

The EU and world trade

**Dick Cunningham,
Peter Lichtenbaum &
Julie Wolf**



ABOUT THE AUTHORS

Richard Cunningham is a senior partner at the Washington law firm of Steptoe & Johnson. He has wide experience in the field of international trade law and policy, particularly in the areas of unfair trade remedies, market access initiatives and GATT/WTO negotiations. Peter Lichtenbaum is also a partner at Steptoe & Johnson, practicing in international trade and business regulation. He has extensive experience in GATT/WTO dispute settlement cases and previously served at the US Department of Treasury.

Julie Wolf reported on the European Union for the *Wall Street Journal Europe* and *The Guardian* from 1986-1999. Among the subjects she covered were transatlantic trade relations, the launching of the EU's single market and the euro, and competition policy. Educated at New York University and Sussex University, Julie Wolf is currently writing on international trade and economic affairs from her new base near Geneva.

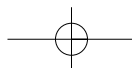
Steven Everts is a research fellow at the Centre for European Reform. He is the author of *The impact of the euro on transatlantic relations*, published by the CER in January 2000.



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Lilly is delighted to sponsor this Centre for European Reform pamphlet on 'The European Union and world trade'. It is clear that the global trade talks are experiencing difficulties. There is no shared vision between the EU, the US and the developing countries regarding the proper focus of a new round of trade negotiations. Meanwhile, public scepticism of the effects of globalisation appears to increase. Complex trade issues, such as regulatory standards and their effects on free trade, are often poorly understood. That is why a genuine debate on trade questions is needed.

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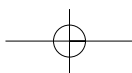
Introduction: new priorities for EU trade policy

Steven Everts

The paradox of trade policy is that, at a time when political leaders in most parts of the world have accepted the intellectual case for trade liberalisation more thoroughly than ever before, public opposition to free trade is on the rise. Most politicians are keen to advance the cause of free trade because they understand that it brings about economic growth. But they know that they must also address the legitimate concerns of developing countries about the workings of the world trading system, while simultaneously trying to respond to domestic criticism by those whose interests may suffer at the hands of market liberalisation.

The task of politicians is complicated by the fact that trade negotiations are increasingly about health and food safety standards, or about rules on competition and inward investment, rather than 'simple' questions such as tariffs and quotas. These issues used to belong firmly to the domestic political sphere, where each national government ruled as it saw fit. But these days they are subject to decision-making in multinational institutions like the European Union (EU) and the World Trade Organisation (WTO).

Governments are struggling to launch a new round of trade liberalisation in the face of rising public scepticism about the supposed benefits of free trade and globalisation, as well as increasing worries about the WTO's perceived lack of accountability. The WTO and other international organisations are often seen as part of the problem, rather than part of the solution. If the politicians fail to counter such fears—which may be misplaced but will not simply disappear—the result is likely to be even greater public hostility and more pressure for protectionism. That is why a debate on global governance, and on how the international institutions such as the WTO should be reformed and strengthened, is so urgently needed.



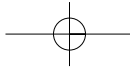
But politicians prefer to avoid making hard choices. And officials often get lost in the minutiae of day-to-day negotiations. Journalists, for their part, tend to focus on a small number of high-profile trade rows, especially between the Europeans and the Americans. Meanwhile, the big picture gets lost, the issues are muddled and trade policy is allowed to drift. At the time of writing (September 2000) there is not much prospect of the WTO round that was still-born in Seattle being revived.

To inject some fresh thinking into the trade debate and offer concrete policy proposals on the way forward, the CER is publishing two essays. First, **Dick Cunningham** and **Peter Lichtenbaum**, two US trade lawyers, explain why there is a leadership vacuum at the WTO and, consequently, why the EU should take the lead and shape the agenda for a new trade round that is suited to its needs.

However, they warn that in order to assume a leadership role and restart negotiations, the EU must take some difficult decisions, particularly on agriculture liberalisation and the curbing of subsidies. The Europeans should search for creative ways in which the 'new issues' on the trade agenda, such as worker rights and environmental standards, can be integrated into trade talks. Yet the EU should stop well short of the sanctions-based approach favoured by some non-governmental organisations (NGOs) and—at least at Seattle—the US administration.

To shore up an open and rule-based trading system, Cunningham and Lichtenbaum call on the EU to abide by all the rulings of the WTO dispute settlement system. This means that in the cases that the EU has lost, such as on beef hormones and banana imports, it should implement the required policy adjustments without further delay.

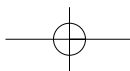
Using a broader canvass, **Julie Wolf**, a former Brussels correspondent of the Wall Street Journal Europe, stresses that trade issues should be discussed in the context of the debate on globalisation. After analysing the reasons behind the failure of Seattle, she concludes that politicians must make, rather than assume, the case for free trade. The task ahead is to construct a more 'people friendly' global trading system, which takes concerns about the environment, human rights and poverty seriously—without provoking a slide toward protectionism.

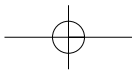
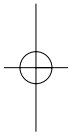
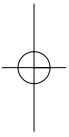
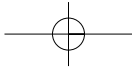


Wolf agrees with Cunningham and Lichtenbaum that the EU should take the lead in trying to restart global trade talks. This is not only because the US will be distracted for months to come by its presidential elections. More fundamentally, the EU is well-placed because it often takes a middle position on the 'new issues', between the US and some radical NGOs on the one hand, and many governments of the developing world on the other.

But to win support and convince the doubters of the EU's free trade intentions, Europe will have to make greater concessions on the important question of agriculture. Wolf proposes further shifts of farm spending, away from export and production-linked subsidies, towards direct income payments for small farmers and the promotion of organic products. Radical reform of the Common Agricultural Policy (CAP) is essential in order to restore the EU's international standing and to reduce the environmental damage that the CAP currently causes.

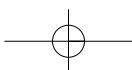
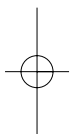
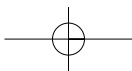
Finally, Wolf suggests streamlining the way the EU structures its decision-making on trade issues. She argues that the Commission should be given full jurisdiction over all areas of trade, not just over trade in goods. Such a reform is necessary to enhance the Commission's ability to negotiate effectively on behalf of the 15 member-states, and to reassure the EU's trading partners that it will be able to 'deliver' on any trade accord it concludes.





How the EU can revive the Millennium Round

**Richard Cunningham and
Peter Lichtenbaum**



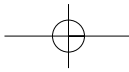
1 Introduction

The attempts to launch a new “Millennium Round” of world trade talks are forcing the EU to rethink its attitude toward trade policy. The United States, which at the Seattle meeting in December 1999 failed to kick-start a new round, is for the time being unlikely to take the lead. As Pascal Lamy, the European Commissioner for trade, has rightly concluded, this temporary leadership vacuum at the WTO provides the opportunity for Europe to take the initiative in reviving that new round.

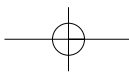
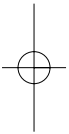
The round is of paramount importance to Europe, not only because its economy would benefit from the removal of trade barriers in markets that matters to its exporters. Europe also needs the pressure of multilateral trade negotiations to carry out reforms—most notably in agriculture but also in subsidies for some manufacturing sectors—that would bring significant economic benefits, but which entrenched domestic constituencies oppose.

It is not clear, however, that Europe has the political will to take the lead, or indeed to accept the conditions necessary for a round to be launched. Unwilling to stand up to pressure from domestic interests, the EU has backed away from important principles agreed in the Uruguay Round on the use of subsidies. Moreover, Europe’s commitment to the non-blockable dispute resolution mechanism—perhaps the single most important achievement of the last round, and a central element of the global trading system—has faltered when the rulings have been politically unpalatable.

Despite these disturbing indications, this paper argues that the EU can and should take a leading role in launching the Millennium Round. It will have to show dexterity and creativity to allow greater participation by the developing nations, and to reach agreement with the US on the major issues of investment and competition policy. Most importantly, the EU will require ingenuity and political courage to handle the negotiations on agriculture, and to deal with the issues of the environment and workers’



rights, in ways that both the developing nations and the “civil society” proponents in Europe and the US can accept.



2 Why the EU should lead a new trade round

The EU is a major beneficiary of the liberalisation of world trade. As the world's largest exporter of goods and services, it stands to gain substantially from a further opening of foreign markets. Exports to markets outside the EU account for 9 per cent of EU GDP and 10 per cent of EU employment—around 11 million jobs. As exports increase—because of the market access commitments and new disciplines imposed on the EU's trading partners by further multilateral trade negotiations—the number of jobs will grow. Moreover, while many countries have resisted a return to protectionism in the wake of the Asian financial crises of 1997, a new round of multilateral liberalisation will reinforce the anti-protectionist policies currently maintained by those states, with obvious economic benefits to the EU.

Further trade liberalisation will also increase imports of foreign goods, a benefit often downplayed by politicians. The development of the EU's internal market is evidence of Europe's recognition that imports serve domestic consumers by enhancing individual choice. Imports, especially raw materials, are also crucial for many European producers which rely on products from outside the EU for the efficient production of their goods.

Multinational trade negotiations have also played an important role in accelerating some forms of economic reform within the EU and other major trading areas. The need to meet WTO commitments has often emboldened governments to confront entrenched domestic interests. The 1992 MacSharry reforms of the Common Agricultural Policy (CAP) provide an example of the benefits brought by international trade negotiations. With its interlocking import barriers, export subsidies, price support mechanisms and production-based payments, the CAP has long been an extraordinarily generous programme of financial support to the farm sector. The policy is maintained at great expense to EU consumers and



at a crushing cost to the EU's budget. Despite these costs, the EU failed to introduce significant reforms until 1992 because of opposition by entrenched and vocal agricultural interests in certain major member-states.

As the Uruguay Round neared its conclusion in 1990 there were massive demonstrations by European farmers opposed to even minimal reform of agricultural support programmes. Resistance from farmers significantly delayed the completion of the round. But in the end the pressure of multilateral negotiations enabled the Commission to adopt a significant package of new agricultural measures—devised by the then commissioner, Ray MacSharry—that were clearly in the Community's broader economic interest.

The value of a new round, as a way of helping to push through difficult internal reforms, may be even greater for the EU today than it was in the early 1990s. In 1990 the EU funded the CAP to the tune of almost €26.5 billion. The EU's 2000 budget, however, allocates over €40.5 billion towards the CAP, an increase in nominal terms of over 52 per cent. In addition, the enlargement of the EU to the central and eastern European states—whose economies are more rural than even the poorest of current members—will have a much more severe impact on the agricultural budget than the earlier accession of Spain and Portugal.

The European Commission is well aware of these problems, and its Agenda 2000 document, adopted by the Berlin European Council in March 1999, acknowledges that it will be impossible to maintain CAP funding at present levels. Translating Agenda 2000 into meaningful reform measures, however, remains a daunting political challenge that may not be achievable without the external pressure of a new round.

The EU is also under international pressure to change the *nature* of its agricultural supports: to eliminate export subsidies and to convert domestic supports into income supplements. This pressure will intensify with the impending expiry in 2003 of the so-called "Peace Clause", which currently insulates from the dispute resolution procedures those aspects of the CAP that are inconsistent with WTO rules on subsidies.

A trade round would also help the EU to achieve economic reforms in other areas, such as subsidies. In aerospace and other industrial sectors,

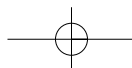
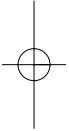


both the EU and national governments continue to subsidise new product development. Such aid is regularly sanctioned on the explicit basis that the project in question would be uneconomic without government support. Moreover, the amounts of such aid are large, both at the EU and member-state level. For example, the EU's "Fifth Framework Programme" provides research aid to the aeronautics sector for the period 1999-2002 worth €700 million, a 137 per cent increase over the previous four years. Even larger amounts are provided by certain member-states, such as France, Germany and Britain. National government aid to Airbus Industrie for development of its A3XX "super jumbo" airliner is expected to total at least €4 billion. The British government has already approved aid for the A3XX worth £530 million, (€832 million) payable to BAE Systems, which comprises 20 per cent of the Airbus consortium. Such aid is normally provided as advances repayable only to the extent that sales of the subsidised product generate sufficient revenue. The WTO has previously ruled that such forms of aid constitute illegal subsidies.

