI's win rate and d* is its weighted number of wins. For MITI, Case 1 also has a weight of 1, while Case 2 is weighted h with

$1 > h > 0$

As is likely, both USTR and MITI will find Case 1 more important. For MITI, as for USTR, the more resources, the more likely a case will be won before the USTR. K are the base resources that MITI uses per case (here also set exogenously to zero). γ are the extra MITI's resources used for Case 1. m are MITI's total resources (also set exogenously to 1)

As before, there is an exogenous 'base' probability that USTR will win each of the two cases. This probability is denoted f(1) and f(2) for Cases 1 and 2, respectively. Resources affect USTR chances according to the following relationship, also a special case of the function used in the preceding sections.

$$g(case) = -e^{-v\tau} + e^{-v\gamma} - \mu\tau\gamma$$

where

$v > 0$ is a measure of the effect of extra resources (set exogenously to 2)

$\mu > 0$ is a measure of the degree of strategic interaction (set exogenously to 1).

For the purposes of illustration here, it is assumed that USTR acts as a strategic substitute. The more resources that MITI puts on one case, the less valuable USTR's resources on that case become, and the less resources USTR wants to put on that case. The opposite is true for MITI. It

acts as a strategic complement.[37] The more resources that USTR puts on a case, the more valuable MITI's resources on that case become and the more resources that MITI wants to put on that case.

From the above, USTR maximizes

$$(.5\alpha+\beta)(f(1)-e^{-v\tau}+e^{-v\gamma}-\mu\tau\gamma+(.5\alpha+x\beta)[f(2)-e^{-v(1-\tau)}$$
$$+e^{-v(1-\gamma)}-\mu(1-\tau)(1-\gamma)],$$

with the first-order condition:

$$(1-w)(\beta(ve^{-v\delta}-\mu\gamma)-\mu(\frac{1}{2}\alpha+\beta)(n-2k)=0.$$

The second-order condition is satisfied for the assumed parameters:

$$-(1-x)\beta(v^2e^{-v\tau})<0$$

In the same way, MITI maximizes

$$(.5\rho+\theta)(1-f(1)+e^{-v\tau}-e^{-v\gamma}-\mu\tau\gamma)+$$
$$(.5\rho+w\theta)[1-f(2)+e^{-v(1-\tau)}-e^{-v(1-\gamma)}+\mu(1-\tau)(1-\gamma)] \quad ,$$

with the first-order condition:

$$(1-h)\theta(ve^{-v\gamma}+\mu\tau)-\mu(\frac{1}{2}\rho+h\theta)(m-2k)=0.$$

Once again, the second-order condition is satisfied for the assumed parameters:

$$-(1-h)\theta(v^2e^{-v\gamma})<0.$$

Table 1 summarizes the equilibria for the setup just presented. The base case assumes $\alpha = \beta = \rho = \theta = 1$ and h = w = 0.5. .05 values for h and w mean that Case 1 is much more important to both USTR and MITI than is Case 2.

The baseline in Table 1 indicates how USTR and MITI divide the extra increment of resources that each gets. Despite USTR and MITI both valuing the first case twenty times more than the second, USTR, unlike MITI, will devote a disproportionate amount of its resources to Case 2. This result follows from the assumption that the USTR acts as a strategic substitute and MITI as a strategic complement.

Δ1 explores what happens when USTR puts less of a weight on Case 2 than does MITI. Unsurprisingly relative to the baseline, USTR becomes more likely to win Case 1 and less likely to win Case 2. More surprisingly in Δ 2, when USTR puts more weight on Case 2 than does MITI, giving USTR more resources, when MITI will get matching resources, will make it less likely that USTR will win Case 2 while it is more likely to win Case 1 relative to the outcome in the baseline. With Δ 3 the more important USTR and MITI find Case 2 relative to Case 1, the more likely relative to the baseline, USTR is to win Case 1, but the less likely it is to win Case 2.

