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The safeguards mess revisited: the fundamental problem

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In the November 2003 issue of this journal, Alan Sykes describes the WTO Safeguards Agreement (SA) as 'a mess' (Sykes, 2003). The author sets out to show that the criteria for using safeguards protection under WTO rules, and Appellate Body (AB) decisions related to dispute settlement cases over such protection, are incoherent. Any use of protection under the SA therefore appears doomed to being struck down in a WTO challenge. The author believes that the AB could rectify this situation in the form of guidelines to make safeguards protection operational, assuming that such protection should be used in the first place.

Finding a systematic way of channeling, controlling, and limiting protectionist pressures in order to maintain the necessary domestic political consensus for trade liberalization has been the 'holy grail' of GATT/WTO safeguards reform for many years. Sykes' analysis demonstrates that the lack of clarity in SA language and AB jurisprudence make the existing safeguards measures a seemingly unattractive legal instrument through which WTO members would channel domestic protectionist demands for import relief, since the AB has shown that it will overturn such measures in a dispute settlement challenge.

Yet Sykes' narrow focus on the legalistic issue of establishing 'coherent' SA practice fails to address the larger issues of the incentive structure for safeguards and related measures and the process of achieving coherence in the consensual WTO system. In short, Sykes digs deeply along the legal dimension of the issue, but gives scant attention to its political dimension.

This note will argue that the safeguards issue is better described as a long-standing 'muddle' that has existed in the GATT/WTO system for many years, rather than as a precipitous 'mess' resulting from the SA and recent AB jurisprudence. It will also argue that (1) the concept of safeguards rests on an inner contradiction, which is why participants in the GATT/WTO system have consistently and deliberately made it difficult to impose trade restrictions on fairly traded goods, (2) challenges to the SA are primarily the result of weakened compensation provisions and changes in the policy environment, which has upset the precarious balance in the safeguards arrangement, and (3) sustainable safeguards reform must proceed on the basis of consensus among WTO members. The real problem lies

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not in the lack of coherent safeguards jurisprudence, but rather in the continued lack of progress by WTO members in promoting adjustment to trade and achieving consensus on what the rules should be.

Safeguards: the inner contradiction

The main shortcoming of Sykes' article is that it provides no coherent policy framework of its own for understanding the underlying safeguards issue, which is how to devise trade negotiating 'insurance' and a 'safety valve' for protectionist pressures, while also contributing to trade adjustment among import-competing industries. Historically, safeguards measures have never been widely used, and the reluctance of WTO members to establish more specific language in the SA may simply reflect their longstanding aversion to legitimizing a clearly defined and easily applied escape clause for disruptive but fairly traded goods. In this regard, I believe that Sykes misses an essential point.

The original GATT safeguards provision allowed protection against fairly traded goods, but only at a high political price – and the GATT Contracting Parties meant it to be that way. Its provisions, if abused, overused or extended, could have reversed much of the trade liberalization that the GATT achieved through multilateral negotiations. Because safeguards allow trade restrictions on fairly traded goods, the GATT Contracting Parties, and later the WTO member countries, have always exhibited a deep-seated suspicion towards them. The problem lies in the fact that countries negotiating reciprocal tariff reductions want to reserve the right to invoke safeguards protection in case future import competition raises protectionist pressures at home. Yet these same countries do not want safeguards measures imposed against their own fairly traded exports. After all, trade liberalization is supposed to allow exports exhibiting increased international competitiveness to gain the increased market share they deserve; safeguards tend to punish exporters for their increased efficiency. In this manner, safeguards embody an inner contradiction for the GATT/WTO system: MFN trade restrictions to promote MFN trade liberalization. Trade negotiators have always had difficulty reconciling these two opposing elements, and so the rules have reflected a marked ambivalence towards the concept of safeguards, acknowledging their political expediency but making them politically expensive. Hence article XIX included an MFN requirement, a serious injury test, and the need to show 'unforeseen' trade disruption, among other requirements, all of which made escape clause protection difficult to apply. Later, the ambivalence reappeared in the muddled language of the SA and the reluctance of the AB, in the absence of WTO consensus, to establish its valid application. Understanding the contradictory nature of safeguards and WTO ambivalence towards them goes a long way towards explaining the safeguards 'mess', which Sykes examines only in terms of its outward, legal manifestation.

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In considering such institutional issues, it is useful to step back and avoid framing the issue as one in which the goal is to make valid safeguards protection 'easier', even if many consider that outcome to be necessary in order for the SA to perform its proper 'safety valve' function. The WTO is set up in principle to balance rights and obligations of *all* its members. Making SA protection easier would take away market access for a WTO member who is likely to regard such access as an integral part of its WTO bargain. Why should WTO members' exporters be made sacrificial lambs so that the SA can 'work better?' Safeguards measures, like nearly all trade protection, are ultimately set up as a one-sided affair that favors import-competing interests at the expense of domestic consumers and foreign exporters, thereby negating the net gains from trade.