European governments justify their assistance on the grounds that the US civil aircraft industry benefits from large contracts with the US Department of Defense and NASA. However, such government procurement of research or defence/space products is not a subsidy under WTO rules, unless the government pays more than the value of what it procures. Moreover, the Airbus partners are themselves major participants in defence procurement in Europe. In any case, an argument about alleged US subsidies would not prevent a WTO panel from condemning the EU subsidies. Under present WTO rules, therefore, the EU may soon come to a point at which it will be directed by a WTO panel to end such subsidies, a ruling that would undoubtedly generate strong political protest from powerful industries. Resolution of the issue would be facilitated by the possibilities for a broader negotiation in the context of a new WTO round.¹

It is also imperative that the EU addresses the use of the "precautionary principle" to stop or delay imports of genetically-modified (GM) foods. On this issue, the domestic political pressure is immense, driven by public opinion, the "green" element in European politics and largely sympathetic administrations in most member-states. However, the EU has agreed to WTO rules which

¹ It should be noted that the authors of this paper are legal counsel to The Boeing Company on the issue of Airbus subsidies



state that imports of a product can be restricted on health and safety grounds only where there is sound scientific evidence that the product poses a threat to health or safety. In the “Beef Hormones” case, the EU argued vigorously that the precautionary principle justified restrictions on imports—in the absence of scientific evidence of harm to health and safety—until it could be established that these products were safe. A WTO dispute resolution panel explicitly rejected that argument because at the time there was no firm evidence of a threat to public health, although more recently certain EU studies have found that the hormones may have some carcinogenic effects.

Nor can the EU take much comfort from the recently-concluded Biosafety Protocol to the United Nations Convention on Biological Diversity. This agreement incorporates the “precautionary principle” as the standard for government restrictions on the trade in living modified organisms. But the preamble to the protocol explicitly provides that it “shall not be interpreted as implying a change in the rights and obligations of a Party under any existing international agreements.” Therefore “scientific principles” remain the basis for WTO dispute settlement in cases concerning trade-restrictive measures taken to protect human, animal, or plant health. Thus, if the EU seeks to apply the precautionary principle to imports of GM foods or other products, it faces trade wars and costly retaliation under the current WTO rules.

In sum, there are powerful reasons for the EU to press for a new round of multilateral trade negotiations. Moreover, since the highly contentious issues—such as agriculture, GM foods and industrial subsidies—consume most EU attention during trade negotiations, it would be highly beneficial for the EU to take the lead in initiating discussion on these topics. In the wake of the Seattle failure, the EU has precisely that chance. But does it have the political will to seize that opportunity?

The failure at Seattle: an open door for the EU

In the run-up to the Seattle ministerial meeting, the EU and the US articulated two quite different visions for the shape of a Millennium Round. Europeans advocated a comprehensive negotiation that would address a broad liberalising agenda, including:



How the EU can revive the Millennium Round

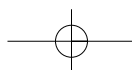
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- ★ Liberalisation of trade in services.
- ★ A framework of rules aimed at securing a stable and predictable climate for investment worldwide.
- ★ Harmonisation of competition laws around core principles.
- ★ Transparency and liberalisation in government procurement.
- ★ Trade facilitation by simplifying customs and border procedures.
- ★ Further industrial tariff reductions and the elimination of both peak tariffs and almost all tariffs on imports from the least-developed countries.
- ★ Limited but significant liberalisation in agriculture.
- ★ Review of the WTO Antidumping Agreement.

In contrast, the US sought a more limited round, focused primarily on market access measures, and it aimed at concluding all negotiations in three years. Both the limited agenda and the three-year duration are central to an understanding of the US-EU division. And the issue of agriculture is relevant to both.

It should be understood at the outset that, with the exception of agriculture and, to a lesser extent, e-commerce, there has been no great pressure for a new round of trade talks from major sectors of the US economy. Indeed, the initial American reaction to a new round was cool. For a time, the US seemed content with pursuing only the so-called “built-in agenda” established at the conclusion of the Uruguay Round (requiring negotiations on agriculture and services). It was pressure from the EU, augmented by the increasingly vocal concerns of the US farm sector, that ultimately persuaded Washington that a full round would be desirable.

Apart from the obvious divergence over agriculture, the major US criticism of the EU agenda related to the proposed negotiations on investment and competition policy. On these issues, US concerns were both substantive and tactical.





With respect to investment, the US did not disagree in general with EU objectives. But American negotiators were convinced that a WTO agreement on investment disciplines was politically impossible. The intense opposition to the Multilateral Agreement on Investment (MAI) was seen as evidence that a WTO investment agreement would be a “non-starter”. The fact that the most vocal opposition to the MAI came from core constituencies of the Clinton administration—trade unions and environmentalists—was of particular concern to US negotiators.

On the issue of competition policy, US opposition was substantive. US antitrust law has undergone a revolution over the past quarter-century. It no longer revolves around protecting smaller and weaker competitors from predatory practices of dominant companies. But it is focused almost entirely on the protection of consumer interests and market efficiency. As a consequence, the US has largely abandoned antitrust enforcement against practices such as the abuse of a dominant position by a major company. There is thus acute concern among US competition policy officials that any international agreement on competition rules would necessarily involve a compromise that would “dilute” the hard-won “purity” of current US antitrust principles. It is hard to overestimate the opposition in the US to any such compromise.

The US also objected to these two “new issues”, espoused by the EU and others, because it wanted to avoid topics which would probably extend the round well beyond the desired three-year deadline. The US view—almost certainly correct—is that reaching international consensus on investment and competition policy, if achievable at all, would require a round which would last far longer than three years. To US negotiators, such a delay is unacceptable, especially because it would postpone liberalisation in agriculture. Indeed some US officials have taken the dark view that EU insistence on including these two issues is a deliberate tactic to delay the day of reckoning on agriculture reform.

As the US chaired the Seattle Ministerial, it was the American agenda that took primacy in the discussions. This comprised:

- ★ Accelerated tariff liberalisation in which there would be immediate, significant tariff reductions in eight sectors—chemicals, energy equipment, environmental goods, fish and fishery products, gems



and jewellery, medical equipment, toys and forest products—with the prospect of further negotiations. While significant duty reductions would be implemented immediately, their implementation would be provisional, subject to agreement on the broader WTO round package at the end of three years.

- ★ Services liberalisation: governments would agree some general principles for the regulation of all service industries, regardless of individual sectors.
- ★ Agriculture: the complete elimination of existing export subsidies and the prohibition of such export subsidies in the future; substantial reductions in “blue box” programmes [ie permissible production-related domestic supports]; no renewal of the “peace clause” which has protected farming subsidies from WTO scrutiny; and restrictions on the role of state-owned trading enterprises in the agricultural sector.
- ★ Improvements in the dispute settlement mechanism, particularly greater openness and tighter rules on the implementation of panel decisions.
- ★ Transparency in government procurement.
- ★ Simplification of customs procedures and greater transparency in border procedures.
- ★ Extension beyond 31 December, 1999 of the WTO moratorium on tariffs and other restraints on e-commerce.

As important as the substance of the US-proposed agenda were the tactics for the negotiations. The goal was to isolate the EU on agriculture, then create a dynamic process that would put intense pressure on the EU as the three-year deadline neared.

To this end, the Office of the US Trade Representative engaged in an 18-month intensive effort to assemble a broad coalition in favour of aggressive agriculture liberalisation. Beginning with the 18-nation Cairns Group, Ambassador Barshefsky's team also obtained commitments of

support (in varying degrees) from most members of the Asia Pacific Economic Co-operation (APEC) forum and from many of the African and Latin American states, to press for both a complete elimination of agricultural export subsidies and for substantial reductions in production-related supports and access barriers.

The US strategy aimed at cornering the EU with the “early harvest” concept. Under this scheme, substantial tariff reductions, transparency in government procurement and measures to assist developing countries in complying with their Uruguay Round obligations would be agreed at the outset of the new round and implemented immediately. However, all these benefits would be withdrawn if agreement was not reached on a comprehensive “single undertaking” at the three-year deadline. This elaborate structure was designed to create a scenario in which the EU could ultimately be forced to choose between accepting an aggressive agreement on agriculture liberalisation or being held responsible for both the failure of the round and the termination for all parties of the “early harvest” benefits.

In the end, of course, the Seattle meeting did not adopt either the US agenda or its structure for a new round. In part, this can legitimately be attributed to a lack of negotiation and preparations prior to the meeting, and to the poor presentation of a complex negotiating strategy. However, there were also deep divisions among the major countries on many important issues. The EU would not accept an agriculture negotiation

² See Randy Green ‘The Uruguay Round Agreement on Agriculture, Law and Policy’ in *International Business*, 31, 2000

draft that included a reference to the “elimination” of export subsidies but made no specific mention of the “multi-functionality” of agriculture.² The EU refused even a final draft in which the dread word “elimination” appeared only in the phrase “in the direction of progressive elimination of all forms of export subsidization”. The EU has long argued that its support for the agriculture sector is as much to prevent rural depopulation and even landscape maintenance as to provide food products for urban markets. EU negotiators insisted that this “multifunctional” element should be recognised by the WTO, a view shared by Japan and Korea. Although the final draft did acknowledge the importance of “non-trade concerns” such as food safety for discussions on agriculture, this phrasing proved ultimately insufficient.

Moreover, the US strategy of isolating the EU failed to hold together as developing nations became increasingly disenchanted with what they regarded as a largely closed process. In particular, they felt that leaders from the developed countries—and especially the US President—sought to impose on them unacceptable new disciplines in environmental protection and workers' rights. With no agreement possible on agriculture, and with the "isolate the EU" strategy in disarray, Ambassador Barshefsky had no alternative but to bring the Ministerial to an inconclusive end.

The failure of Seattle, coupled with the fact that the US is now in the midst of a presidential election, has created—at least for the year 2000—a leadership vacuum with respect to a new round. The incumbent US Administration's candidate for the presidency, Vice-President Gore, numbers labour unions and environmentalists among his core constituency. For that reason, and because of his personal convictions, Al Gore would insist that any proposals for a new US round should emphasise worker rights and environmental issues. But the developing nations are reluctant to address these issues. Since the US needs their support for its position (notably on agriculture), it is highly unlikely that the US will take the lead this year in developing a new round agenda, or in organising a new ministerial meeting.

This leadership vacuum poses a major opportunity for the EU. As discussed above, the EU would benefit greatly from a new round, especially if it could craft an agenda suited to its particular needs. However, there are strong reasons to believe that domestic political constraints may inhibit the EU from embarking on this beneficial course.

Ambivalence toward the WTO

In every WTO member-state, negotiations on further trade liberalisation will, to some extent, provoke opposition from domestic constituencies that see their interests threatened. Each member must therefore strike a balance between the benefits of liberalisation for specific sectors—plus the economy in general—and the interests of industries whose domestic markets or subsidies would be negatively affected. In the EU, concern for the latter may make it politically unappealing to take a leading role in the WTO.

Domestic opposition in the EU is in large part a reaction to the radical changes wrought by the last round of multilateral negotiations. The WTO,



created under the Uruguay Round, is different from its predecessor, the General Agreement on Tariffs and Trade (GATT), in three critical ways. First, whereas in many areas the GATT rules were imprecise and largely hortatory, the new WTO disciplines are detailed and specific. A primary example is the WTO agreement on subsidies, which for the first time achieved an agreed international definition of what actually constitutes a “subsidy”.

Second, the WTO rules extend to areas formerly regarded as matters of domestic regulatory practice, when such practices affect trade flows. There are numerous examples: the WTO Agreement on Standards and Phytosanitary (SPS) Measures, the Agreement on Technical Barriers to Trade, the Agreement on Trade-Related Intellectual Property Rights (TRIPS), and the Basic Telecom Agreement. These deal with matters—ranging from food safety and intellectual property to telecommunications regulation—that had previously been considered as domestic rather than international issues.