Δ 4 and Δ5 explore how the allocation of incremental resources for USTR and MITI changes when, unlike the baseline and the preceding simulation, USTR and MITI place different weights on the success rates and the winning of cases weighted by their importance. Surprisingly for Δ4 the more importance that USTR places on the success rate relative to MITI, the less likely it is to win Case 2, while becoming no more likely to win Case 1. For Δ5, and in contrast with the results for USTR, if MITI places relatively more importance on success rates than does USTR, MITI becomes more likely to win Case 2, but somewhat less likely to win Case 1.

From the perspective of the issues discussed in the preceding section, in each instance (though least for the base case), extra resources actually lower the success rate for USTR. Even for Δ4, the more important the success rate for USTR, with extra resources for both USTR and MITI, the lower the success rate is likely to be for them. Unlike the preceding section, this finding does not follow from extra resources encouraging USTR to take on additional cases with a low probability of success. Rather as a strategic substitute, it is poorly suited to improve its welfare in an environment where both sides have more resources. For example, were USTR to attempt to bring only the first case and not the second to the WTO, both USTR and MITI would put all their resources on this case and g(1) = - 1. For the setup here, it makes sense for USTR to try both cases. The results for MITI, which are the exact opposite of those for USTR, show that for a

strategic complement, more resources can lead to both a higher success rate and a greater likelihood of winning the most important cases notwithstanding USTR getting the same increment in new resources.

VIII. Consistency and the Use of the WTO Dispute Settlement Mechanism

Since the enhancement of the DSM with the creation of the WTO, there has been an upsurge in its use. During the 1980s, 127 complaints were taken to the DSM.[38] During its first five years of operation alone, the WTO's DSM has received 185 complaints.[39] U.S. use of the DSM reflects these general trends. Between 1980 and the beginning of 1990, the United States brought 39 complaints to the DSM.[40] Between 1995 and the beginning of 2001, the United States has brought 60 complaints.[41] This implies an increase in the annual incidence of complaining to the WTO by the United States of over 200%.

The greatly increased U.S. use of the DSM cannot be the result of increased resources. In the late 1990s, the USTR budget has been no greater than it was in the 1980s. Nor does it seem likely, given all the emphasis on USTR's success rate a, that in recent years more emphasis is being put on total successes b.[42] Rather, it has been suggested that the WTO's DSM might be used more often now because the Uruguay Round Agreements texts, being new, are inherently ambiguous.[43] A more predictable environment allows parties to a conflict to save themselves the trouble of using up scarce resources by resolving their dispute outside the WTO, anticipating what would happen if they went through the DSM process. While this is a plausible view of the relationship between uncertainty and the use of the DSM, in theory, the inverse relationship is also plausible. Consider the following.

Suppose USTR has a case that it believes has merit φ. It is assumed USTR's information about the merit of the case that it can take to the WTO is private information.[44] If USTR takes the case to the DSM, it will get:

$(1 - \rho)\,\varphi + \rho\,\varepsilon$,

where ρ is a noise parameter and ε is a population mean of a random drawing of possible remedies for USTR's complaints. Both USTR and MITI know ρ and ε. If ρ = 1, the DSM result is pure noise, if ρ = 0, there will be an outcome with merit φ. Suppose that MITI offers p settlement to USTR. MITI gets −p, if USTR accepts but $-[r + (1-\rho)\varphi + (\rho\varepsilon)]$ if USTR rejects where n is the resource cost of pursuing the case at WTO.

USTR will accept p if $p \geq (1-\rho)\varphi + \rho\varepsilon$ or $(p - \rho\varepsilon)/(1-\rho) \geq \varphi$. MITI's expected payoff (not knowing φ) is:

$$pF[\frac{p-\rho\varepsilon}{1-\rho}] + \int_{\frac{p-\rho\varepsilon}{1-\rho}}^{\infty} \{(1-\rho)\varphi + \rho\varepsilon + r\}dF(\varphi),$$

where F is prior on φ.