Sykes clearly acknowledges the economic problems with safeguards protection in principle. It should be clear that a balanced political agreement among WTO members on its use is necessary in order to maintain an overall, sustainable WTO bargain. In this regard, it is important to note that the original GATT article XIX tended to prevent the abuse of safeguards measures through built-in reciprocity, which allowed affected exporting countries either to receive compensation in the form of equivalent trade concessions or to retaliate in a proportionate manner. The SA, however, weakened this compensation provision in an apparent effort to make safeguards protection relatively more attractive and thereby to establish its role as a more effective safety valve. It is quite possible, in this regard, that at least some WTO members looked upon the SA as sufficiently vague on qualifying criteria for protection that they were willing to give up the compensation requirement for the first three years as part of the bargain. Allowing the AB to fill in the legal gaps could therefore upset the political balance that established the SA in the first place.

The changing policy environment

The SA forms part of a broader 'safeguards complex' that also includes anti-dumping, countervailing duty, and other WTO provisions allowing members to withdraw normal WTO trade policy obligations. Sykes pays little attention to the interdependency of protective devices, as well as dispute settlement dynamics (Bown, 2002), which contribute to the incentive structure for WTO members to use various trade restrictions. In this context the terms of the SA are part of a balancing act that determines the relative attractiveness of various alternative policy devices, especially between 'fair' and allegedly 'unfair' trade, used in response to a surge in imports. Changing SA jurisprudence to clarify its terms would surely make it more coherent, but if such clarity were to lead to a large increase in its application, then the repercussions for the trading system could be dangerous. The weakening of compensation provisions in the SA could trigger such responses, for example. Retaliation in kind, or through alternative unfair trade measures, might ensue. There would be economic incentives for exporting

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countries to pursue more dispute settlement challenges to the SA. If activist AB jurisprudence were seen as an unauthorized change in WTO obligations, a political crisis could result, undermining the credibility of the trading system.

At the same time, it is useful to look at the record of safeguards initiations in order to see how disruptive the 'mess' has been. As noted earlier, safeguards measures have never been very popular in the GATT/WTO system, although their use has actually increased under the SA. Under the GATT system from 1950 to 1994, 150 'emergency' (safeguards) actions were taken under article XIX, an average of just 3.4 per year (see Hoekman and Kostecki, 2001, chapter 9 and Finger, 2003). In the 1960s, discriminatory VER agreements had begun to supplant article XIX measures as the way to deal with troublesome imports, beginning with textile trade restrictions. The popularity of VERs increased throughout the 1970s and 1980s, but this trend was accompanied by a massive increase in antidumping initiations, which have now become the instrument of choice in dealing with politically difficult imports – 1,868 initiations and 1,059 actual measures taken from 1995–2001 alone (WTO, 2003). SA negotiations were part of a package that eliminated the use of VERs, although the discriminatory nature of antidumping measures meant that this instrument would continue to proliferate. Under the revised SA, WTO members notified initiation of 110 article XIX actions from 1995–2002, representing a significant increase over the GATT period to an average of nearly 14 per year (WTO, 2003).

In the period since the beginning of the SA, six WTO dispute settlement cases involving safeguards actions have reached the AB (four against the US, one against Korea and one against Argentina). In each of these cases the AB overturned the use of safeguards, and this development is the subject of Sykes' analysis. From the statistics alone, however, it is not clear that AB decisions have rendered the SA a 'dead letter', or that the decisions have even diminished the overall application of article XIX measures – safeguards initiations actually increased in the 2000–2002 period compared with the previous three-year period. In addition, numerous other dispute settlement cases involving safeguards have ended either with bilateral agreements or with acceptance of panel decisions (see WTO website, 2004). Furthermore, Sykes fails to make a compelling case that the AB decisions threaten the overall WTO system. He cites the danger that legal incoherency in the SA will encourage WTO members to resort to antidumping cases or extra-legal measures such as VERs. Yet it is not clear from his analysis that a fine-tuned SA would effectively reduce the overall use of protective devices against imports. In fact, the number of antidumping cases has risen even as the number of safeguards cases has risen.

