Dispute Settlement Mechanisms and Power Asymmetry in Regional Trade Agreements

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The resurgence in regionalism

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DSMs in RTAs are much less in use

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Why do states design the DSMs in RTAs the way they do?

Medium-level of legalism for most RTAs

Why do the DSMs in RTAs generate the outcomes they generate?

Reinforce the power disparity & Less frequent use
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- **Less Frequent Use of RTA-DSMs**
  The study on systemic difference on DSMs in the WTO and RTAs

- **Structural Differences on the DSMs**
  Game theoretic model to analyze how DSMs affect the states’ decision making

- **RTA-game theoretic model**
  The extension of the structural analysis on the DSM in Rosendorff’s (2005) from the WTO-DSM to the RTA-DSM
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Introduction

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Model Set-Up

Excerpt from Rosendorff (2005)
“Stability and Rigidity: Politics and Design of the WTO’s Dispute Settlement Procedure”

Model Set-Up

strong player ($P_s$): export $x$ and import $m$, weaker player ($P_w$): complement tariff: $t$ for ($P_s$) and $\tau$ for ($P_w$)

political pressure: $a$ for ($P_s$) and $\alpha$ for ($P_w$), distributed $(0, +\infty)$ cdf of $\Phi$

The Infinitely Repeated Prisoners’ Dilemma (PD) Game
Dispute Settlement Strategy (DSS)

Figure 3: Under the WTO with the DSM, Rosendorff (2005)

$P_s$ having drawn politics type $\hat{a}$ has the following DSS:

[C] if $\hat{a} < a$, $t = t^c$

[DS] if $a \leq \hat{a} \leq \bar{a}$, $t = t^D(\hat{a})$ and pay compensation if lost

[D] if $\hat{a} > \bar{a}$, $t = t^D(\hat{a})$ and exit from the treaty without paying compensation if lost
RTA-Components

Costs Considerations: $K_{\text{strong}} < K_{\text{weak}}$

- Disparities in legal resources
- Equally shared costs of case proceedings
- Access to external legal assistance (experts of the WTO secretariat)

Winning Probability: $\theta_{\text{weak}} < \theta < \theta_{\text{strong}}$

- Vulnerable to domestic politics: economic/political conditions
- Less-likely impartial third-party review, Ad-hoc panel
- Power-based: not effectively mitigating power asymmetries
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1. Disparate Winning Probability $\theta$

Changes in Slope $\Rightarrow$ Changes in cutpoints

- **[WTO]** Same Chance of Winning, $\theta$, for both players

- **[RTA: $P_s$]** Smaller chance to fail to win ($\theta_w < \theta$) $\Rightarrow$ wider $DS$
  
  $\theta_w = \text{the winning probability of } P_w$

- **[RTA: $P_w$]** Greater chance to fail to win ($\theta_s > \theta$) $\Rightarrow$ narrower $DS$

  $\theta_s = \text{the winning probability of } P_s$
2. Disproportional Costs Burdens $K_i$

- [RTA] Costs burdens $\implies$ Lift of $\theta_i L_i(a) \implies$ Smaller area of $DS$ ($K_w > K_s$)

- [Magnitude of the effects]
  1. $[P_s]$ smaller $\theta_w \Rightarrow$ flatter slope $\Rightarrow$ weak narrowing effect of $K_s$
  2. $[P_w]$ larger $\theta_s \Rightarrow$ steeper slope $\Rightarrow$ strong narrowing effect of $K_w$
Increasing Gap

► Stronger Player \([P_s]\)
Smaller chance to lose (flatter slope) + Smaller costs burdens (less narrowing effect) \(\Rightarrow\) **Larger** \(DS\)

► Weaker Player \([P_w]\)
Larger Chance to lose (steeper slope) + Greater costs burdens (greater narrowing effect) \(\Rightarrow\) **Smaller** \(DS\)

► Hence, **Increasing the gap** in the range of \(DS\)
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Findings

- Reinforcement of inequalities with a greater magnitude
  1. $P_s$: more manipulating power than $P_w$
  2. $P_w$: less flexibility in RTAs than in the WTO.

- Uncertain effects of RTA-DSMs to stability of the system
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Questions and Answers

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Medium level of legalism (An Alternative Forum)
Similar Designs (Emulation of the WTO’s DSM)

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Why: Different levels of legalism + different environment
Outcome: Increased levels of disparities in flexibility
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Implications

- [Survival]
  Multilateralism survives in spite of the surge of RTAs. The superiority of the WTO-DSM: minimizing inequality, raising stability

- [Small Countries]
  High political pressure at home for sensitive trade sectors

- [RTAs] Access to external support for small and weak countries

- [WTO] More incentives or lower burdens for small and weak countries
THANK YOU !!

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DSS: Cut points in the WTO

(1) Lower bound, $a$ s.t.

$$\theta L(a) = D(a) - C(a) \equiv B(a)$$

the compensation it would have to pay = the gains from defection

(2) Upper bound, $\bar{a}$ s.t.

$$\theta L(\bar{a}) = \frac{\delta}{1-\delta} \left( p^2(N - S - D + C) + p(D - 2N + S) \right) \equiv \wedge DS$$

where $p = Pr(a < a)$, and $I = \int_\alpha \int_a I(a, \alpha) d\Phi d\Phi$ for $I = D, N, S, C$.

the expected level of compensation to pay = the expected benefits from cooperation into the indefinite future
DSS: Cut points in the RTA

- **Lower bound**, \( a_1 \) s.t. \( D_s(a_1) - \theta_w L_w(a_1) - K_s = C_s(a_1) \)
  the expected gain by temporary defection = the expected cooperation value

- **Upper bound**, \( a_2 \) s.t. \( L_w(a_2) = \frac{\delta}{1-\delta}(C_s - N_s) \equiv \wedge_{DS} \)
  the maximum amount of the penalty to pay = the present discounted expected losses of future punishments

- **Where**
  \[ C_s(a) = \Phi(\alpha_1)C_s(a) + \int_{\alpha_1}^{+\infty} S_s(a, \alpha)d\Phi(\alpha) + \theta_s \int_{\alpha_1}^{\alpha_2} L_s(\alpha)d\Phi(\alpha). \]