Third, and perhaps most fundamentally, WTO rules are now truly enforceable. Under the GATT, a country facing an adverse ruling from a GATT arbitration panel could simply block a final decision. At the WTO, by contrast, rulings are binding automatically unless there is a consensus against the decision. While WTO rules are still not enforceable in the sense of domestic court decisions—the WTO has no police force—the new rules greatly increase the likelihood that a country will have to comply with an adverse decision.

This new system has worked to the EU’s benefit in some very significant cases. The EU has been one of the most active users of WTO dispute settlement, responsible for 52 of the 210 complaints brought as of 1 July, 2000, and it has won a substantial number of these cases. For example, the EU has used the new subsidy rules to obtain a ruling that the US Foreign Sales Corporation (FSC) tax legislation provides an illegal export subsidy. Moreover, the EU has obtained a ruling that Indonesian government subsidies to its local automobile industry were hampering EU exports. And the EU has also been able to use the threat of going to the WTO to exert leverage on the US in disputes over the extraterritorial impact of Helms-Burton legislation relating to Cuba and similar legislation regarding Iran and Libya.



And yet, the Europeans sometimes appear unwilling to live by the disciplines agreed to in the Uruguay Round. For example, the EU seems intent on maintaining subsidy programmes that are clearly inconsistent with the tough new disciplines of the Agreement on Subsidies and Countervailing Measures. As noted earlier, some member-states still fund product development through royalty-based “repayable advances”, and the European Commission continues to approve the practice. This form of subsidy has been challenged by the US in a case brought against French assistance to its domestic avionics industry. While this has not yet reached the panel stage, a WTO ruling on a similar case brought by Brazil against Canada in 1999 found that a Canadian programme of this nature was indeed a subsidy. The EU filed third-party submissions, arguing that repayable advances are not subsidies. But the WTO panel rejected those arguments. Despite this ruling, European governments apparently intend to continue providing very significant subsidies of this type.

For the most part, the subsidies that the EU seeks to preserve go either to uneconomic industries (for example, the Italian steel sector) or to companies that are already market leaders, and thus need no state aid (such as Airbus, which has over 50 per cent of the world market). These subsidies to uneconomic industries and market leaders undermine the EU’s ability to speak with credibility to developing countries in the WTO about the benefits of a market-oriented economy.

A similar concern arises in the context of standards. The WTO Agreement on Standards and Phyto-Sanitary (SPS) Measures permits states to take steps to protect human, animal, or plant health. But the SPS agreement requires that, except for provisional measures in instances of scientific uncertainty, those actions should be “based on scientific principles and...not maintained without sufficient scientific evidence”. Furthermore, when a national measure sets a standard that is higher than the protection afforded by international standards, the national standard must be based on a scientific assessment of the risk associated with the product in question. Despite these requirements, agreed under the Uruguay Round, the EU imposes measures based on a “precautionary principle” that would turn the “sound science” approach on its head. The EU has lost the first WTO battle on this issue (the Beef Hormones case), and has refused to comply with the WTO ruling. And while the recently-negotiated Biosafety Protocol embodies a version of the precautionary principle, that Protocol



is not binding on WTO panels. Moreover, it applies only to living modified organisms, not to foods, animal feeds or other products made from genetically-modified foods.

EU member-states are also interfering with trade in GM products in areas not even covered by EU directives. At the beginning of this year, for example, officials of the Dutch government urged feed processors not to use imported feed components made from the 1999 US corn crop on the grounds that much of the corn grown in the US that year was genetically-modified. Whatever view one may have of the merits of the GM issue, one must conclude that both the EU and national governments appear to have little concern for whether their actions on this politically-charged issue are consistent with the EU's WTO obligations.

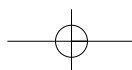
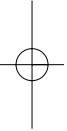
Equally troubling is the EU's willingness to defy the new WTO dispute settlement system. It seems to be standard EU practice to refuse to engage in meaningful consultations at the outset of WTO dispute resolution, despite the express requirement that countries enter into these consultations in good faith. This posture undermines the chances that the process will yield an outcome acceptable to both parties.

Most disturbing is that the EU appears ready to disregard panel decisions whose implementation would force it to confront influential domestic interests. The EU has refused to implement the WTO recommendations in the two most significant rulings against it, the banana regime and beef hormones cases. Regarding the bananas case, Deputy US Trade Representative Rita Hayes recently said that even though the EU's deadline for complying with WTO rules expired more than a year ago, the EU "has provided no indication if, let alone when, it will ever come into compliance." Similarly, Canada and the US obtained a WTO ruling that the EU's exclusion of hormone-treated beef is unjustifiable under WTO rules. However, the EU has quite openly acknowledged that it views non-compliance, and the resulting retaliation by the US and Canada, as preferable to complying with the WTO ruling.

This posture by one of the leading WTO members—rejecting important substantive disciplines to which it agreed in the Uruguay Round, and refusing to comply with decisions of WTO panels—is dangerous for the WTO system. It also seriously undermines the EU's ability to lead a new



round. Other WTO members will be less willing to accept commitments in the upcoming Millennium Round if they perceive the EU as simply rejecting disciplines it does not like. This leaves something of a dilemma. On the one hand, the EU would benefit greatly from a new round. In view of the American political timetable, it has a unique opportunity to take the lead in negotiating the new round agenda. Yet Europe will not be able to reap the rewards if it remains the captive of domestic interests, refusing to negotiate meaningfully on some issues, such as agriculture, and defying the WTO dispute resolution process on others, such as health and safety standards. To resolve this dilemma, it must re-order its priorities.



3 The challenge for the EU: crafting a round agenda

To lead a new round, the EU and its member-states must develop a consensus on an array of issues that is acceptable both to the WTO membership and to important constituencies in Europe. Crucially, its own negotiating position gives it two advantages in this respect.

First, unlike the US, the EU has consistently urged a comprehensive round that covers not only major issues, such as investment rules and competition policy, but also a review of the anti-dumping laws (rules that allow countries to protect their own producers if they believe that products are being “dumped” on their domestic markets at prices below their true value). The EU’s approach thus enjoys greater support among many WTO signatories, including major players such as Japan, India and Mexico, than the narrower round advocated by the US.

Second, the EU has advocated an array of measures that would benefit developing countries, particularly the least developed nations. These include duty-free access for almost all exports and substantial flexibility on the important issue of extending the deadlines for developing countries to implement their Uruguay Round commitments. Many developing countries believe that their interests were largely neglected in the Uruguay Round. Moreover, at Seattle the developing nations loudly voiced their concerns about not being adequately involved in the preparations. Any new round must therefore address the needs of the developing world and the EU is well-placed to help devise an agenda that does this.

Despite these advantages, the EU will have to tread carefully in order to build a consensus within the WTO without its constituent government losing political support at home.



The process for a new round

It was clear from the Seattle maelstrom that many developing nations felt excluded from the real decision-making over the development of the round agenda. This matters, for developing countries now make up the great majority of the WTO's 135-nation membership. There will have to be greater transparency in the deliberations and more influence for the developing countries over the substantive decisions if a new round is to be launched successfully.

For the EU, the problem is essentially organisational, not political. In the past, rounds of multilateral trade negotiations have finally come together when a relatively small group of countries had hammered out a comprehensive set of agreements (involving interlocking concessions among the major nations). These were then submitted as a package to the broader GATT (now WTO) membership. It is not clear that a round can succeed without using such trade-offs among different negotiating sectors (agriculture versus services versus market access, for example). This suggests that this basic dynamic of past rounds should be retained, but that the "inner circle" or "green room" negotiations should be made more transparent to other WTO members, with greater representation for the developing countries.

A related issue is the role of non-governmental organisations (NGOs), especially labour unions and environmental groups, in the negotiating process. This is certainly a political issue, especially for the more progressive administrations in the US and EU. But they should be cautious. The WTO is an organisation of governments, and negotiations are on a government-to-government basis. At present it is up to each government to decide how NGOs should be involved in that country's decision-making process. Most WTO members are unlikely to want the WTO to dictate how they should accommodate the views of NGOs.

Moreover, involving labour and environmental NGOs directly in the negotiations—the "seat at the table" demanded by protestors at Seattle—could seriously undermine the viability of the negotiating process. In addition, it is difficult to see how one would select participants from among the labour and environmental NGOs and the vast array of other civil society groups—farmer organisations, business groups, human rights groups, churches, professional organisations, think-tanks and academics.

Greater public transparency of the round process, for instance by publishing more WTO documents on the internet, would be a preferable approach.

Agriculture

Agriculture is obviously the sector where the EU will have most difficulty accepting an agreement, let alone drawing up a negotiating mandate. This link between a new round and agricultural politics in the EU was acknowledged by UK agriculture minister Nick Brown in a recent address to the Brookings Institution. He agreed that “negotiations in the World Trade Organisation to reform agricultural policies would require a comprehensive approach for the EU to overcome disagreement among member-states”. Yet recently, France and Belgium have blocked an attempt by other EU members to offer a more flexible approach on agriculture. French trade minister François Huwart has stated that: “Flexibility is not the priority of the moment.” The hard fact is, however, that no round agenda will be acceptable to the US, or to most of the developing countries, unless it contains an aggressive mandate on agriculture.

Fortunately, there are several legitimate reasons to think that a sufficiently “aggressive” mandate can be devised which would be acceptable to the EU as a whole. Now that the US “early harvest” tactic appears no longer viable, there is greater scope for a trade-off between the length of the round and the language describing the degree of liberalisation to be negotiated. In other words, in the context of a round expected to last six or eight years, the EU may well be able to agree that the goal for negotiation on export subsidies could contain the term “complete elimination”, or something close thereto.

Moreover, the negotiations on agriculture are not a “one-way street”. The US will also have to be prepared to discuss some of its practices. The EU has already raised America’s use of export credits and of Market Loss Assistance (MLA) emergency payments to farmers. The latter have been repeatedly used at the end of each farm-year, arguably encouraging US farmers to plant more in the expectation that any fall in price will be compensated by MLA payments. Thus, the EU argues, MLA payments distort trade in a similar way to production-related payments. Nick Brown has suggested that the US tends to “spend its way out of trouble”, while the EU maintains a fixed limit on the CAP budget.



Finally, at the end of the Seattle meeting, it seemed the negotiators were close to agreeing a mandate for the agriculture sector of the round. In such negotiations, the art is devising language so that both sides can claim victory. The last Seattle draft used the term “elimination” in the discussion of export subsidies, but did so in the phrase “in the direction of progressive elimination of all forms of export subsidisation”. This would allow EU negotiators to assure their farmers that they had not agreed on actual elimination of export subsidies, but only on movement in that direction. And the EU could stress that references to “all forms of export subsidisation” would mean that US export credits would also be subject to negotiations.

In sum, agriculture issues do not pose an insuperable bar to an EU initiative for a new round. While an ambitious agenda in this sector is clearly a *sine qua non* for gaining consensus on a new round, it appears possible to craft an agenda in a way that is acceptable to EU agricultural interests. The key is for the EU to accept the use of the term “elimination” with respect to export subsidies, albeit qualified by language similar to that used in the last Seattle draft. In addition, the EU should accept negotiations for the possible modification of present rules relating to domestic supports—the so-called “blue box”. It should be possible to do so without language that suggests that the final outcome will be the full elimination of such supports or the complete decoupling of domestic supports from prices and production levels. The US could then accept a number of points important to the EU: an extended timetable (both for reaching round agreement and for implementing agricultural reforms), abandonment of the US “early harvest” tactic, and placing on the agenda the issue of MLA payments.

4 New trade issues

A new EU initiative would presumably look for a “comprehensive round”, advocating WTO agreements on competition policy and on investment rules. But before investing too much capital in trying to incorporate these issues, the EU should weigh carefully the value of such agreements against the difficulties of achieving them.

