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The adoption of the 'Best Practices' for regional and free trade agreements in APEC: a road towards more WTO-consistent regional trade agreements?

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I. States have a fundamental right to form regional trade agreements

Historically, States have always formed closer links with some other States for, *inter alia*, cultural, trade and security reasons. When they created the *General Agreement of Tariffs and Trade* (GATT) in 1947, States could not ignore this economic and political reality; hence the inclusion of Article XXIV, which recognizes the right (albeit conditional) of States to form preferential regional trade agreements (RTAs). The philosophy of the GATT/World Trade Organization (WTO) disciplines with respect to RTAs is to ensure that the formation and evolution of such preferential arrangements support the multilateral trading system. Since multilateral trade is about greater trade opening, RTAs have to be supportive of this principle: RTAs should facilitate trade between the constituent territories and not raise barriers to the trade of non-RTA States. This principle is reflected in paragraph 4 of Article XXIV:

The contracting parties recognize the desirability of increasing freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries parties to such agreements. They also recognize that the purpose of a customs union or of a free-trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories. (Italics added)

¹ The views expressed in this chapter are personal to the author and do not bind the WTO Members or the WTO Secretariat. The author is grateful to Roberto Fiorentino, Pablo Furche, Arancha Gonzalez, and Alejandro Jara for comments on previous drafts. Mistakes are those of the author only.

As stated by the Appellate Body in the context of its discussion of the general exceptions in Article XX of the GATT 1994, WTO market access obligations must be balanced against the right of WTO Members to invoke exception provisions.² The Appellate Body repeated the same principle in *Turkey – Textiles* when dealing with a complaint by India that, as a result of the harmonization process that followed the formation of the European Communities–Turkey customs union, Turkey imposed a new import restriction on textiles that was contrary to the *Agreement on Textiles and Clothing (ATC)* and Article XI of the GATT of 1994. The Appellate Body stated:

This objective demands that a balance be struck by the constituent members of a customs union. A customs union should facilitate trade within the customs union, but it should *not* do so in a way that raises barriers to trade with third countries. We note that the *Understanding on Article XXIV* explicitly reaffirms this purpose of a customs union, and states that in the formation or enlargement of a customs union, the constituent members should 'to the greatest possible extent avoid creating adverse affects on the trade of other Members'.³ (Italics added; footnote omitted)

For RTAs, this balance has been articulated and made operational in the form of two conditions that must be respected whenever a WTO Member wants to justify a market access restriction or discrimination resulting from the formation of an RTA. In *Turkey – Textiles*, the Appellate Body made clear that RTAs must respect a series of conditions in order to be considered GATT/WTO-consistent:

Accordingly, on the basis of this analysis of the text and the context of the chapeau of paragraph 5 of Article XXIV, we are of the view that Article XXIV may justify a measure which is inconsistent with certain other GATT provisions. However, in a case involving the formation of a customs union, this 'defence' is available only when two conditions are fulfilled. First, the party claiming the benefit of this defence must demonstrate that the measure at issue is introduced upon the formation of a customs union that fully meets the requirements of sub-paragraphs 8(a) and 5(a) of Article XXIV. And, second, that party must demonstrate that the formation of that customs union would be prevented if it were not allowed to introduce the

² Appellate Body Report, *US – Gasoline*, p. 22, DSR 1996:I, 3, 21; Appellate Body Report, *US – Shrimp*, para. 159; Appellate Body Report, *Korea – Various Measures on Beef*, para. 164.
³ Appellate Body Report, *Turkey – Textiles*, para. 57.

measure at issue. Again, both these conditions must be met to have the benefit of the defence under Article XXIV.

We would expect a panel, when examining such a measure, to require a party to establish that both of these conditions have been fulfilled. It may not always be possible to determine whether the second of the two conditions has been fulfilled without initially determining whether the first condition has been fulfilled. In other words, it may not always be possible to determine whether not applying a measure would prevent the formation of a customs union without first determining whether there *is* a customs union.⁴ (Italics added)

Clearly, the formation of an RTA may justify measures that are inconsistent with any GATT rule, but only after having demonstrated compliance with a series of requirements relating to the RTA as a whole (Article XXIV:5) and to its internal and external (as far as customs unions are concerned), which must respect the provisions of Article XXIV:8. Finally, the inconsistent measure must be necessary to the formation of the RTA.⁵ Note the onerous burden of proof imposed on the WTO Member invoking Article XXIV to justify an inconsistent measure.