Consider also the US steel industry, which received safeguards protection that the AB recently found to be in violation of the SA. In the United States, the steel industry has received various forms of trade protection for most of the time period from 1968 to the present, including article XIX safeguards, anti-dumping duties, 'trigger prices' and numerous voluntary restraint agreements. The wording of the

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safeguards clause is that protection should be temporary – normally no more than four years – and geared towards adjustment, even though this term is not defined specifically. If the AB had 'clarified' SA practice and consequently upheld the US steel safeguards measures, could one realistically expect steel protection to end after four years, or would one rather expect the industry to continue to use any and all other available avenues of protection, as it always has? This problem points to the need for comprehensive reform across the entire safeguards complex, with across-the-board incentives for adjustment and tighter rules on ending contingent protection, in order to achieve meaningful progress in managing trade disruptions and disputes. SA coherence, on its own, is unlikely to move towards this goal.

Other aspects of the changing policy environment have shaped the safeguards issue over the years. In the absence of a binding dispute settlement system under the GATT, for example, many of the criteria for Art. XIX interpretation were never authoritatively defined. Furthermore, clever trade policy officials came up with VERs as a way of avoiding the MFN trade restrictions and other onerous GATT rules, opting for the politically cheaper discrimination of bilaterally negotiated quotas. The SA negotiations acknowledged the heavy systemic and economic cost of VERs, and formally banned their use as part of a package of safeguards reforms (see Robertson, 1992). Yet the ill-defined terms of the SA, which Sykes investigates in detail, reveal that WTO members were still very wary about opening up the escape clause window too far with clear-cut rules on key elements, such as how to prove serious injury due mainly to trade. More likely, the ambiguity that resulted was designed to stop VERs while allowing existing national safeguards legislation to continue under the hazy rules. The fly in the ointment, however, was the introduction of a revised Dispute Settlement Understanding with its new, virtually blockage-proof panel/AB decisions. In order to confirm a valid application of the SA, the panels and AB would have to take a stand on critical definitions. The decisions of the AB suggest that it is not ready to adjudicate the terms of SA application in the absence of consensus on the negotiated SA text itself.

The purposeful obfuscation in the SA text is in this regard also likely to be a result of the dangers of providing too solid a foundation for 'safety valve' measures. The original GATT enshrined antidumping as a legitimate trade policy device in article VI, a measure that was also widely accepted at the time as a necessary concession to import-competing interests, part of a political balancing act that would facilitate a coalition for trade liberalization. Yet opening the door to targeted restrictions against 'unfair' trade eventually led to their protectionist capture, administrative mutation and massive proliferation. Antidumping laws are discriminatory and unilateral, the politically 'cheapest', and therefore the most attractive and widely used trade policy device in the safeguards complex. WTO members are unlikely to favor an extension and deepening of administered protection into the realm of fairly traded goods through detailed safeguards

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rules, which could be a real danger if they encouraged governments to turn decision-making over to an independent technical process within administrative bodies, as is the case with unfair trade law.

Sykes rightly concludes that safeguards measures have no direct economic justification on their own, but only insofar as they can facilitate trade liberalization. Yet the ambivalence of countries towards these measures and the availability of alternative measures suggest that his contractarian theory of safeguards does not work neatly in practice. According to Sykes, 'an ideal trade agreement … will maximize the net political gains relative to political costs, allowing the officials to achieve their Pareto frontier' (Sykes, 2003). Safeguards contribute to this outcome, according to his theory, because they allow one party the right to revoke a trade liberalizing measure that would cause a *net* political cost to the two parties. Thus, a surge in fairly traded imports may increase the political cost of trade liberalization in the importing country, whose trade officials then gain politically by invoking safeguards protection. At the same time, the safeguards protection presumably does less damage to exporters and trade officials in the exporting country, because the increased exports that caused the problem are typically a sign of expansion and prosperity. Trade officials in the exporting country are therefore likely to accept the safeguards measure in principle because of the prospect that they will suffer less political damage from it, while recognizing that such measures are necessary to support the broader goals of trade liberalization in general.

This 'mutual gains' theory of safeguards is surely a tenuous proposition in light of its delicate balance between the political fortunes of trade for governments in the importing and exporting countries, which implies that any such agreement is likely to be subject to defection, challenge, and re-negotiation, in other words, a safeguards 'mess'. As noted earlier, countries may accept the general concept of safeguards measures *ex ante* and yet oppose them (when reality strikes on the receiving end) *ex post*, especially since the goods involved are fairly traded. In addition, the acceptability of the agreement will be very sensitive to the terms as they apply to both parties. The weakening of the compensation provisions in the SA surely altered the incentive structure of formally opposing a safeguards initiation in this regard, since it made a dispute settlement challenge more worthwhile to the exporting countries.