Competition policy

A negotiation in this area must cope with two major difficulties: the lack of anything approaching a WTO-wide consensus on the substance of competition policy—many WTO members do not even have antitrust laws—and adamant US opposition to anything that might compromise the orientation of current US antitrust law. This suggests that a negotiation on competition policy should focus only on “core practices”, those widely recognised as being anti-competitive, such as cartels, price-fixing and agreements among competitors to allocate markets. In these areas, which are *per se* antitrust violations under US law, it may be possible to achieve sufficient international consensus. But the US is almost certain to block agreement on substantive WTO disciplines covering closed distribution systems or exclusive supply agreements. It will not negotiate on practices which US antitrust law does not condemn, unless they are so restrictive that they cause a “substantial lessening of competition” in the market as a whole. Nor does it seem likely that a global consensus (or even an agreement between the US and Europe) could be reached on substantive criteria for merger analysis. On such issues it may be more productive to use the existing WTO Working Group on Trade and Competition to pursue the process of building consensus that could lead to more substantive negotiations in a future round.

Investment disciplines

In light of the heated opposition to, and subsequent collapse of, the proposed Multilateral Agreement on Investment, any effort to develop investment rules in the WTO is probably doomed to failure. The protests in Seattle showed that the strength of organised opposition to rules on free



trade and investment that might inhibit governments' abilities to protect the environment or the welfare of workers, is stronger than ever. Indeed, there is even more hostility to global rules that limit governments' power to regulate investments than there is to unrestricted trade flows. Again, it would be more sensible to refer the issue to a consensus-building WTO Working Group.

Environmental protection and workers' rights

The Seattle ministerial meeting clearly showed that attempts to address environmental protection and workers' rights could alienate developing countries and make it impossible to reach a consensus for a new round. Yet it is these issues that are of most concern to critics of the WTO, and of globalisation in general—the labour unions and environmentalists, who are core supporters of centre-left governments. Finding the necessary balance on these issues is, together with a deal on agriculture, the key to a new round. The EU has far greater flexibility in this regard than the US. In a presidential election year, the Clinton-Gore administration has little option but to appeal to its core supporters by arguing strongly for meaningful WTO disciplines—perhaps backed by sanctions—on worker rights violations and environmentally damaging practices.

One way to deal with these issues would be to stress that restrictions on trade flows would do little to improve worker rights and protect the environment, and may well be counterproductive. Of course, few in the industrialised world would argue that child labour or environmental devastation are to be condoned. But there is no evidence that restricting imports from countries that tolerate such practices is an effective way of changing the domestic policies of those countries. There are very few success stories in the long history of using trade sanctions to tackle non-trade problems.

A more effective approach may lie outside the WTO, in multilateral or bilateral agreements or via protocols in which countries agree to refrain from pernicious practices and to enact and enforce laws to that effect. If discussions are appropriate in a WTO context, Working Groups and liaisons with other multilateral entities—such as the International Labour Organisation (ILO) and the Biodiversity and Biosafety Protocols—are useful ways of building consensus. The ILO has already been granted observer status at the WTO. The WTO Committee on Trade and

Environment (CTE), established in 1994, has performed a useful role in clarifying issues and identifying potential areas of agreement. For instance, the CTE has provided a forum for discussions of multilateral environmental agreements, subsidies that harm the environment, and the precautionary principle.

The EU should focus its efforts on areas where it can achieve constructive progress. For example, it may be possible to reach agreement on an interpretative statement about the relationship of separate multilateral environmental agreements (MEAs) to the WTO system. If countries have already agreed a particular MEA, this makes it more likely that an accord can be reached on enforcing it through the WTO. Since countries would have reached agreement on the substantive environmental provisions of the MEA, it is more likely that they would be able to accept the use of trade measures to enforce commitments on which there is international consensus. Moreover, it should be possible to reach agreement on standards for “eco-labelling” rules and to promote other environment-friendly trade measures, such as reducing subsidies that harm the environment, and providing greater market access for environmental protection products. It might also be useful to work toward a Code of Good Conduct under WTO auspices, which would set out core environmental or labour principles and oblige countries to consult with other WTO members that objected to one of their national measures.

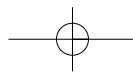
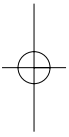
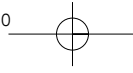
However, a number of thorny issues will remain unresolved. For example, it is not clear whether any MEA exemption would affect the rights of WTO members who are not parties to the MEA. In other words, if a WTO member did not join a particular MEA, could that country still challenge another country’s measure even if that disputed measure had been authorised by the MEA? But these are the types of issues that WTO members may be able to resolve in negotiations that are undertaken in good faith. By directing the debate into such channels, the EU could make a significant contribution, both to launching a new WTO round and to advancing the causes of the environment and workers’ rights.

5 Conclusions

The Millennium Round is in serious trouble and important European interests are thus in jeopardy. European business stands to benefit greatly from further trade liberalisation. The EU also needs this round to help it resolve important internal issues concerning standards and subsidies, and to encourage it to reform its agriculture regime. At such junctures in the past, when multilateral trade negotiations have stalled, the US has often taken the lead in reviving the round. But in this election year, US leadership is unlikely. Moreover, if Vice President Al Gore is elected, the dilemma for the US administration may continue.

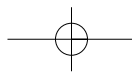
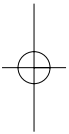
In this vacuum, the EU has a unique opportunity to assume the leadership role and negotiate an ambitious agenda for the new round. But to accomplish this, Europe must take some politically courageous steps. It should be prepared to expand on its Seattle position and offer further compromises over agricultural reform. And on the politically explosive “new issues”, the EU must find ways to vigorously advocate the cause of worker rights and the environment. At the same time, however, the EU needs to stress that using trade sanctions to force changes in other countries’ policies is at best ineffective and at worst counterproductive.

These are undoubtedly difficult challenges. But the rewards of success are great, as are the dangers of failure. In the last analysis, this is an opportunity that the EU must seize.



How the EU can reform the global trading system

Julie Wolf



1 Introduction

The failure by WTO countries last December to agree on a new trade round—and the events surrounding the disastrous Seattle meeting—have been a wake-up call to many politicians and trade experts on both sides of the Atlantic.

The meeting made it clearer than ever that trade liberalisation cannot be dealt with in isolation and behind closed doors. A more open debate on how freer trade should relate to other economic and political goals is to be welcomed. It is clear that growing global economic interdependence raises new issues that can blur traditional distinctions between protectionists and free-traders. Especially in Europe, opposition to free trade no longer comes only from sectoral economic interests and producer lobbies, although these groups certainly have played a role in stoking public fears. Consumers welcome the opportunity to buy cheaper textiles and cars, but reject the idea of genetically modified foods. Trade unions seek to protect domestic jobs but at the same time work with counterparts in the developing world to improve working conditions and access to markets. While such nuances pose a challenge for the political class, they also open the way for the free-trade case to be put in a less simplistic and divisive way.

Pascal Lamy, the EU's trade commissioner, has begun to try and rise to this challenge. He argues that a wide-ranging approach to trade talks is all the more relevant after Seattle. According to Lamy, only a broad round of talks will allow for the kind of trade-offs needed to tackle the issues raised by critics of the WTO in both the developed and developing world. The commissioner also sees such a comprehensive round as a way of channelling the debate about trade liberalisation that Seattle has made so necessary in a productive direction. In addition, Lamy's strategy appears aimed at improving and strengthening the WTO and establishing links between it and other organisations, to allow for a more coherent and democratic system of international economic governance.



This stance is encouraging because it provides a wider political—even philosophical—justification for the Millennium Round, to supplement the traditional argument that comprehensive new talks would be good for the European economy.

At first glance, Europe would seem well placed to pick up the post-Seattle baton. With the notable exception of agriculture, the EU has historically played a constructive role in reducing trade barriers. The opening up of trade between European countries created a dynamic that helped spur international trade liberalisation.

But to pursue a successful post-Seattle strategy, the EU will need to be more cohesive and courageous than it has been in recent years. Not only will European politicians and officials have to turn around public opinion at home, they also will have to convince other countries, especially in the developing world, that the EU is serious about reducing barriers in difficult sectors. The latter is especially important because of the hostility shown in Seattle by many developing countries to the idea of a wide-ranging Millennium Round.

The biggest obstacle on this front is the Common Agricultural Policy (CAP), which despite recent reforms continues to be a major frustration for the EU's trading partners. Another problem involves the internal divisions and the institutional weaknesses that have so often undermined the EU's ability to live up to its ambitions internationally. Improving relations with the US will also be important, although substantial progress may not come until the presidential elections are over. This paper looks at the role played by the EU in setting the stage for Seattle and offers suggestions on where the EU should go from here.

2 The reasons behind the Seattle failure

The popular perception about the Seattle WTO ministerial is that a deal was foiled by the opponents of globalisation, who took to the streets in their thousands. This, of course, is a very partial picture. There is no doubt the demonstrations—and the way they were mishandled by the authorities—embittered an already sour mood in Seattle. But the demonstrators had little direct impact on what was going on in meeting rooms. What they did was symbolise the failure of politicians and trade officials in Europe and the US to heed warning signs that had been apparent for some time.

The most blatant of these was the collapse in 1998 of plans for a Multilateral Agreement on Investment. The MAI negotiations, held under the auspices of the Organisation for Economic Co-operation and Development (OECD), were blocked mainly because of fears raised by NGOs that freer flows of investment would undermine developing countries and add to unemployment in the developed world. Many of these groups went on to oppose new trade talks in Seattle. In Europe, controversy over food safety brought a wider grouping of consumers and environmentalists onto the anti-WTO bandwagon, already occupied by the outspoken farming lobby.

On both sides of the Atlantic, trade matters tend to be handled by a small group of ministers and officials who spend more time talking to each other than to NGOs or even other parts of their own governments. Some free-trade advocates appear to believe that the less outsiders are involved in the process, the better. But Seattle, where a variety of interest groups came together although they had little in common, demonstrated that the case for trade liberalisation needs to be made, not assumed.

The failure of the political class in Europe to read the public mood was only one factor, however. In addition to tensions between developed and



developing countries, a key element was that the EU and US have been on very different wavelengths in recent years. Two noisy transatlantic trade disputes, over bananas and beef hormones—both of which remain unresolved—are symptomatic of the lack of understanding that has built up. In both cases, the US has been quick to accuse the EU of protectionism and disregard for WTO decisions. While there is some truth in these charges, the fundamental reasons for the EU's behaviour in those two cases lie in internal divisions and weaknesses in its system of government, alongside different views on consumer protection.

As other trade differences come along, the importance of the bananas and beef hormone cases are likely to diminish. But both sides will have to work hard to ensure that such arguments do not prevent progress at the WTO. In the US, this will mean more understanding of the political and economic forces behind the EU's actions and less reliance on the nuclear option of trade sanctions. In Europe, efforts must be made to improve decision-making procedures and foster unity among the member-states.

Trouble in Brussels

The successful conclusion of the GATT Uruguay Round in 1994 was a high point for EU trade policy-makers. Despite many difficult moments during the years of negotiations, the EU managed to balance the interests of different member-states and lobbies and still achieve a market-opening agreement with its trading partners.

The accord marked a personal triumph for Sir Leon Brittan (now Lord Brittan), the EU's then trade commissioner. He gained a reputation as a tough, clever negotiator able to defend European interests as well as promote a liberal free-trade agenda. But the extensive nature of the Uruguay Round also sowed seeds of discontent among some politicians and interests groups, especially in countries such as France, where there is traditional hostility to freer trade. The farming lobby was the most vociferous in criticising the agreement. As time went on, farmers were joined by consumers, environmentalists and trade unions who argued ever more forcefully that free-trade rules have to be balanced by other considerations, such as environmental protection and better conditions for workers.

Within the EU, other factors, including political miscalculations and just plain bad luck, also came into play. The most significant trend has been



a weaker Commission. This began under Sir Leon, whose clout with member-states was hurt by the poor relations between John Major's weak and divided Conservative government and the rest of the EU. Moreover, some governments accused Sir Leon and, to a lesser extent, other commissioners of overstepping the negotiating mandates handed down by EU ministers to secure trade agreements with other countries.