It is in the context of the conditions that must be respected for an RTA to be WTO-consistent that the recent Guidelines of the Asia-Pacific Economic Cooperation (APEC) forum must be examined. Recall that in Bogor, Indonesia, the APEC economies committed to free and open trade and investment in Asia-Pacific by 2010 for developed countries and by 2020 for developing countries. Although APEC economies have achieved significant liberalization and facilitation of trade and investment since 1994, the target dates seem to have forced APEC Ministers to address the possibility of reaching these target dates through RTAs. Indeed, in order to accelerate progress towards the Bogor Goals, APEC Ministers emphasized the need for promotion of 'high quality' RTAs and free trade

⁴ Ibid., paras. 58-59.

⁵ In particular, (i) the overall effect of the RTA must be compatible with Article XXIV:(5), which provides that the situation of third countries after the RTA must not be worse than before the RTA; (ii) internally the RTA must respect the provisions of Article XXIV(8)(a)(i); (iii) externally the RTA must respect the provisions of Article XXIV(8)(a)(ii); and (iv) the inconsistent measure must have been necessary to the formation of the RTA. For further and expanded discussion on the conditions for WTO-consistent RTAs see Gabrielle Marceau and Cornelis Reiman, 'When and How is a Regional Trade Agreement Compatible with the WTO?' (2001) 28 Legal Issues of Regional Integration, 297–336; and Nicolas Lockart and Andrew Mitchell, 'Regional Trade Agreements under GATT: An exception and its Limits', in Andrew Mitchell (ed.), Challenges and prospects for the WTO (London, 2005), p. 217.

agreements (FTAs),⁶ hence the adoption of the guidelines discussed hereafter. Will compliance with the APEC Guidelines facilitate or even ensure that WTO Members forming RTAs respect the requirements (conditions) for a WTO-consistent RTA? Hopefully, the APEC Best Practices for RTAs will have just this effect.

II. The 'Best Practices' for RTAs/FTAs in APEC

On the occasion of the 16th Ministerial meeting of APEC held in Santiago, Chile, on 17–18 November 2004, member economies endorsed the 'Best Practice for RTAs/FTAs in APEC' (herein, 'Best Practices'). On 6 September 2005, Chile and Korea jointly notified the APEC Best Practices to the WTO Secretariat and requested their circulation to WTO Members.⁷ These APEC Best Practices are quite innovative and are discussed briefly below.

APEC's Best Practices are beneficial to all WTO Members to the extent that they either reinforce or clarify WTO disciplines applicable to RTAs; they also offer an improved monitoring and surveillance mechanism. By building upon the existing WTO provisions on RTAs, APEC countries indicated that they endorse the principles contained in these provisions, and therefore that they support the multilateral trading system. Notably, these principles are complementary to and aim at ensuring the effective operation of the principle mentioned in Article XXIV:4 that RTAs should facilitate trade between RTA parties and not raise barriers with non-RTA parties.

Let us look at some of the APEC principles.

Consistency with APEC principles and goals

Consistent with APEC goals, they promote structural reform among the parties through the implementation of transparent, open and non-discriminatory regulatory frameworks and decision-making processes.

The issue of decision-making is important, but has not been explored in the context of WTO law generally. What is the legal value of decisions taken by an RTA body in case of a dispute entertained by WTO adjudicating bodies? Can WTO Members, which are also members of an RTA,

⁷ The APEC Best Practices were circulated as WTO document TN/RL/W/187, which is annexed to this chapter.