On the other hand, the 'cost' of using safeguards protection, compared with the alternatives, will typically determine the frequency of its use. The strictures of safeguards criteria have tended to cause countries facing troublesome imports to 'defect' from the safeguards contract and turn increasingly to easy-to-use, discriminatory, unilateral, non-compensated antidumping measures. Insofar as a safeguards contract exists in the WTO system, it seems to have taken the form of a broader implicit agreement that depends heavily on labeling disruptive imports as 'unfair', so that administrative protection can be applied, while officially maintaining WTO-negotiated market access for fairly traded goods. Changes in safeguards practice under the SA, combined with the elimination of VERs and

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the strengthening of dispute settlement procedures, clearly upset the balance of expectations in the contract in a number of cases. On an issue of this magnitude, the AB has not ventured to re-strike the balance in the absence of a WTO consensus.

Consensus as the basis for reform

Sykes implies that WTO members are counting on the AB to provide clarity on the issue through a series of landmark decisions defining terms such as 'serious injury' and how it can be sufficiently demonstrated. He compares the lack of coherence in the SA with the vague provisions of US Sherman Anti-trust Act of 1890, which the US courts eventually clarified through their active interpretation and jurisprudence. Yet the comparison of the WTO dispute settlement system with a federal system of national law, supported by a constitution and the powers of a sovereign state, is inappropriate.

The WTO dispute settlement system rests on the consensus of its members, with the provision that panel and AB decisions will not impose any new obligations on the members. While some international law scholars believe that the AB should actively extend international law through their interpretive powers, a broader perspective on the political and historical context of the SA suggests that any attempt by the AB alone to tilt the rules towards facilitating safeguards protection would be likely to lead to serious conflict among WTO member countries, because safeguards are a potentially huge loophole for reversing trade liberalization. In the meantime, the cycle of dispute settlement case filing, review, and appeals has at least in some cases allowed countries to get away with 'unacceptable' SA protection and phase it out before the political temperature gets too high and retaliation becomes an issue, as in the recent US steel safeguards case. The broader question is therefore how much trouble SA reform, re-negotiation or definitive interpretation is worth, based on the amount of tension and systemic instability it might cause. Defining the terms of legitimate SA application is only one part of the puzzle, since protection flows in a 'hydraulic' institutional system towards the channels of easiest use and lowest political cost.

Ultimately, one can conclude that the safeguards system is 'not working', in the sense that the AB has overturned its application each time a challenge has reached that stage, but this observation begs the more fundamental question of how the safeguards system should be working. Protectionist pressures will continue for the foreseeable future, and it will therefore be necessary to provide for some sort of device that provides a safety valve for such pressure to protect against future protectionist disruption of trade relations. Yet it is not clear that activist AB decisions should tread where reluctant WTO members are fearful to go. In addition, a codified set of legal rules or activist WTO jurisprudence to backtrack from trade liberalization regarding fairly traded goods could do more damage in

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establishing administratively managed protection along the lines of GATT article VI than would be gained by channeling protectionist pleas away from anti-dumping and other sources.

The WTO safeguards 'system', such as it is, appears to serve trade liberalization in *ad hoc*, 'messy' and at times inconsistent ways. Member countries seem to accept safeguards, however ill-defined, as a necessary provision for trade negotiations and the management of trade relations without using it very much – or lately, without expecting it to survive a WTO challenge. The SA was part of a political bargain that eliminated the use of VERs, and this was a major accomplishment of the Uruguay Round. Yet one could not expect the underlying pressures for trade restrictions to go away simply by plugging the VER loophole, and trade officials were not ready to conclude an SA that would act as a close substitute for VERs or antidumping measures. In this regard, safeguards reform still needs to work towards a comprehensive system of incentives for adjustment and a reduction in trade conflict. The way forward is for governments to develop more effective industrial and worker adjustment policies, thereby reducing the protectionist pressure that safeguards must relieve.

Reform of the SA itself should begin by establishing a negotiating agenda for workable definitions and methodologies, with an eye towards the relative attractiveness of alternative measures that serve as channels for protectionist policies. This is not necessarily to advocate a new agreement, but to test the waters thoroughly for the political will to take action, since a systematic reduction in trade conflict can be secured only through consensual action by the WTO members. In the meantime, WTO members will be wary of any panel and AB decisions to establish SA guidelines on this politically sensitive issue. The economic models discussed by Sykes to sort out injury questions provide a useful starting point for establishing practical rules, as long as they can avoid protectionist capture, but WTO members are unlikely to accept AB decisions that unilaterally introduce such methodologies. Some politically creative way of introducing these rules on the basis of multilateral consensus will be required. Those who think that this step will be easy should ask any economist who has had the pleasure of pleading for economic analysis as the basis for trade law regulation before government officials in charge of the process.

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