That feeling contributed to the rejection by EU leaders meeting in Amsterdam in June 1997 of proposed treaty changes that would have extended the Commission's jurisdiction to more trade areas, such as services. As a result, the Commission and member-states now "share" jurisdiction over trade accords covering sectors other than manufacturing and agriculture, which these days means most trade pacts. This is a prime example of the kind of messy EU procedures that sow confusion internationally and hinder Europe's effectiveness.

Under the EU's constitutional arrangements, when the Commission has jurisdiction (or competence in EU jargon) in trade areas, any agreement it reaches needs to be approved by a weighted majority of member-states, rather than unanimously. In practice, this gives Commission negotiators more room for manoeuvre.

Theoretically, unanimity can be a positive political factor in EU decision-making, ensuring that all countries are committed to trade agreements and that they cannot blame "Brussels" for potentially unpopular decisions. But in practice, unanimity seriously undermines the EU's ability to negotiate by slowing down the process and enabling one member-state to hijack wide-ranging accords over relatively minor issues.

For example, in the EU's long-running trade talks with South Africa, "final" agreements were shot down several times by individual southern European countries, leading trading partners to question the ability of the EU to deliver on its promises. US officials often complain that they are never sure whether the Commission is speaking on the behalf of the EU, although the Clinton administration's inability to obtain fast-track negotiating authority from Congress has prompted similar concerns among Europeans. (Under fast-track, Congress has to vote yes or no on trade pacts in their entirety, instead of being able to reject individual elements of such deals.)



Unfortunately, so far there are few signs that EU countries plan to reverse their Amsterdam decision not to extend the Commission's current powers in trade policy to more sectors. On the contrary, the political trend in Europe is toward curbing the Commission and giving more clout to the European Council and, to a lesser extent, the European Parliament.

Usually, treaty articles such as the one setting jurisdiction for trade matters can only be changed through cumbersome inter-governmental conferences (IGCs), which take several years to complete and ratify. However, in Amsterdam a new paragraph was added to the article governing trade policy (now Article 133) allowing EU governments to extend the Commission's jurisdiction in trade matters without holding another such IGC. This means that EU ministers, acting unanimously, could decide at any time to give the Commission greater powers in trade matters.

It would increase the EU's credibility and facilitate future trade negotiations if EU governments took advantage of this treaty provision. Such a move would not be a big sacrifice for the member-states, given that trade agreements would still need a qualified (or weighted) majority of votes to be adopted by ministers.

Another institutional difficulty for the EU in concluding international trade agreements is that responsibilities are split among different ministers. Although foreign ministers and EU heads of government have the ultimate say when it comes to endorsing a WTO accord, their counterparts in ministries ranging from agriculture, to the environment to transport need to sign off on any resulting changes needed in EU legislation. These ministers are increasingly mistrustful of the Commission and keen to become more directly involved in international trade talks. Sometimes they attend trade meetings as part of national delegations. In Seattle, for example, Pascal Lamy enraged some EU environment ministers when he agreed to the creation of a working group on biotechnology without consulting them.

It is obviously not in anybody's interest for the Commission to offer compromises only to withdraw them later because of opposition from governments. But equally it causes immense frustration among the EU's negotiating partners when it is not clear which ministers are in charge during international trade talks. To cope with this problem, the EU should



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consider ways of improving co-ordination between the Commission and specialist ministers.

One way would involve the creation of an inter-ministerial group to maintain contact with the Commission before, during and after global trade talks. This would allow ministers handling different sectors to consult with each other at EU level, as well as working with the Commission. To prevent such a body from becoming unwieldy, it would be best to limit the number of member-states involved at any one time. Given that EU countries are notoriously reluctant to be excluded, there should be a balance between the countries that tend to support freer trade, such as Britain and the Scandinavians, and the more cautious southern European member-states. Another way to counter complaints about lack of representation would be to rotate membership among EU countries.

Banana fiasco

While the debate over voting rules has exposed tensions between the Commission and member-states, wider divisions among EU governments, between governments and the European Parliament, and sometimes even within national administrations, can also cause confusion in the way the EU copes with trade issues.

Such differences were a key reason for the EU's poor handling of a trade case brought by the US against Europe's rules on banana imports. To understand the banana case, it is necessary to look at the origins of the EU's complex banana regime, which was cobbled together in the early 1990s with the creation of the single market. Before then, countries such as Germany had an open market in bananas, while others, such as France and Britain, restricted imports of Latin American bananas in favour of those from former colonies in Africa and the Caribbean. To bridge the gap, the EU came up with a complex system of tariffs and quotas that benefited so-called ACP (Africa, Caribbean and Pacific) bananas, as well as European banana importing companies and the few existing European producers.

The restrictions were highly unpopular in some EU member-states, especially Germany, which was only too happy when in September 1997 the WTO sided with the US and several Central American



countries judging that the EU was breaking international trade rules. By this time, Germany enjoyed the backing of the new Nordic member-states, and the EU was split almost evenly over bananas. As a result, it took the EU until January 1999 to make modest changes to the rules, which were rejected as insufficient by the US. That set the stage for months of extraordinarily bad-tempered exchanges between the EU and US, with the Americans eventually slapping annual sanctions worth nearly \$200 million on EU exports. Both Europeans and Americans allowed the rhetoric to spiral out of proportion to the actual problem. Neither is a major producer of bananas, although Chiquita Brands International has strong support within the US administration and Congress, which contributed to the hard line adopted by the US administration.

In the EU's case, clumsy handling of the banana issue was mainly due to the near paralysis among member-states, which only managed to agree on changes to the regime as part of a wider farm package. But there was also sloppy legal work by the Commission, while Sir Leon appeared to relish last year's confrontation with the US over who was undermining the WTO most.

The kind of procedural wrangling that the EU and US engaged in at the WTO during the bananas case harmed the WTO and transatlantic relations. But it is overly simplistic—and not particularly helpful—to say, as do many Americans, that the EU deliberately set out to thwart a WTO ruling. Moreover, in a more recent trade dispute, the shoe is on the other foot with the EU rejecting as inadequate the US response to the WTO judgement against the Foreign Sales Corporations (FSC) scheme.

Food fight

Another big EU-US dispute, over Europe's ban on meat imports treated with growth-promoting hormones, is of wider political significance than the banana row. That is because the hormones issue—and the separate problem of genetically modified crops—have become focal points for critics of the WTO and of globalisation. Their contention, that countries should have the right to restrict trade to protect their consumers and the environment, has a wide resonance with European public opinion, especially in light of recent food safety scandals.



To a certain extent, the disagreements over hormones and GM foods highlight differences in European and American attitudes toward food and public institutions charged with protecting health. If it is possible to generalise about eating habits, Americans tend to be happier about mass-produced cheap food than many Europeans, especially those in France and southern European countries. Europeans are used to a wealth of local and regional specialities, which coexist alongside industrialised food production. This reverence for “traditional” foods combines with a more hesitant European view of technological change and a somewhat romantic attachment to country life to make EU consumers wary of new food production methods.

There is also a growing gap between how the US and the EU are choosing to respond to risks involving food and other products. The EU is developing the idea of a “precautionary” principle which should allow foods and goods to be banned on safety grounds, even if scientific evidence is uncertain or inconclusive. The US, on the other hand, argues that there should be evidence that items are unsafe before they are withdrawn from the market.

These kinds of cultural attitudes, however, are only part of the story. The EU’s lengthy legislative process, involving the European Parliament and member-states with different regulatory regimes and eating habits, has meant that food laws have not always kept pace with the single market. It can take years for the EU to agree on what constitutes chocolate or on how “novel” food should be labelled. Meanwhile, food circulates freely and consumers become more and more worried about what they are eating.

Moreover, the EU has a complex approval process for foods, involving committees made up of national representatives and the Commission, that are subject to a variety of voting procedures. In at least one case, genetically modified maize, the voting rules for such committees obliged the “unelected” Commission to approve a product despite lack of support from member-states. The controversy that surrounded this case was a key factor in the EU’s decision to revise its legislation on the approval of GM products. The whole committee system (known in EU jargon as comitology) was altered in the Amsterdam Treaty to make it more democratic—yet the public perception remains one of bureaucrats in Brussels deciding behind closed doors what we eat.



The Commission's recent proposals for a European Food Agency should go some way towards the creation of a more open process that can inspire public trust, although it is unfortunate that the Commission was not bold enough to call for a truly independent body with decision-making powers. This reflected the reluctance of national governments to relinquish political control over food safety. In parallel to the development of a new EU institution, member-states are increasingly setting up their own, national food standards agencies. While these can help to improve public confidence, there is the potential for conflict between different agencies. The French government, for example, has cited the opinion of its food safety panel in refusing to lift the ban on British beef, in defiance of the Commission.

As a result of these problems, the EU has often found itself scrambling to react to food problems, which can result in flawed rules. The hormone ban was one such instance. It took effect in 1989 after a series of health scandals earlier in the 1980s, including the discovery of hormones in baby food in Italy. The Commission had originally sought less far-reaching legislation, but changed tack under pressure from the European Parliament and EU governments. They persuaded the Commission that a partial ban affecting only hormones known to be dangerous would be publicly unacceptable and would also be hard to administer throughout the EU.

One thing the measure was not aimed at specifically was American meat, which represented only a small part of the EU market. At the time, it might have seemed to some EU officials, who knew of the lack of scientific evidence, that the ban could be changed if it was found illegal internationally. In retrospect, it might have been better for the EU to opt for a labelling regime, although it is not clear the US would have gone along with that either.

Any chance for a labelling solution came to end, however, with the crisis over mad-cow disease, or bovine spongiform encephalopathy (BSE), which broke out in the mid-1990s and complicated further the EU's handling of food issues. BSE left many Europeans distrustful of scientists and governments, who had assured the public for years that the illness in cows posed no threat to humans, only to reverse their position suddenly. This provoked surprise and outrage among consumers throughout the EU, many of whom boycotted beef, causing a collapse in the beef market.



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After BSE, the EU was in a “lose-lose” situation on the hormone ban, which was ruled illegal by the WTO on the grounds that the EU had failed to provide adequate scientific justification. Politically, the EU could not lift the ban because, as a French official said last year, “what politician is going to tell voters that they have to eat meat with hormones in it”.

BSE, and the more recent scandal in Belgium over high levels of dioxins in poultry and meat, have also forced a choice between free trade (within the EU) and food safety. (In both the BSE and dioxin crises, the EU slapped export bans on British and Belgian products.) This is now being transferred to the world stage, with the potential for another big EU-US food row, over GM crops.

After much confusion and debate over how to handle GM foods, the EU appears to be opting for using labels to allow consumers to choose what they eat. But if exports of GM crops from the US and elsewhere are not kept separate from traditional varieties, it is difficult for labelling in the EU to be of any use to consumers. After all, a label that says a product “may contain” GM products does not tell people much. The official US government position is that keeping GM crops apart from traditional varieties is expensive and unnecessary, because the products are perfectly safe.

Nonetheless, the two sides appear to be trying to avoid a confrontation on this issue, which dwarfs bananas and hormone-treated meat in terms of trade importance. Both the EU and US backed a global treaty on biosafety in Montreal in January 2000, which allows countries to block imports of GM crops in some circumstances. The treaty also requires that shipments of GM crops be labelled. But it does not deal with how to label consumer products made with such crops, which is the focus of most controversy in Europe.

There are several other developments that could help to reduce trade friction on GM foods. One is the decision by some US producers and grain exporters to keep GM crops separate, to maintain their access to the European market. Moreover, the Clinton administration has responded to concerns among US consumers by tightening regulatory controls over GM foods. There are also signs that the idea of labelling foods is catching on in the US itself. Despite the difficulty and expense of segregating GM crops, it seems that labelling is the best way forward. Consumers should



be given the choice and over time, they may well opt for GM products, especially if these are cheaper.

Leadership crisis

It is easier to understand the EU's trade difficulties over food issues than the mess the Union got itself into last year over the choice of a director-general to succeed Renato Ruggiero at the WTO. The lengthy process, which resulted in a compromise calling for New Zealand's Michael Moore and Thailand's Supachai Panitchpakdi to share a six-year term, delayed preparations for Seattle and soured relations between developed and developing countries.