⁶ Statement of the Chair, Meeting of APEC Ministers Responsible for Trade, Jeju, Korea, 2–3 June 2005, available at http://www.apec.org/apec/ministerial_statements/sectoral_ministerial/trade/2005_trade.html.

take a decision in an RTA that goes against other rules of the WTO? Does Article XXIV provide justification for any type of WTO- inconsistency?

A related issue is to what extent members of an RTA can have a dispute settlement mechanism that would complete (that is, add to) or override that of the WTO. For instance, if parties to an RTA impose countermeasures for a violation of an RTA obligation, in accordance with the RTA's specific dispute settlement procedures, is the imposition of those countermeasures inconsistent with Article 23 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (DSU)? Or Article XI or II of the GATT 1994? Does Article XXIV of the GATT allow WTO Members to ignore Article 23 of the DSU, which prohibits a WTO Member from unilaterally determining that another WTO Member has violated the WTO agreements (including the application of countermeasures)? What is the reach of Article XXIV of the GATT 1994? Does it cover other multilateral trade agreements?

In addition, calling for transparency in decision-making is specially important when dealing with regulations of the members forming the RTA. Recall that the formation of an RTAs implies the evaluation of the impact of duties and other 'regulations of commerce' (Article XXIV:5 and XXIV:8). If, on the one hand, the elimination of duties in RTAs can be easily quantified, regulations, on the other hand, are hard to measure, though they are a central pillar of the requirements of XXIV, both in terms of internal liberalization and of not raising barriers to third parties. Transparency, as to the context for the adoption of such regulations together with their administration, would be crucial to ensure a decent assessment of their impact on international trade.

Consistency with the WTO

They are fully consistent with the disciplines of the WTO, especially those contained in Article XXIV of the GATT and Article V of the GATS. When they involve developing economies to whom the Enabling Clause applies, they are, whenever possible, consistent with Article XXIV of the GATT and Article V of the GATS.

This point is very interesting as it seems to imply that APEC would favour RTAs that would not use the flexibilities of the Enabling Clause,⁸ whatever scope it offers (a full exemption of Article XXIV requirements or only an exemption from the internal requirements of RTAs provided in

Box Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries, GATT document L/4903, 28 November 1979, BISD 26S/203.

Article XXVIII:8). In other words, APEC developing countries would form RTAs that would (to the extent possible) respect the disciplines of Article XXIV of the GATT and Article V of the General Agreement on Trade in Services (GATS). Note that several developing countries have been notifying their RTAs under Article XXIV instead of the Enabling clause (or both).

Go beyond WTO commitments

In areas that are covered by the WTO, they build upon existing WTO obligations. They also explore commitments related to trade and investment in areas not covered, or only partly covered, by the WTO. By so doing, APEC economies are in a better position to provide leadership in any future WTO negotiations on these issues.

This principle raises the issue of the extent to which RTAs can cover matters not otherwise covered by the WTO law. Clearly, States have the right to sign treaties on any matter (that do not violate *jus cognens*), but in limiting the scope of the WTO's jurisdiction (by excluding labour norms, for instance), have WTO Members decided that such issues cannot be dealt with in an RTA? It is doubtful. The difficult issue is how to reconcile actions in RTAs that may have effects in sectors covered by the WTO. For instance, assume that an RTA member violates the labour provisions of that RTA and, in accordance with the RTA's dispute settlement procedures, countermeasures are imposed in the form of an import restriction on textile products from the other RTA member (also a WTO Member). Are these textile import restrictions consistent with the WTO agreements? Are they authorized by Article XXIV? Do they need to be?

Transparency

By making the texts of RTAs/FTAs, including any annexes or schedules, readily available, the Parties ensure that business is in the best position to understand and take advantage of liberalized trade conditions. Once they have been signed, agreements are made public, in English wherever possible, through official websites as well as through the APEC Secretariat website.

Member economies notify and report their new and existing agreements in line with WTO obligations and procedures.

This is an important point calling for openness with respect to RTA information in line with the relevant WTO provisions. It also reflects the objectives being pursued by WTO Members in the Negotiating Group on Rules on RTAs in the area of transparency.

⁹ See Revised Informal Note by the Chairman, 'Elements for an RTA's Transparency Mechanism', JOB (06)/2. See also Decision TN/RL/18.