Solving for offer p in equilibrium, the first-order condition is:

$$F[\frac{p-\rho\varepsilon}{1-\rho}] + \frac{p}{1-\rho}F'[\frac{p-\rho\varepsilon}{1-\rho}] - \frac{p+r}{1-\rho}F'[\frac{p-\rho\varepsilon}{1-\rho}] = 0 \ ,$$

or $(1-\rho)\frac{F}{F'} = r$,

when F is uniform $p = \varepsilon\rho + n$ (ε = ½).

In this case USTR will accept if:

$$r \geq (1-\rho)\varphi \ \text{ or } \ \frac{r}{1-\rho} \geq \varphi \ .$$

Thus, with a uniform distribution, more noise ρ:

1) increases offer p;

2) increases the probability that the conflict will not be taken to the WTO.

This suggests that it may not be a new, untested and unpredictable WTO that is generating more cases. In fact, the set-up allows the inference that perhaps the new WTO's DSM is more rather than less predictable than the GATT's forty-year old DSM.[45] The speed and automaticity (panel

findings accepted except if opposed by a consensus of WTO Council Members) of the new DSM may make the whole WTO more predictable than before, notwithstanding the inevitable vagueness of a new trade treaty.[46] And, because it is more predictable than before, it is being used.[47]

IX. Conclusions

At the time the Uruguay Round Agreements were passed by Congress, particular concern was expressed about their implications for U.S. national sovereignty. Concern was sufficiently great that the Clinton Administration committed its support to the creation of a commission that would review each adverse decision against the United States by the WTO. The commission was designed such that the outcome of its review process might trigger a serious Congressional consideration of U.S. withdrawal from the WTO.

While the so-called Dole Commission was never created, the Congressional controversy surrounding the ratification of the Uruguay Round Agreement has led to particular concern with USTR performance at the WTO. Curiously, enhanced Congressional concern has not gone hand in hand with more resources for USTR. Over the 1990s, USTR has rarely asked for, and, until 2000 has not received additional resources for its work.

The analysis here shows that if the USTR is concerned not only about the number of cases it wins but also about its rate of success, having more resources may have an ambiguous impact on the USTR's rate of success. Depending on how relatively promising are the additional cases that may yet be brought by USTR to the WTO, and how usefully additional resources may be applied to existing cases, it is possible that more resources can lower USTR's success rate. This is true, though for different reasons, when explicit allowance is made for the response by the other party to the dispute to a USTR commitment of additional resources.

More resources cannot explain the increased use that the USTR has made since the WTO was established, because until recently USTR has received no additional resources. Rather, a more predictable DSM may have encouraged more rather than fewer cases to be brought to the WTO in preference to further efforts at extra-WTO bilateral settlements.

Appendix 1

The problem for the USTR is:

$$Max_{X,\delta} U\left(\underset{+}{a(X,\delta)}, \underset{+}{b(X,\delta)} \right) subject\ to\ (K+\delta)X \le m.$$

Note the success rate, $a(X, \delta) = \frac{1}{X}\int_0^X f(y)dy + g(\delta)$ with:

$$\frac{da}{dX} = \frac{1}{X} f(X) - \frac{1}{X^2}\int_0^X f(y)dy < 0$$

$$\frac{d^2a}{dX^2} = \frac{1}{X} f'(X) - \frac{2}{X^2} f(X) + \frac{2}{X^3}\int_0^X f(y)dy \underset{<}{>} 0$$

$$\frac{d^2a}{dXd\delta} = 0$$

$$\frac{da}{d\delta} = g'(\delta) > 0$$

$$\frac{d^2a}{d\delta^2} = g''(\delta) < 0$$

and the number of wins, $b(X, \delta) = Xa(X,\delta) = \int_0^X f(y)dy + Xg(\delta)$

$$\frac{db}{dX} = f(X) + g(\delta) > 0$$

$$\frac{d^2b}{dX^2} = f'(X) < 0$$

$$\frac{d^2b}{dXd\delta} = g'(\delta) > 0$$

$$\frac{db}{d\delta} = Xg'(\delta) > 0$$

$$\frac{d^2b}{d\delta^2} = Xg''(\delta) < 0 .$$

The USTR's problem written as a LaGrangean is:

