

The Future of U.S. Involvement in the WTO

To: Secretary of State Hillary Clinton
Subject: The Impact of the WTO on U.S. and Global Inequality
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Executive Summary

I recommend that the U.S. remove itself from the World Trade Organization and establish a new trade and equality forum to better respond to the increasing economic inequality both within and between nations. The WTO has failed to use globalization as a mechanism for equality within nations. By facilitating the unregulated growth of Foreign Direct Investment, it has aided the erosion of the U.S. middle class and undermined union bargaining power. The WTO has also made no effort to increase transparency or include unions, NGOs or other civil society groups in the international trade discussion.

In addition to increasing economic inequality within the U.S., the WTO has assisted the growth of between-nation inequality through the passage of the TRIMS, TRIPS and GATS Agreements. These acts force developing nations to compete with multinational corporations, prevent them from establishing a stable domestic infrastructure, and burden them with the high costs of implementation. Finally, the structural asymmetries in the WTO's decision-making process and dispute resolution system prevent less powerful nations from voicing their concerns or catalyzing progressive change. Therefore, I recommend that the U.S. remove itself from the WTO and create an open forum that utilizes trade as a mechanism for national and global equality.

Introduction

In supporting my recommendation that the U.S. should leave the WTO, I first present the WTO's effect on U.S. economic inequality. Empirical studies show that increased trade with developing countries, as managed by WTO policies, accounts for twenty percent of the reduction in the "earnings of low-skilled American workers relative to high-skilled workers."¹ I then discuss how its mechanisms prevent any progressive movement towards global economic equality. After addressing the potential difficulties that may arise with this policy, I end with the argument that the WTO, through its policies and its structure, show no signs of changing and should be replaced with a more open, representative trade and equality forum.

The WTO's management of foreign direct investment erodes U.S. middle class

Since the WTO's formation in 1995, more than "3.8 million manufacturing jobs have been lost" due to the rising trade deficit.² Manufacturing jobs make up the lion's share of what Robert Reich calls routine production jobs, which "entail the kinds of tasks performed by the old foot soldiers of American capitalism in high-volume enterprise."³ Since they require less skill and education, routine production jobs are easily outsourced to developing nations where labor costs are low. Multinational corporations have capitalized on the relative simplicity of these jobs by increasing foreign direct investment in developing nations. In response, the WTO has made no attempt to regulate FDI growth in order to minimize consequential job loss. For example, "global foreign direct investment (FDI) inflows amounted to \$1,306 billion in 2006, rising more than 38% over the previous year."⁴ Therefore, by failing to properly regulate the international flow of FDI, the

¹ Michael J. Trebilcock and Robert Howse, *Regulation of International Trade* (New York: Routledge, 2005), 12.

² Peter Morici, "The Trade Deficit and Job Losses," *Counterpunch*, August 12, 2008, <http://www.counterpunch.org/morici08122008.html> (accessed April 24, 2009).

³ Robert Reich, *Work of Nations* (New York: Vintage Books, 1992), 174.

⁴ "Widespread Growth of Foreign Direct Investment Reported for 2006," *United Nations Conference on Trade and Development Website*, October 16, 2007, <http://www.unctad.org/Templates/webflyer.asp?docid=9100&intItemID=4431&lang=1> (accessed April 24, 2009).

WTO has directly contributed to the rise of wage inequality in America.

New corporate mobility prevents unions from gaining leverage

The WTO's failure to regulate FDI has also caused a decline in union bargaining power, resulting in lower wages for middle class workers. Since corporations now have the opportunity to exit markets where there is labor resistance, unions must accept either lower wages or job cuts. More specifically, "the more substitutable domestic workers are with foreign workers due to e.g. international trade, outsourcing and FDI, the lower the enterprise surplus ends up with workers... [and] as a consequence, unions have become weaker."⁵ This weakness directly translates to a future of increased wage inequality. Unions reduce wage inequality by "raising wages more at the bottom and in the middle of the wage scale than at the top. Lower-wage, middle-wage, blue-collar, and high-school-educated workers are also more likely than high-wage, white-collar, and college-educated workers to be represented by unions," which also contributes to decreased inequality.⁶ By undermining union bargaining power, the WTO has decreased the unions' effect on reducing inequality. In addition, no mechanisms exist within the WTO to allow union engagement. "Unlike a number of other international organizations, the WTO permits only representatives of governments and selected intergovernmental organizations to participate in or observe the processes of its regular activities."⁷ The lack of union voice, or the voice of civil society in general, seriously restricts any opportunity for constructive change. By allowing union power to be subverted by increased corporate mobility and by restricting participation in such decisions to states only, the WTO has crippled a key combatant against wage inequality.