Transparency is a very difficult issue for all RTAs. Efforts have been made to encourage RTA parties to notify their proposed agreement as soon as possible so as to facilitate exchanges of views in the WTO Committee on Regional Trade Agreements (CRTA). The Decision of the WTO Council for Trade in Goods, ¹⁰ the procedures adopted by the Council for Trade in Services, ¹¹ and the checklist prepared for the CRTA ¹² also contain excellent wording requiring statistics and other technical information, but these decisions have not been adequately followed and respected by Members. Notification and review of RTAs covered by the Enabling Clause have also been problematic. ¹³ The APEC principle on transparency would mean that APEC developing countries will provide the information required pursuant to these decisions.

Simple Rules of Origin that facilitate trade

To avoid the possibility of high compliance costs for business, Rules of Origin (ROOs) are easy to understand and to comply with. Wherever possible, an economy's ROOs are consistent across all of its FTAs and RTAs.

They recognize the increasingly globalized nature of production and the achievements of APEC in promoting regional economic integration by adopting ROOs that maximize trade creation and minimize trade distortion.

Simple rules of origin, which has become a very controversial issue in RTAs, deserve important attention. Indeed, rules of origin can nullify the benefits of any market access negotiation, including the increased market access possibilities offered by the RTAs.

One difficult issue is whether rules of origin are to be considered as 'other regulation of trade' and, if so, how to evaluate and calculate their impact under paragraphs (5) and (8)(a)(ii) of Article XXIV. Further research and proposals are needed in this area.

Mechanisms for consultation and dispute settlement

Recognizing that disputes over implementation of RTAs/FTAs can be costly and can raise uncertainty for business, they include proper mechanisms to prevent and resolve disagreements in an expeditious manner, such as through consultation, mediation or arbitration, avoiding duplication with the WTO dispute settlement mechanism where appropriate.

¹⁰ Procedures on Reporting on Regional Trade Agreements, G/L/286.

¹¹ Procedures on Reporting on Regional Trade Agreements, S/C/W/92.

¹² Checklist of Points on the Operation of Regional Trade Agreements, WT/REG/W/3.

¹³ See WT/COMTD/W/114.

The issue of the overlap of dispute settlement systems is complex. It is even more complicated in the area of trade because Article XXIV of the GATT 1994 explicitly authorizes States to form preferential groupings, which, by implication, would contain a specific RTA dispute settlement system. There are now a few examples of those situations where two parties initiated disputes involving the same issues both in the RTA forum and in the WTO forum. We have had also an overlap of jurisdiction in the dispute between Chile and the European Communities over the landing of swordfish. The recent *Mexico – Taxes on Soft Drinks* case examined whether non-compliance with the North American Free Trade Agreement (NAFTA) could be invoked as a defence/justification for noncompliance under Article XX of the GATT.

Some FTAs contain a conflicts clause that gives priority, and sometimes exclusivity, to the FTA. However, it is difficult to see how these clauses could be enforced by WTO panels. This is because the WTO's DSU provides for an automatic process. Moreover, to the extent a simple allegation suffices to trigger the WTO dispute settlement mechanism, and because Article 23 of the DSU gives exclusive jurisdiction to WTO panels to determine WTO issues, the WTO adjudicating bodies will necessarily 'attract' jurisdiction. Often, States will prefer to initiate a dispute in the WTO, which is a faster and more efficient forum. In practice, because of its speed, the WTO dispute settlement mechanism will be able to provide adjudication – in the form of panel, Appellate Body, or arbitration reports – much faster than many other systems and will provide for automatic sanctions, while the other systems do not have such capabilities.

This means that, in the context of a dispute between two WTO Members involving situations covered by both an RTA and the WTO agreements, either WTO Member has the right to trigger the WTO dispute settlement mechanism and to request the establishment of a panel (even if there is a similar dispute in an RTA) if it considers that any of its WTO benefits have been nullified or impaired. Such WTO Member

¹⁴ See Panel Report, Argentina – Poultry Anti-Dumping Duties, para. 7.38; and Argentina – Cotton, Request for Consultations by Brazil, WT/DS190/1. Aspects of these disputes were also brought before the dispute settlement mechanism of the Southern Common Market (MERCOSUR).