$$L(X,\delta,\lambda) = U(a(X,\delta),b(X,\delta)) - \lambda((K+\delta)X - m),$$

which leads to the first order conditions

$$\frac{\partial U}{\partial a}\frac{da}{dX} + \frac{\partial U}{\partial b}\frac{db}{dX} = (K+\delta)\lambda$$

$$\frac{\partial U}{\partial a}\frac{da}{d\delta} + \frac{\partial U}{\partial b}\frac{db}{d\delta} = X\lambda$$

$$(K+\delta)X = m.$$

The Hessian here is:

$$\begin{bmatrix} \overset{<0}{\frac{\partial U}{\partial a}\frac{d^2a}{dX^2}} + \overset{<0}{\frac{\partial U}{\partial b}} f'(X) & \frac{\partial U}{\partial b} g'(\delta) > 0 \\ \frac{\partial U}{\partial b} g'(\delta) > 0 & \frac{\partial U}{\partial a} g''(\delta) + \frac{\partial U}{\partial b} Xg''(\delta) < 0 \end{bmatrix} .$$

The Hessian is negative semi-definite as long as g'(δ) is not too big, and $\frac{d^2U}{dX^2}$, (the top left corner) is negative.

Appendix 2

Totally differentiating the first-order conditions given in Appendix 1 with respect to (X, δ,λ, m) leads to:

$$\frac{\partial U}{\partial a}\left(\frac{d^2a}{dX^2}\frac{dX}{dm}\right) + \frac{\partial U}{\partial b}\left(f'(X)\frac{dX}{dm} + g'(\delta)\frac{d\delta}{dm}\right) = \lambda\frac{d\delta}{dm} + (k+\delta)\frac{d\lambda}{dm}$$

$$\frac{\partial U}{\partial a}\left(g''(m)\frac{d\delta}{dm}\right) + \frac{\partial U}{\partial b}\left(g'(\delta)\frac{dX}{dm} + Xg''\frac{d\delta}{dm}\right) = \lambda\frac{dX}{dm} + X\frac{d\lambda}{dm} \qquad (K+\delta)\frac{dX}{dm} + X\frac{d\delta}{dm} = 1$$

These three equations can be solved as a system to find $\frac{dX}{dM}$ *and* $\frac{d\delta}{dm}$.

$$\frac{d\delta}{dm} = \left[X + \frac{1}{K+\delta}\left(\frac{-U_b(K+\delta)Xg''(\delta) - U_a(K+\delta)g''(\delta) - X\lambda}{U_b(K+\delta)g'(\delta) - U_aX\frac{d^2a}{dX^2} - (K+\delta)\lambda} \right) \right]^{-1}$$

and

$$\frac{dX}{dm} = \frac{1}{(K+\delta)}\left(1 - X\frac{d\delta}{dm}\right), \text{ or } \delta \text{ and X are substitutes.}$$

Notes

∗ The first four sections of this paper rely on the research assistance of Chan Ho Song. Rodney Wallace played a major role in formulating Sections V and VI as did Joel Sobel with Section VII. Their help is much appreciated and none of them are to blame for the context within which their insights and analyses have been

used. The comments of CGP Conference participants are also much appreciated, particularly those of Theresa Greaney, Jude Hays, Rob Howse, T. N. Srinivasan and David Weinstein.

[1] See the discussion on this point in Ernest H. Preeg, *Traders in a Brave New World* (Chicago: University of Chicago Press, 1995) p. 182.

[2] Alan Wm. Wolff, "Hearing on the WTO Dispute Settlement Review Commission Act," Senate Finance Commission, Washington, D.C., May 10, 1995.