While it is not certain that a unified EU position would have broken the deadlock among WTO members, who take decisions by consensus, it would almost certainly have shortened the process, increased the EU's standing in Geneva and made things less murky. As it was, the EU started off split between the four original candidates and ended up divided over whether Moore or Supachai should get the job. Stories circulated about at least one EU country trading its vote to obtain a deputy director-general post. The divided EU won kudos neither with those Asian countries backing Supachai nor with the US, which supported Moore.

For its part, the Commission appeared to make little effort to forge an agreement among EU countries, leading to speculation among some Geneva diplomats that Sir Leon wanted the job for himself. While this was highly unlikely, Sir Leon's political skills were not much in evidence during the saga. At one point he convinced foreign ministers, who had not themselves been handling the discussions, to back Supachai, only to see the decision reversed several days later.

Many trade diplomats argue that a united EU is crucial for the effective functioning of the WTO, even if there are the inevitable trade spats with the US. "It is when they sit on their hands that there is a real problem", says one trade diplomat.

3 After Seattle

In contrast to their differences over the choice of a new director-general for the WTO, EU countries managed to remain remarkably united over trade policy in the months leading up to the Seattle meeting, and even during the ministerial itself. It was not always clear that this would be the case. When Sir Leon first floated the idea of a “Millennium Round” to extend the Uruguay Round’s trade liberalisation, there was only moderate enthusiasm among European governments. France, in particular, was sceptical, arguing that the world still needed to digest the changes brought by the Uruguay Round.

Gradually, however, support for the idea grew, with European business leaders playing an important role in arguing for more ambitious market opening, especially in areas such as services and investment. The key factor to sway France and southern European countries was the knowledge that the EU in any event would have to engage in global talks to reduce trade-distorting farm subsidies. Under the Uruguay Round accords, participants had agreed to tackle “unfinished business” with new negotiations on agriculture and services at the turn of the century. If the EU was going to be called on to make concessions on agriculture, it might as well get something in return in other sectors, the argument went.

But the EU’s stance has its drawbacks. Outside the EU, there is suspicion that Europe’s call for a comprehensive trade round is actually designed to delay for years progress toward more open agricultural trade. And within the EU, the EU’s strategy leaves the door open for critics of the WTO to blame globalisation for undermining farmers. This situation sets a double challenge for the EU of satisfying critics both at home and abroad.

The Millennium Round—pros and cons

As mentioned above, the initial impetus in the EU for a Millennium Round came from Sir Leon and the business sector, with support following from those who sought to widen the scheduled talks on agriculture to encompass other issues. The economic benefits to the EU of such an



approach are fairly clear: European companies would gain from a lowering of barriers elsewhere in the world, especially in sectors such as investment and services. With the exception of textiles and agriculture, most European industries have more to win abroad than to lose at home from further trade liberalisation.

The picture is less clear-cut, however, when it comes to the inclusion of new issues, such as competition, the environment and labour standards, in the next WTO round. European companies tend to fear that raising these controversial issues will prevent or delay completion of a new round, even though they might benefit from clearer rules elsewhere in the world, especially in the area of anti-trust policy.

It is on the wider political and social front where justifying a comprehensive Millennium Round becomes more tricky. In the past, many free-trade advocates in Europe, including Sir Leon, have not focused enough on this. The tendency has been to believe that once the bulk of the business community was won over, the rest of the general public would follow, especially if it could be wooed by the discussion of labour standards and the environment in the next trade round.

Even before Seattle, this was a mistake, because it contributed to the perception of trade liberalisation as a “right-wing” objective, aimed at benefiting companies, especially multinationals, at the expense of others. That perception has been compounded by the unwillingness of some free-trade supporters to admit that there can be a down-side to the current world trading system and its further liberalisation. Waving aside job losses in Europe or unpopular WTO rulings as inevitable but relatively unimportant is no way to sell a new trade round to the public.

Seattle illustrated with a vengeance the need to ensure that a wider section of European society is brought on board to support a comprehensive trade round. It is certainly possible to make the case for the EU’s proposed Millennium Round from a social democratic or centre-left political perspective. Europe’s own experience has shown that trade liberalisation, in the form of the single market, can be accompanied by legislation aimed at protecting workers rights and the environment. Moreover, it can be argued that putting subjects such as the environment and labour standards on the table opens the way for the



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WTO talks to cover issues other than the traditional lowering of trade barriers.

Enter Pascal Lamy, who took over from Sir Leon as EU trade commissioner in Autumn 1999. His appointment broke the recent tradition of placing centre-right politicians in the EU trade job. Though not a professional politician, Lamy was nominated by a French Socialist government as his country's "senior" commissioner. A high-flying French civil servant, Lamy came to the Commission from France's *Crédit Lyonnais*, where he helped to clean up the troubled bank's finances. His main experience of European affairs was a lengthy stint as top aide (*chef de cabinet*) to Jacques Delors, the French Socialist who as Commission president from 1985-95 played a pivotal role in the establishment of the single market and single currency.

It is too early to tell how Lamy will fare in the trade post. His lack of experience in elected office may make it harder for him to connect with the public and cut deals with EU ministers, who tend to respect ministerial experience. On the other hand, Lamy's background and nationality make him sensitive to the need to respond to European critics of a new trade round by focusing on the political as well as economic issues at stake. "The round provides a rare opportunity for a much-needed democratic debate on globalisation, its consequences and conditions. While the necessity of this debate was not so clear before Seattle, it is afterwards," Lamy said in a recent interview with this writer.

The debate on [trade] liberalisation poses the question of what takes precedence—trade or environmental laws, trade opening or consumer protection, intellectual property rights or the health of people in the developing world. These subjects have to be dealt with. If we miss out on this debate, we will see the slow growth in our societies of forces that will oppose the opening of markets, because of simplistic but politically efficient scape-goating.

Lamy also contends that further trade liberalisation can only be achieved through a wide-ranging round, rather than talks on a limited number of sectors, as some members of the US administration have suggested. "There is no other way to achieve the type of north-north and north-south trade-



offs that are needed to make progress in the liberalisation of trade. We do not have any other option,” he said.

While he is probably right, especially given the resistance from some EU countries to agricultural reform on its own, the notion of “trade-offs” has disadvantages. The idea of a wide-ranging round has been deeply resented by outside critics of European farm policies, especially in the agricultural exporting nations known as the Cairns group, who are fearful that it is a tactic for delaying painful agricultural reform.

Needless to say, such charges are vehemently denied by European officials. They argue that the EU wants and needs to overhaul its farm policies, to reduce the amount spent on subsidies and to prepare for the entry of countries from central and eastern Europe. These officials also point to the EU’s call for the Millennium Round to be concluded within three years, a relatively short period for such negotiations.

Given the many different strands of opinion within the EU, no doubt some staunch defenders of the Common Agricultural Policy (CAP) backed the concept of a new trade round in an effort to head off farm reform. But there is no evidence that this is the view of the policy-making establishment in EU governments and the Commission. On the contrary, some of the strongest proponents of agricultural reform see another comprehensive trade round as a way to force through change in agriculture. These officials and politicians believe that an alliance of other interest groups is needed if the EU’s powerful farm lobby is to be over-ruled.

It is clear that selling CAP reform will be easier as part of a wide-ranging global trade deal, especially if this addresses other issues that European citizens care about, such as the environment. But apart from the trouble it causes with EU critics abroad, there are domestic political problems with this strategy, particularly because it prevents the kind of public debate on European agricultural policies that the EU so desperately needs. It would be better if politicians tackled head-on the issues involved in farm policy, instead of insinuating that European farmers should suffer so that other sectors of the economy—including “rich” bankers—can benefit.

It is also unclear whether the EU is capable of maintaining a unified front during a complex trade round covering such a wide range of issues. It is



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one thing to put together an eight-page position paper ahead of Seattle that has something for everybody, but quite another to follow through during global negotiations. A glance at the one issue that EU countries had the most trouble agreeing on ahead of Seattle shows some of the underlying tensions over trade in the EU.

Labour standards dilemma

One problem the WTO had in preparing for Seattle was that the EU's own negotiating stance was endorsed only weeks before the ministerial meeting. The delay was mainly due to the resignation in March 1999 of the Commission led by Jacques Santer. But it also reflected difficulties in resolving a major substantive disagreement among EU governments ahead of Seattle, which involved the sensitive issue of labour standards.

The EU has been split for years over whether there should be any discussion of labour and human rights issues within the General Agreement on Tariffs and Trade (GATT) and its successor, the WTO. Countries such as France and Belgium argue that the EU should use all means possible to promote core labour standards, which are usually defined as the right to join a trade union and the elimination of forced labour, child labour and discrimination in employment. But others, led by the UK and the Netherlands, are traditionally sceptical about linking labour issues to the WTO, for fear that this could result in protectionism.

The dispute reflects different philosophies over trade liberalisation, with "purists" in the UK and the Netherlands contending that the WTO is not the place for discussing labour and human rights. But there has also been the practical question of whether it is worth alienating developing country governments, many of which are deeply hostile to widening the WTO's remit to include labour and environmental standards.

The EU itself has already established a link between human rights and trade in its scheme of trade concessions for developing countries, known as the Generalised System of Preferences, or GSP. A clause introduced in the mid-1990s into the GSP gives the EU the right to withdraw favourable trade conditions, such as low tariffs, to a developing country that allows the use of forced labour. So far, the only country to have its concessions suspended is Burma (Myanmar), where the use of forced labour is well



documented. Although the EU has considered acting against Pakistan, so far it has not done so.

Given the stance of many developing countries, even those EU member-states that want to put labour standards on the WTO's agenda have been cautious about suggesting that measures similar to the GSP human rights clause be adopted at an international level. Instead, the EU's internal debate has focused on whether and how the issue should be dealt with at the WTO. The compromise that officials and ministers arrived at in October 1999 after several months of haggling called for closer links between the WTO and the International Labour Organisation (ILO), the Geneva-based United Nations body responsible for setting and supervising international labour standards.

It was a sign of how sensitive the issue is, even within the EU, that the compromise adopted by EU ministers ahead of Seattle was vague. Its only concrete proposal was the creation of an ILO-WTO "standing, working forum on trade, globalisation and labour issues." The EU was not very clear on the forum's mission, with the ministers saying that it would aim "to promote a better understanding of the issues involved through a substantive dialogue between all interested parties (including governments, employers, trade unions and other relevant international organisations)".

This formal EU ministerial position also "confirmed the EU's opposition to any sanctions-based approaches". Internationally, this stance put Europe mid-way between the US, which demanded that labour standards be put firmly on the WTO agenda, and the developing countries, which wanted no mention of the subject at all. The vagueness of the EU stance caused some confusion, with delegates in Geneva asking what exactly an ILO-WTO working party would mean. But that very lack of clarity now gives the EU the chance to play the role of mediator between the two opposing sides.

That opportunity has grown after the US's mishandling of the labour question in Seattle. While American officials at the ministerial meeting were telling their counterparts from developing countries that the US was not pressing for sanctions to be imposed on countries that do not meet basic labour standards, President Bill Clinton, speaking elsewhere, called for just that. For some developing countries, already angry with the way



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the Seattle meeting was going, President Clinton's comments were the last straw.

This controversy, along with the uncertainty over whether the next US administration will pursue labour standards, means the issue could well end up on the back burner in the short term. But it certainly will not go away, given concerns among trade unions, NGOs and the wider public about the impact of globalisation on the less well-off in both industrialised and developing countries. If the EU maintains its opposition to a sanctions-based approach—too open to protectionism and difficult to enforce—it may be able to play the peace-maker in future WTO negotiations, helping to dispel some of the fears about globalisation.

Whether the EU can succeed on this front is contingent on EU countries remaining united while at the same time fleshing out their idea of an ILO-WTO forum. Although it may be useful to avoid too many specifics at the start of negotiations, in the medium run more details will be needed to provide credibility and reassure doubters on both sides.