⁵ Ellen Brock and Sabien Dobbelaere, "Has International Trade Affected Workers' Bargaining Power?" *Centre for Institutions and Economic Performance* (2003), <http://ideas.repec.org/p/lic/licosd/13603.html#provider> (accessed April 25, 2009).

⁶ Lawrence Mishel, Jared Bernstein and Heidi Shierholtz, "The State of Working America 2008/2009: Unions and the Economy," *Economic Policy Institute* (2008), <http://www.stateofworkingamerica.org/> (accessed April 26, 2009).

⁷ Kofi Annan, "Foundations for a Fair and Free World Trade System," *The Role of the World Trade Organization in Global Governance*, ed. Gary Sampson (New York: United Nations University Press, 2001), 11.

WTO policies promote exploitation of developing countries

The WTO has aided the unrestricted exploitation of developing nations through the TRIMS Agreement, the TRIPS Agreement, and the GATS (General Agreement on Trade in Services). The TRIMS Agreement “clarifies that certain types of investment measures applied to enterprises... are inconsistent with the GATT” Article III and must be removed by members in a specific time period.⁸ Article III states that “once border duties have been paid by foreign exporters, as provided for in a country’s tariff schedules, no additional burdens may be imposed... where domestic producers of the like product do not bear the same burden.”⁹ And unless “FDI is carefully regulated and fits well into a host country’s development programme, technology transfer and other economic benefits may not take place, and the effect may merely be to ‘crowd out’ local investment.”¹⁰ Therefore, the TRIMS forces developing nations to give up their legislative control over foreign competition with domestic industries. Since the foreign competition is usually a large multinational corporation, the TRIMS Agreement hampers the host nations ability to establish a stable base of native companies for long-term development.

The TRIPS Agreement also acts against global equality by preventing the free flow of technological innovation to developing countries. Brought into effect in 1995, the TRIPS Agreement set “high standards of protection for patents, copyrights, trademarks, and industrial design and licenses.”¹¹ Since developing countries don’t have the resources to compete with multinational corporations in creating and patenting new ideas, they must instead pay to reproduce the technologies. In 1994, UNCTAD “estimated that the first year of implementation of the TRIPS

⁸ Richard Blackhurst and Adrian Otten, *Trade and Foreign Direct Investment*, October 9, 2006, http://www.wto.org/english/news_e/pres96_e/pr057_e.htm (accessed April 25, 2009).

⁹ Trebilcock and Howse, 456.

¹⁰ Fatoumata Jawara and Aileen Kwa, *Behind the Scenes at the WTO* (New York: Zed Books, 2003), 41.

¹¹ Jawara and Kwa, 36.

Agreement could cost a least developed country almost US\$20 million.”¹² The TRIPS also has prevented the use of new medicines to prevent the spread of disease in less developed nations, since they cannot afford to pay for the rights.

Finally the General Agreement on Trade and Services (GATS) has liberalized the service sector to the point that service companies in developing nations can’t compete with the financial strength and IT capabilities of multinational corporations. The agreement also “acts as a ‘ratchet’: once a country makes a commitment... it can neither breach the commitment nor change it in a way that makes it less favorable to exporters” without compensation or punishment through trade sanctions.¹³ Finally, it inhibits members from giving preferential treatment to other members, hampering the formation of regional negotiations that would act as an incremental step to full globalization. In combination, the GATS, TRIPS, and TRIMS all decrease global equality by entrenching less developed nations on the bottom of the global economic ladder.

The WTO’s power structure solidifies between-nation inequality

The structural asymmetries within the WTO’s decision-making and dispute settlement systems have facilitated the rise of between-nation inequality. The rise of between-nation inequality has driven the “dramatic divergence of incomes around the globe over the past two centuries.”¹⁴

The WTO makes decisions based off a consensus system. Proposals are presented and decided upon through informal negotiations known as “green room meetings.” However, the consensus system is inherently flawed because it “transforms the decision-making into a negotiating process that aims at reaching a bargain made of mutual concessions.”¹⁵ Since “most small

¹² Rubens Ricupero, “Rebuilding Confidence in the Multilateral Trading System,” *The Role of the World Trade Organization in Global Governance*, ed. Gary Sampson (New York: United Nations University Press, 2001), 52.

¹³ Jawara and Kwa, 32.

¹⁴ Trebilcock and Howse, 12.