[3] John H. Jackson, "Testimony Prepared for the U.S. Senate Finance Committee Hearing, March 23rd, 1994 on Uruguay Round," University of Michigan Research Forum on International Economics Discussion Paper No. 353. Panel findings can be brought to the Appellate Body by the losing party. The decisions of the Appellate Body are adopted by the WTO except where a consensus of the WTO Council decides otherwise.

[4] Alan Wm. Wolff, "Hearing on the WTO Dispute Settlement Review Commission Act."

[5] John H. Jackson, "Strengthening of the Dispute Settlement Function and Future GATT Activities," in *The Uruguay Round: Appraisal and Implications for Investment Trade and Investment*, Tokyo: Fair Trade Center, p. 182. Already during the years prior to the WTO's establishment, no country (or even the EC as a whole) made more use of the DSM than did the United States. Almost one-third of all cases brought to the DSM stemmed from complaints by the United States. See Robert E. Hudec, *Enforcing International Trade Law: The Evolution of the Modern GATT Legal System* (Salem, New Hampshire: Butterworth Legal Publishers, 1993) p. 316.

[6] Peter Behr, "Dole Joins President on GATT," *Washington Post*, November 24, 1994. The strength of populist sentiment fanned by import-competing industries has led some political scientists to argue that the new DSM by removing the single country veto may allow national political leaders too little flexibility in dealing with aggrieved domestic interests. This lack of flexibility may stifle further liberalization. See, for example, Judith Goldstein and Lisa L. Martin, "Legalization, Trade Liberalization and Domestic Politics: A Cautionary Note," *International Organization* Vol. 54 No. 3 Summer, 2000, pp. 603-632, and George W. Downs and David Rock, *Optimal Imperfection?: Domestic Uncertainty and Institutions in International Relations*, Chapter 4 (Princeton, NJ: Princeton University Press, 1995). Not all observers agree that the WTO's DSM allows political leaders little flexibility. Monika Butler and Heinz Hauser, "The WTO Dispute Settlement System: A First Assessment from an Economic Perspective," *The Journal of Law, Economics and Organization*, Vol. 16, No. 2, October, 2000, pp. 503-534, appear to conclude just the opposite.

[7] The establishment of such a review commission as a by-product of the passage of controversial legislation is not unprecedented. The Spring 2000 discussion of a joint White House Congressional commission with powers to review human rights, labor policies and development of the rule of law in China in connection with legislation to grant China permanent Most-Favored Nation status is just the latest instance of the use of this device. For example, see Joseph Kahn, "To Aid Trade Bill, Democrat Creates Plan for Rights Panel," *New York Times*, May 4, 2000.

[8] Congressional Record Senate Volume 141 No. 1, January 4, 1995.

[9] Keith M. Rockwell, "Dole Prepared to Compromise on WTO Review Panel Plan," *Journal of Commerce*, May 11, 1995, p. 3A.

[10] Alan Wm. Wolff, "Hearing on the WTO Settlement Review Commission Act."

[11] Alan E. Holmer, "Hearing on the WTO Dispute Settlement Review Commission Act," Senate Finance Commission, Washington, D.C., May 10, 1995.

[12] Alan Wm. Wolff and John A. Ragosta, "How the Uruguay Round Will Change the Practice of International Trade Law in the United States" (July, 1996).

[13] United States Senate Bill No. 1438, 104th Congress (November 30th, 1995).

[14] John Maggs, "Dole Makes Another Push for WTO Oversight Bill," *Journal of Commerce*, December 6, 195. p. 3A.

[15] John Maggs, "Dole Unlikely to Pass WTO Bill in '95," *Journal of Commerce*.

[16] John Maggs, "Dole Paves Way for Commission to Review WTO," *Journal of Commerce*, June 10, 1996, p. 3A.

[17] John Maggs, "Dole Gives Bill Final Push," *Journal of Commerce*, June 12, 1996, p. 3A.