The positive element in the EU's proposal is its recognition of the need for a more coherent approach to regulating international economic relations. Trade liberalisation should be part of a wider effort to improve the living standards of people throughout the world, which includes eliminating practices such as child labour and forced labour. Given that virtually all WTO countries are also ILO members, closer links between the two bodies would put pressure on ILO countries to enforce the core labour standards that they have signed up to. But the danger with the EU's stance is that it could turn out to be a half-way house, satisfying neither the developing countries, nor critics of globalisation in the developed world, and leaving the EU split.

Lamy's game-plan

In recent speeches and interviews, Pascal Lamy has outlined his game-plan for putting the WTO trade talks back on course. He has argued that the world does not have to wait until after the US elections to agree on launching a new round, a view that is not shared by many others, including this author.



Specifically, Lamy proposes a series of steps aimed at re-establishing confidence in the WTO and the world trading system, with special emphasis on the concerns of developing countries and the wider public in the developed world, sometimes referred to as “civil society”. Regarding developing countries, the commissioner suggests: rapid agreement on the elimination of tariffs and quotas on exports from the world’s least developed nations; open-minded discussions about requests by developing countries for more time to implement commitments made under the Uruguay Round; and improvements in the way WTO ministerial meetings are organised and run to provide an enhanced role for the developing world.

In response to the widespread view among NGOs and non-business interest groups that the WTO process is remote and secretive, Lamy calls for efforts to make the system more inclusive. According to the commissioner, this could be done by accrediting NGOs to the WTO in Geneva, holding public meetings of the WTO to discuss the organisation, and creating new links between the WTO and parliamentarians in member countries, perhaps through an annual meeting of MPs.

These suggestions are a good start and mark a welcome effort to learn from the problems that came to the fore in Seattle. Some trade diplomats believe the EU is currently in a better position than the US to push through changes in the WTO, because of the view among many WTO members that Washington put domestic political considerations ahead of securing a trade deal in Seattle. America’s economic and military might can also lead other WTO countries to bridle at proposals from Washington, regardless of their merit. This was a factor in the opposition to Mike Moore, who became viewed as America’s candidate to head the WTO even though he had no particular links with the US.

At any rate, the EU has made some of its own efforts at change. It included for the first time members of NGOs—as observers in its delegation to Seattle—and has helped to sponsor seminars in Geneva to familiarise outsiders with the WTO. The EU has been both more active and realistic than the US about what can be done to improve the way the WTO works.

However, there is plenty of scope for Lamy’s ideas to be developed further. For example, WTO member countries are notoriously restrictive and



sensitive about the publication of documents—as well as the provision of on-the-record comments—by the organisation’s secretariat. Within its own structures, the EU itself is traditionally reluctant to make documents available to the wider public, leading to accusations that it is overly secretive. Given that similar charges are now being levelled against the WTO, the EU would gain credit by pushing for more openness in Geneva. In particular, the Commission should press member-states to agree to immediately publish the documents related to panel decisions on the internet.

And although it may not be technically or politically feasible to make fully public the WTO’s procedures for settling disputes, ways should be found for outside parties with relevant information to be allowed to make submissions to the experts who decide the cases. Some trade officials fear that this would drown the WTO’s dispute panels, which already have to cope with thousands of pages of submissions. But the solution is to set criteria to ensure that outside briefs are of real use to the panels, not shut out bodies such as environmental lobbies.

Lamy and national politicians also need to work on convincing the public of the benefits of an open trading system. It is crucial that they avoid blaming the WTO for EU policy reforms that are necessary, especially in agriculture (which will be discussed in more depth in the next chapter). Strategies should also be developed to counter the arguments of lobby groups seeking to maintain subsidies or protection for their own sectors. For example, there are environmental benefits in reducing subsidies to big industrial farmers and to the fishing sector. It should therefore be possible to enlist the support of groups such as Friends of the Earth and Greenpeace for measures that result in a less polluted countryside and more fish in the sea.

While Lamy understands the need to get the backing of sceptical developing countries for a new trade round, the EU would have a greater chance of succeeding on this front if it addressed more concerns about the openness of the European market. For example, the plan endorsed by the EU to eliminate barriers on imports from the least developed countries still excludes highly sensitive products, including some agricultural goods. As a result, it has met with a muted response. Developing countries also are keen to see lower barriers to textile exports and much tighter controls on

the use of anti-dumping measures, viewed by many as authorised protectionism. Unlike the US, the EU is willing to discuss anti-dumping, but it should be more specific on this.

The more the EU shows its hand ahead of a new trade round, the more chance it has of convincing wary trading partners it is worth their while to go along with such a round. A show of willingness to take in more exports from developing countries would also help to counter criticism from the US, which with its massive trade deficit does much to stimulate the world economy.

What about agriculture?

The biggest test of the EU's commitment to a new world trade round will be its handling of the so-called built-in agenda. This left-over from the Uruguay Round calls for negotiations to reduce barriers to trade in agriculture and services, two areas where GATT members agreed that the Uruguay Round did not go far enough. So far, Lamy has said that efforts to restore confidence in the world trading system should run in parallel with the talks on agriculture and services. The services negotiations do not pose big problems for the EU, which will have to make relatively minor concessions to secure open markets in other parts of the world.

That is not the case with agriculture, where the EU is under heavy pressure for concessions. Lamy told this writer he would be "very surprised" to see the built-in agenda wrapped up without a new trade round.

On agriculture, I have serious doubts. The type of concessions that we're prepared to make on agriculture, we're not going to make without getting something in exchange on the new areas such as environment, health and core labour standards, because otherwise there would not be any pressure to treat these issues.

It may not be politically feasible for the EU to sign up to a final WTO agreement on reducing farm subsidies without a wider trade round, but other trading partners will be looking for proof that it is negotiating seriously on agriculture. This means showing flexibility and contemplating the kind of changes to the CAP that so far have not been on the cards.

4 The EU's agricultural problem

It is impossible to underestimate the damage done to the EU's image with its trading partners by the Common Agricultural Policy. This complex system of subsidies was set up in the 1960s with the then understandable goal of making Europe as self-sufficient as possible in food. Unfortunately it was overly successful, producing the notorious food mountains that eventually had to be dumped on world markets at great cost to European taxpayers and food producers elsewhere in the world. The prospect of ever-growing CAP expenditure, combined with intense pressure from the US and other agricultural exporters, led the EU to accept the need for changes in its agricultural policies. These began with the so-called MacSharry reforms in 1992 and were followed by last year's Agenda 2000 agreement.

In parallel, the 1994 Uruguay Round accords established the first comprehensive international rules on agricultural trade and subsidies, under which Europe and other signatories agreed to scale back export subsidies. These payments have been used by the EU to make up the difference between the high internal prices set under the CAP and lower world commodity prices. By allowing the EU to shed its overproduction and gain markets it otherwise would not be competitive in, they have distorted trade and put a downward pressure on world prices. With its combination of high guaranteed domestic prices, export subsidies and barriers to imports, the EU had by the 1980s gained an international reputation as highly protectionist when it came to agriculture. This image persists despite the MacSharry reforms. The view among other WTO members, especially the US and the countries of the Cairns Group, is that the EU has to be dragged kicking and screaming into further liberalisation of farm trade.

The EU, for its part, made considerable efforts to dispel such views during the Seattle ministerial. According to participants, when the meeting collapsed the agricultural group was tantalisingly close to agreement on a far-reaching mandate for talks on liberalising farm trade. "It was not



agriculture that blocked a deal in Seattle,” says one trade official. But the EU’s problem is that despite all the promises of the early 1990s, the CAP reforms undertaken so far have failed to dent EU spending on farm subsidies, and only partially succeeded in reining in overproduction. There are several reasons for this.

Partial reforms

The fundamental change introduced under MacSharry was a shift away from high guaranteed prices toward direct income payments to farmers. This was done because the CAP’s price supports not only encouraged overproduction but also concentrated subsidies on the 20 per cent of farmers responsible for 80 per cent of food production. As a result, the CAP was not fulfilling a central EU policy goal of maintaining rural incomes throughout the European countryside. Moreover, it wasted money on some large-scale farmers, such as cereal producers in northern France and southern England, who were competitive enough to sell on world markets without subsidies. And by rewarding intensive farming, the CAP encouraged the use of pesticides, fertilisers and other environmental pollutants.

However, the strong resistance to change among the EU agricultural lobby—particularly the large farmers who wield the most clout in national farm organisations—meant the MacSharry reforms were not as sweeping as they might have been. The most far-reaching changes, including mechanisms to cut production, focused on a limited number of crops, such as cereals and oilseeds. The beef sector, which was later hit by the BSE crisis, was only partially overhauled and other areas remained unchanged. So while the reforms marked a fundamental departure in the way the CAP was run, their relatively narrow product coverage meant that soon after their adoption, people began talking about the need to extend the method to other sectors.

The other disappointing aspect of the CAP overhaul involved the method used to replace the price supports. Instead of getting a guaranteed price, farmers began receiving “compensatory payments” to make up for the price cuts. In theory, these were a form of income support that would not encourage production and would be spread more evenly across the farming community. But because the payments were partially linked to the amount previously produced, large-scale farms continued to draw the bulk of EU subsidies. Such farms are also in the best position to invest in



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increasing productivity. So although the EU's system of direct payments is not as market-distorting as high guaranteed prices, it still has the capacity to create overproduction. Moreover, given that world prices for cereals rose in years after the reforms took effect, farmers were compensated for price cuts that did not actually happen.

The Commission's own report on the operation of the compensatory payments tells the story. "It can be estimated that 11 per cent of the aids in 1993-4, 42 per cent in 1995-6 and 21 per cent in 1996 were over-compensation," the report said. The total paid in the period for price cuts that did not take place was €8.5 billion, according to the Commission's calculations. Although the 1992 reforms succeeded in reducing spending on export subsidies for crops such as cereals, that decline was more than made up for by the direct payments. The direct aids to farmers were a key factor in the growth of the EU's farm budget to an estimated €41 billion in 1999, up from €34 billion in 1993.

Despite its historical advocacy of farm reform, the UK played an important role in ensuring that the CAP continued as a costly mechanism for funding production. Along with the Netherlands, the UK fought hard to protect the interests of its large-scale "efficient" farmers when the MacSharry reforms were negotiated. So while the Conservatives then in power in Britain repeatedly attacked EU spending as excessive, they bore considerable responsibility for the continued high cost of the CAP. The current Labour administration has also defended big producers from bearing a larger share of subsidy cuts, although it has been willing to see across-the-board reductions in direct payments.

The compensatory payments had initially been considered a transitional measure, but they were not phased out or substantially altered in last year's Agenda 2000 agreement, which established the EU's budgetary framework until 2006. EU governments were divided over the Commission's call for so-called degressivity, which would have gradually reduced aids to the biggest producers, as well as the idea of "co-financing", or sharing the cost of direct payments between the EU and national budgets. As a result, neither idea made it into the final Agenda 2000 deal.

The Agenda 2000 accord, reached by EU leaders at their Berlin summit in March 1999, does deepen and extend to more sectors the price cuts of



the MacSharry reforms. But because EU governments decided to delay the introduction of some reforms, the changes are unlikely to satisfy trading partners and may not even keep farm spending within the limits set by the EU leaders.

Curbing export subsidies

The most successful aspect of the farm reforms has been a reduction in the EU's reliance on export subsidies. However, market conditions mean this trend may not continue. In the years after the MacSharry reforms took effect, world prices for commodities such as cereals rose, allowing the EU to cut back export subsidies, as required under the Uruguay Round accords. But a variety of factors, including the economic crises in Asia and Russia, have led to a big drop in world prices in the past two to three years.

The Organisation for Economic Co-operation and Development's Agricultural Outlook 1999-2004, published in 1999, highlights the problem this poses for the EU. Because of lower-than-anticipated world prices for cereals, the EU is likely to continue needing export subsidies in the next few years. As a result, "the internationally agreed restrictions on them [export subsidies] will limit EU exports and so likely lead to stock accumulation in particular years," the OECD report says.