¹⁵ Andreas R. Ziegler and Yves Bonzon, “How to Reform WTO Decision-Making?” *Swiss National Center of Competence in Research* (2007), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1049441 (accessed April 26, 2009).

delegations from developing countries do not have the appropriate resources in Geneva or at home to service the increasingly frequent, complex, and resource-intensive negotiation process,” the concessions are asymmetrical and further entrench the most destitute in exploitative trade agreements.¹⁶ In addition, green room meetings are “totally non-transparent. Attendance is ‘by invitation’ only, invitations being issued either by the director general or by the chair of the negotiating group. Most members who are uninvited are left in ignorance about what consultations are taking place, between which members, on which issues.”¹⁷

Between-nation inequality is also supported by the WTO’s dispute resolution system. The Dispute Settlement Body (DSB) appoints panels of independent experts to analyze disputes and present their decision, which the DSB then accepts or rejects. The DSB also oversees the punishment inflicted on the illegally acting state. Three problems arise with this system. First, the panels of experts are not chosen democratically, and the entire case is kept closed to civil society. In addition “WTO panel decisions are automatically adopted by the WTO member countries unless there is consensus against doing so,” creating a guilty-until-proven-innocent dynamic.¹⁸ Second, developing countries do not have the resources to hire representation or build a legitimate case, making the entire process tilted in favor of wealthy nations. As Roy Wilkinson writes, “the plight of developing countries has been further compounded by their relative deficiencies in legal expertise and by the sheer volume of complaints brought against them since the Organization’s establishment.”¹⁹ Finally, dispute settlement rulings are enforced through the sanctioning of retaliatory trade restrictions. This creates serious structural inequality because “trade restrictions by the USA or the European Communities (EC) against any other country would have a real impact on

¹⁶ Annan, 11.

¹⁷ Jawara and Kwa, 18.

¹⁸ Claude Martin, “The Relationship between Trade and Environment Regimes.” *The Role of the World Trade Organization in Global Governance*, ed. Gary Sampson (New York: United Nations University Press, 2001), 143.

¹⁹ Roy Wilkinson, *The WTO: Crisis and the Governance of Global Trade* (New York: Routledge, 2006), 97.

its economy, but the effect of trade restrictions by any but the very largest developing countries would have no effect at all.”²⁰ The dispute resolution mechanisms therefore prevent any opportunity to build a level playing field for all members.

Leaving the WTO may have serious consequences

While my research has thus far shown that leaving the WTO would decrease inequality on a national and global scale, several potential consequences to this policy must be considered. First, globalization and trade liberalization have been proven to aid developed and developing countries in certain instances. International trade makes goods and services cheaper, which decreases the cost of living for those who need it. For example, “lowering services barriers by one third under the Doha Development Agenda would raise developing countries’ incomes by around \$60 billion.”²¹ Globalization under the WTO’s management can also stimulate job growth. While the short-term effects may cause job loss in developed countries, in the long-term “the efficiency gains caused by trade liberalization are expected to lead to positive overall employment effects.”²² In addition, the WTO allows developing nations to access to technology and investment, effectively decreasing the gross number of poor people in the world.²³ Therefore, pulling the leading economic power out of the WTO may catalyze a new wave of protectionism that would be seriously detrimental to development and intra-national equality by access.

Second, despite all the WTO’s structural flaws and power imbalances, it is one of the only organizations that brings together developing and developed nations in an attempt to form mutually beneficial trade agreements. Leaving the WTO would destroy one of the few potential mechanisms

²⁰ Jawara and Kwa, 6.

²¹ “10 benefits of the WTO trading system,” *World Trade Organization Website*, http://www.wto.org/english/thewto_e/whatis_e/10ben_e/10b04_e.htm (accessed April 27, 2009).

²² Marion Jansen and Eddy Lee, *Trade and Employment* (Switzerland: WTO Secretariat, 2007), 12.

²³ Michael Weinstein, *Globalization: What’s New* (New York: Columbia University Press, 2005) 105.

of international trade regulation, and would open developing nations up to powerful corporate lobbyists that could further entrench them in the global economic basement. Although the WTO advocates unrestricted free trade, it acts as a buffer between developing nations and multinational corporations by allowing developing nations to voice their opinion to countries and companies that wouldn't otherwise listen. Leaving the WTO could potentially jeopardize all that the organization has already accomplished. Finally, doing so would be politically difficult, and establishing a more balanced forum would cost an unestimatable amount of resources that could be used to fund other policies to reduce U.S. inequality, like education or tax reform.

Conclusion

Despite the persuasive arguments opposed to pulling out of the WTO, the costs of continuing to support its policies through membership still outweigh the benefits. These costs manifest themselves in the demise of the U.S. middle class and the global increase in between-nation inequality. Although the laws passed by the WTO give a short-term economic boost to developing nations through investment and technology, in the long-term they trap them on the bottom of the economic ladder without the rungs to move up. In addition, the asymmetrical power structure of the WTO prevents those with less economic impact from making the changes necessary to solve such problems. The improbability of progressive change within the WTO necessitates the removal of the U.S. from membership. Instead, the U.S. should partner with NGOs, less developed nations, and institutions like the United Nations Conference on Trade and Development to create a more transparent and representative organization designed not just to facilitate international free trade, but to use trade as a mechanism for global economic equality.

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