[18] See, for example, House of Representatives Bill No. 4706, 106th Congress, 2nd Session, June 21, 2000. This bill, introduced at the time of the floor debate of a resolution that would lead to U.S. withdrawal from the WTO, includes only those provisions to which the Clinton Administration had originally agreed 5-1/2 years earlier. While this bill had bi-partisan sponsorship, it had no chance of passage.

[19] Office of the United States Trade Representative, *2000 Trade Policy Agenda and 1999 Annual Report of the President of the United States on the Trade Agreements Program* (Washington, D.C., 2000), Chapter 2.

[20] Both export industries and import-competing industries appear to agree that a higher USTR success rate at the WTO is an indication that the revised DSM is working in accord with U.S. interests. See James McCall Smith, "Domestic Politics and WTO Dispute Settlement Reform," paper prepared for delivery at the 2000 Meeting of the American Political Science Association.

[21] In 77 cases in the 1980s, as either plaintiff or defendant, the United States prevailed in 57. Overall, for the period between 1948 and 1998 in 125 cases, the United States prevailed in 84. See Robert E. Hudec, *Enforcing International Trade Law*, pp. 302-325.

[22] 103rd Congress, 2nd Session, *Uruguay Round Agreements Acts*, Section 125.

[23] Bruce Stokes, "Preparing to Bypass the WTO," *Financial Times* March 29, 2000, p.13. Actually, the joint resolution was initially introduced even before the USTR report was sent to Congress, because the USTR report was sent late. The resolution was then withdrawn and re-introduced ("House Members Move to Sponsor Resolution for U.S. WTO Withdrawal"), *Inside U.S. Trade*, Vol. 18, No. 2 March 3, 2000.

[24] James McCall Smith, "Domestic Politics and WTO Dispute Settlement Reform."

[25] See the remarks of Members of Congress Benjamin Cardin (Democrat, Maryland), Doug Bereuter (Republican, Nebraska), Nancy Johnson (Republican, Conecticut), Kenneth Bentsen (Democrat, Texas), and Phillip Crane (Republican, Illinois) opposing House Joint Resolution 90 in the 106th Congress, 2nd Session, *Congressional Record*, Vol. 146, No. 6 H4787-H4807.

[26] Alan Wm. Wolff, "Hearing on the WTO Dispute Settlement Review Commission Act."

[27] Michael Kantor, "Hearings," House International Affairs Committee, August 4, 1995, *JEI Report* No. 31B, p. 9.

[28] In 1993, this consisted of 173 positions with USTR and 30 authorized detailees from other agencies. In 2000, USTR had 178 positions with 25 authorized detailees (Michael Kantor, "Hearings," House Appropriations Committee, Subcommittee on Commerce, Justice, State, the Judiciary and Related Agencies, April 5, 1995; Charlene Barshefsky, "Hearings on USTR Agenda and Budget Request," House Appropriations Committee, Subcommittee on Commerce, Justice State and the Judiciary, April, 2000). While global and regional agreements have created new responsibilities for USTR, it is also true that it is not yet engaged in a round of world-wide multilateral negotiations as it was in the early 1990s.

[29] Charlene Barshefsky, "USTR Agenda and Budget Request," House Appropriations Committee, Sub-Committee on Commerce, Justice, State, the Judiciary and Related Agencies, March 17, 1999.

[30] Office of the United States Trade Representative, "Budget Proposal for Fiscal Year 2002," April 9, 2001.

[31] For the purposes of this section, it can be assumed that the trading partner on the opposing side of the case refuses to engage in bilateral negotiations under any circumstances. Clearly, this is only one of many assumptions that might be made.

[32] The justification for a USTR utility function of this form is outlined in Sections I, II and III of this paper.

[33] See Appendix 1.

[34] Figure 1 is taken from David Weinstein's October, 2000 comment on this paper.

[35] On the last three points, see Robert E. Hudec, *Enforcing International Trade Law*, p. 326.

[36] I would like to thank participants in the May Pre-Conference, particularly Theresa Greaney and Rob Howse, for their suggestion that this section be written. Needless to say, they are not to blame for the form it has taken.