A return to big EU agricultural surpluses that need to be stockpiled would be bad news for at least two reasons. They would put extra pressure on the EU's budget and dent hopes among agricultural exporting countries for an upturn in international commodity prices. The prospect of such a scenario means that the EU's trading partners are certain to press for further CAP reforms to prevent overproduction. The EU also will come under international pressure to reduce the direct income payments to farmers, which were not subject to restrictions under the Uruguay Round accords and are set to increase under Agenda 2000.

Many experts in agricultural policies also believe the Agenda 2000 agreement is not radical enough to meet its stated aim of preparing the EU for enlargement to include Central and Eastern Europe. During their accession negotiations, the applicants are pressing for full access to compensatory payments. This demand has been resisted by the Commission as too costly, although agriculture commissioner Franz Fischler appears to be shifting towards the applicant countries' position.



New directions

With all these pressures for change, the EU should seize the opportunity to rethink the CAP. That does not mean that Europe has to abandon its support for the agricultural sector. For one thing, EU countries are not the only ones to subsidise their farmers. But most ways of measuring farm support show that transfers to farmers in the EU are higher than the OECD average and well above those in the US. According to most OECD measures of support, only Switzerland, Norway, Iceland, Korea and Japan are more generous to their farmers than the EU. And the latest annual OECD report on agricultural policies shows that after declining in the early 1990s, farm subsidies have risen again in the past few years in Europe as well as in the US. Commission officials argue that as a percentage of GDP, the EU and US spend similar amounts on farm subsidies, but according to independent analysts the EU's policies are more trade distorting than those of the US.

There is a consensus among European governments in favour of maintaining a rural population that includes smaller farms. In many parts of Europe, from France's Haute Savoie to the Welsh hills, farmers are not able to compete at the world level without protection or subsidies. Some population shift from agriculture to other sectors is probably unavoidable if protection is to be reined back. But it should be possible to design policies that encourage many people to remain on the land and in rural areas.

The most obvious improvement would be to stop sinking billions of euro into farms that are internationally competitive. This could be done either by gradually reducing payments to bigger farmers, as provided for under the Commission's "degressivity" plan, or by establishing a cut-off point for subsidies based on the size of a farm. Another way could be to target payments on low-income farmers. Payments to encourage organic farming, which are provided for under Agenda 2000, could also be vastly expanded. The EU's current strategy of devolving environmental aid schemes to member-states should also be reviewed, because it could result in some countries failing to do enough to encourage organic farming. To avoid this, the EU could set guidelines or minimum spending levels to be followed by national governments.

The EU could also expand schemes aimed at helping small producers, especially organic farmers, to work together to meet the demand from the



retail sector for large quantities and steady supplies. Cooperatives and other joint marketing arrangements already exist in some members-states, but there is room for expansion on a regional and even cross-border basis.

Given public hostility to the kind of intensive farming practices that have been linked to food safety crises, politicians should be able to harness support for these kinds of CAP reform. One way for the EU to defuse some of the tensions surrounding the WTO Round would be to work with animal welfare, environmental and consumers' lobbies to come up with pro-farming policies that are less trade-distorting. Such a strategy would take on the agricultural lobbies, which all too often have succeeded in convincing the public that the current CAP is the only way to protect small farmers and the countryside. But the strategy would not be effective unless politicians and policy-makers were much more honest about the economic and environmental drawbacks of the CAP.

European governments also need to improve infrastructure in rural areas, to attract and keep a non-agricultural population. The internet and other forms of communication open up possibilities for the self-employed and small businesses to locate away from urban centres. But if roads are bad, mobile phones cannot find a signal and there is a dearth of competent communications technicians, people will just not stay. Although Agenda 2000 includes rural development funds, these should be increased and targeted more specifically on infrastructure.

However, some long-time watchers of EU agricultural policy believe that such measures will not suffice and that a yet more radical approach is needed. Brian Gardner, a senior policy analyst at PRM Consultants in Brussels, argues that the past decade's CAP reforms are "nothing of the sort". He urges "the replacement of the current agricultural policy with a wider and more comprehensive rural policy".

Specifically, he calls for the speedy elimination of all production-linked subsidies and their replacement by "green" subsidies. Gardner believes that all market intervention for agricultural commodities should be phased out and production quotas for milk and sugar eliminated. On the external front, he calls for the scaling down of import tariffs, the elimination of import quotas and the end of export subsidies and export credits. All



this would be done in the framework of the WTO and accompanied by direct aid schemes for developing countries that currently benefit from quotas. It would lead to the establishment of an effective European agro-environmental policy where payment of subsidies depended on compliance with environmental protection standards, Gardner suggests.

Doubtless, such a package is too ambitious in the short-term. But it contains elements that the Commission should pursue. Of particular interest is the idea of green subsidies that pay farmers to shift toward organic farming or use less chemical pesticides and fertilisers. Unless there is a move in this direction before enlargement, farmers in the new member-states from Central and Eastern Europe will use subsidies to invest in the chemicals and equipment that will worsen the overproduction and pollution.

The fact that the CAP continues to benefit mainly large producers also undermines the EU's contention that trading partners should recognise a "European model" of agriculture. Other countries are certainly leery about the EU's push for the "multifunctional" nature of European agriculture to be recognised within the WTO. In Seattle, the EU tried to insist on having the term multifunctional included in the mandate for agricultural trade negotiations, but had to relent.

Time for business

The EU's position on agriculture ahead of Seattle was far from revolutionary. In offering the Agenda 2000 deal as a basis for the negotiation, the EU put itself on the defensive, given that most trading partners consider Agenda 2000 a disappointment. In the aftermath of Seattle, the EU, and Pascal Lamy, have given little away on how the EU will handle the farm talks called for under the Uruguay Round's "built-in agenda". Lamy told this writer that he accepts more agricultural reform may be needed "in the future", not just because of trade pressures but to cope with an enlarged EU. "I have no doubts that the moves begun in 1992 and reinforced in 1999 should be continued."

Unfortunately, though, the EU does not see the near-agreement on agriculture in Seattle as a starting point for the current farm negotiations, because it was conditional on the launching of a full WTO round. In effect, that means the agricultural negotiators have to go back to square



one. Although the EU is taking part in the built-in agenda talks, signs of European foot-dragging on agriculture have emerged. These included EU efforts to prevent a senior Brazilian diplomat from being appointed to chair the talks, because his country is a member of the Cairns group.

Such tactics should be avoided at all costs, because they risk further undermining the WTO and will not make it easier for the EU to get what it really wants: a full-scale trade round. Moreover, they could hinder the EU's efforts to garner international support for its concept of the "precautionary principle" in trade. Until now, the WTO has accepted that countries can block imports temporarily due to concerns about health or safety, until adequate evidence can be gathered. The EU's experience with mad-cow disease, however, has shown that it can take years for scientists to decide definitively that something is dangerous.

As a result, the EU is pressing for a clearer mechanism that allows trade to be interrupted if governments believe the evidence of a product's safety is not conclusive. The EU is right to try to have this issue clarified, because it will not do the world trading system any good if the WTO is seen to be forcing people to eat foods they do not want. But the EU drive faces strong resistance from the US and other agricultural exporters, who fear any such mechanism could be used for protectionist purposes.

To allay such concerns, the EU should consider accepting limits to the use of the precautionary principle, which would only come into play if efforts at labelling schemes and international standard-setting fail. Of course, the best way to convince others that the EU's proposals are not protectionism in disguise would be to get down to serious negotiations on the liberalisation of agricultural trade.

Political fallout

One frequently heard justification for the moderation of the EU's agricultural reforms is the difficulty of overcoming opposition from Europe's notoriously strong farming lobby. As suggested earlier, one strategy would be to convince the wider public of the environmental and financial drawbacks of the CAP as it is now. But even better would be to gain support for change from at least part of the agricultural community.



It is highly unlikely that big industrial farmers can be convinced that a reduction in their subsidies is a good thing. After the Uruguay Round agreement set limits on the use of export credits, EU policy-makers promoted cuts in guaranteed farm prices as a way to ensure that the EU could continue exporting on world markets. Although this did not turn large-scale farmers into supporters of CAP reform, the argument—along with the compensatory payments—neutralised some opposition, especially in France’s internationally-competitive cereals sector. The next steps, however, will be even more difficult to sell to this group. Any reduction in direct payments to farmers or lowering of protective barriers—two key demands of Europe’s trading partners—will be fiercely resisted by national agricultural lobbies.

So far, these organisations have succeeded in remaining unified at both the national and European level, with small farmers turning out in their thousands to demonstrate in favour of a system that mainly benefits the big producers. The development of policies designed to enhance the livelihood of smaller producers would allow politicians and EU officials to go on the offensive, seeking the support of as many farmers as possible.

It should not be too difficult to sell most farmers a scaling back of direct payments to big, competitive producers and an increase in rural and “green” subsidies that mainly benefit small and medium-sized farms. The lowering of external barriers is more problematic, however, because Europe’s smaller farms have much higher costs than competitors in Cairns Group countries and the US. As a result, to retain the backing of at least part of the farm lobby, the EU may have to open its market more slowly than Europe’s trading partners would like.

5 Conclusions

The collapse of the WTO ministerial in Seattle was not just a setback in the drive for further trade liberalisation. It signalled the failure of the political class in the EU and US to convince many of their own citizens, as well as governments in developing countries, of the benefits of the existing world trading system. The reasons for this were many and varied on each side of the Atlantic, with the US electoral calendar playing a large role in the Clinton administration's handling of the talks. Tensions in the EU-US relationship, weakened European institutions and residual ill-feeling over the selection of the head of the WTO, all took their toll.

If the damage is to be repaired in coming months, it will take a concerted and creative effort by all. In Europe, the temptation has been to blame the US for the Seattle failure and to await the outcome of the US elections. While it may take a new administration to give impetus to global trade negotiations, and put EU-US trade relations on a happier footing, there is plenty to be done in the meantime.

The EU needs to operate on several different fronts. Commissioner Lamy and European governments should work together on ideas for a more people-friendly international trading system. Concerns about the environment, human rights and poverty are real and need to be addressed globally. This would help to widen support in developed countries for a new round and counter fears about globalisation. Governments from all parts of the political spectrum, including centre-left administrations, have to ensure that the breakdown in Seattle does not result in a slide toward protectionism.

At the same time, the EU will have to counter suspicions among trading partners in the developed and developing world that its strategy for a new trade round would actually encourage protectionist practices. The most effective way to reassure doubters and get them to the table would be to show some of the EU's negotiating hand. In this respect, agriculture is of more political and symbolic importance than its weight in the global



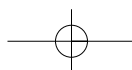
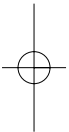
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economy would imply. Too often in the past, important trade liberalisation packages have been held up by the EU's unwillingness to make concessions on agriculture. On the other hand, the rest of the world should avoid using terms like "the complete elimination of subsidies", which experience has shown do not help produce agreements with the EU.

Among the moves that European trade policy-makers and politicians should consider are:

- ★ Offering trade concessions to developing countries, including in the areas of textiles and anti-dumping.
- ★ Engaging in serious negotiations in the Uruguay Round's built-in agenda of agriculture and services.
- ★ Avoiding unnecessary confrontations over personalities and procedures in Geneva.
- ★ Being more honest with European citizens about the drawbacks of the CAP.
- ★ Showing willingness to reform further the CAP, without waiting to be forced to by a WTO trade round.
- ★ Giving the Commission jurisdiction over all areas of trade.
- ★ Improving co-ordination between EU ministers and the Commission during international trade talks.
- ★ Working for better EU-US relations. While it may take until after the American elections for some issues to be resolved, efforts should start now. The most pressing area is food safety, where the two sides could work on confidence-building in the hope of eventually agreeing on common standards and inspection procedures. One way would be to set up joint EU-US committees to look at the way food safety laws and regulators work on both sides of the Atlantic.
- ★ Devising strategies to cope with hostility to globalisation. These should include pressing for changes in the WTO to make the world





trading system more acceptable to the wider public. At the same time, the EU should avoid blaming the WTO for unpopular decisions at home.

These efforts will be complex, controversial and even painful, especially when it comes to agricultural reform. But if they mean that the EU succeeds in helping to shape and maintain an open multilateral trading system that benefits as many people as possible, they will have been worthwhile.