[37] The assignment of these roles to USTR and MITI is arbitrary. The roles could equally well be reversed. The analysis here is merely meant to be illustrative.

[38] Robert E. Hudec, *Enforcing International Trade Law*, p. 319.

[39] Young Duk Park and Barbara Eggers, "WTO Dispute Settlement 1995-99: A Statistical Analysis," *Journal of International Economic Law*, Vol. 3 No. 1 (March 2000) pp. 183-204.

[40] Robert E. Hudec, *Enforcing International Trade Law*, p. 316.

[41] Young Duk Park and Barbara Eggers, "WTO Dispute Settlement 1995-99: A Statistical Analysis," p. 195.

[42] As noted in the analyses in Section V, were this to happen, it would lead to the USTR taking more cases to the WTO.

[43] John H. Jackson, *The Jurisprudence of GATT and the WTO* (Cambridge: Cambridge University Press, 2000) pp. 179-80.

[44] It is assumed in this analysis that the plaintiff in a WTO case knows more about the merits of the case it brings then does the defendant. For example, a plaintiff government knows better whether its constituent firms have been injured by the failure of a defendant government to meet its WTO obligations than the defendant government itself. While this may not always be the case, it is not inconsistent with assuming that both parties to the dispute know ρ, the quality of the DSM, and ε, the random drawing of all possible remedies.

[45] In the conventional legal setting, there is a substantial literature that finds that the more information there is about judicial outcomes, the more probable it is that litigants will risk a trial. See, for example, John B. Gould, "The Economics of Legal Conflicts," *Journal of Legal Studies*, June, 1973 2(2) pp. 225-251; Robert H. Mnookin and Lewis Kornhauser, "Bargaining in the Shadow of the Law: The Case of Divorce," *Yale Law Journal*, April, 1979, 88 (5) pp. 951-997; Henry S. Farber and Harry C. Katz, "Interest Arbitration, Outcomes, and the Incentive to Bargain," *Industrial and Labor Relations Review*, October, 1979. Unlike the analysis presented here, this literature assumes that the litigants are risk-adverse.

[46] William J. Davey, "The WTO Dispute Settlement System," *Journal of International Economic Law* Vol. 3 No. 1 (March, 2000) pp. 15-18.

[47] There is already a substantial analytical literature on the resolution of trade disputes whether inside or outside the GATT or WTO. See, for example, Kathryn E. Speir and David E. Weinstein, "Retaliatory Mechanisms for Eliminating Trade Barriers: Aggressive Unilateralism vs. GATT Co-operation" in Winston W. Chang and Seiichi Katayama (eds.) *Imperfect Competition in International Trade* (Boston: Kluwer Academic Publishers, 1995). None of this work, however, allows for USTR concern with success rates.

Table 1. USTR and MITI: Likelihood of Success with Incremental Resources and Differential Weights on Outcomes

		Baseline	Δ 1a	Δ 1b	Δ 2a	Δ 2b	Δ 3	Δ 4a	Δ 4b	Δ 5a	Δ 5b
	α	1	1	1	1	1	1	1.25	1.5	1	1
	β	1	1	1	1	1	1	1	1	1	1
	ρ	1	1	1	1	1	1	1	1	1.25	1.5
	θ	1	1	1	1	1	1	1	1	1	1
action	δ	0.1825	0.21	0.24	0.16	0.14	.1845	0.15	0.12	.225	.265
action	γ	0.8093	0.75	0.67	0.78	0.75	.7612	.771	.732	.705	.601
	h	.05	0.1	0.15	0.05	0.05	.075	0.05	0.05	0.05	0.05
	x	0.05	0.5	0.5	0.1	0.15	.075	0.05	0.05	0.05	0.05
result g (case 1)		-.6437	-.59	-.52	-.6408	-.637	-.6137	-.6415	-.6431	-.552	-.4473
result g (case 2)		.332	.203	0.05	0.27	0.21	.2298	.25402	.1772	.1134	-.073

Figure 1 Equilibrium