¹⁵ See Chile – Swordfish, Request for Consultations by the European Communities, WT/DS193/1. The dispute was also brought to the International Tribunal for the Law of the Sea (See Case on Conservation of Swordfish Stocks between Chile and the European Communits in the South-Eastern Pacific Ocean).

¹⁶ Appellate Body Report, Mexico - Taxes on Soft Drinks, paras. 66-80.

cannot be asked, and arguably cannot even agree under Article 23 of the DSU, to take its WTO dispute to another forum, even if that other forum appears to be more relevant or better equipped to deal with the sort of problems at issue. In initiating a parallel WTO dispute, the WTO Member may be in violation of an RTA (where it promised not to do so), but this is not a matter to be decided by WTO panels or the Appellate Body. If a different result were desirable, then Article 23 of the DSU, the reverse consensus rule and the entire WTO dispute mechanism would have to be adjusted. However, if the RTA treaty prohibits its signatories from taking RTA related disputes to the WTO in certain circumstances, a WTO Member that would ignore this RTA prescription may risk RTA retaliation if it triggers the WTO dispute settlement mechanism, and such RTA retaliation, in my view, could be WTO-consistent pursuant to Article XXIV of the GATT 1994, which allows for (effective) RTAs.

Sustainable development

Reflecting the inter-dependent and mutually supportive linkages between the three pillars of sustainable development – economic development, social development and environmental protection – of which trade is an integral component, they reinforce the objectives of sustainable development.

The APEC definition of sustainable development is remarkable, particularly its reference to the inter-linkages between its economic, social and environmental components. This principle is also reflected in the Preamble to the *Marrakesh Agreement Establishing the World Trade Organization (WTO Agreement)* and has had tremendous influence on WTO jurisprudence.¹⁷ It would not be surprising to see the APEC definition quoted in future Appellate Body reports.

III. Conclusion

The issue of RTAs and their legal and economic compatibility with WTO disciplines and principles is complex. Although most WTO Members support multilateral liberalism, regional arrangements are often easier to negotiate and are often used as general foreign policy tools. They thus encompass policy considerations other than trade, although they are generally considered conducive to increased trade. If the WTO agreements provide that the formation of an RTA can justify inconsistencies with other WTO obligations, it also imposes conditions — relating to the RTA

¹⁷ See, for example, Appellate Body Report, US - Shrimp, paga. 153.

itself and its impact on non-RTA states – for such RTA to be WTO consistent. WTO Members and WTO jurisprudence have on occasion clarified the meaning of such conditions and have agreed on procedures to favour transparency and exchanges relating to the assessment and monitoring of RTAs. But WTO Members lack political will; as the number of RTAs increases, Members find themselves caught between difficult conflicting interests. In addition, given Members' limited human resources, WTO notification, reporting, reviewing and monitoring of RTAs are not handled seriously enough.

In this context, the fact that the APEC countries have decided unilaterally to set for themselves standards and principles that confirm, clarify and reinforce WTO disciplines and mechanisms set up to ensure that RTAs evolve so as to favour multilateral trade can only be received with praise. The APEC principles not only have the merit of pointing without any scruples to the difficult issues surrounding the co-habitation of regional and multilateral systems (Enabling Clause, RTAs, rules of origin, transparency of domestic regulations, reporting transparency and monitoring, dual dispute settlement systems, etc.), they also contain commitments that will strengthen the WTO multilateral system.

ANNEX

WORLD TRADE ORGANIZATION

TN/RL/W/187 12 September 2005 (05–3939)

English

Original:

Negotiating Group on Rules

BEST PRACTICE FOR RTAS/FTAS IN APEC1

Communication from Chile and the Republic of Korea

The following communication, dated 6 September 2005, is being circulated at the request of the Delegations of Chile and the Republic of Korea, for information.

RTAs/FTAs involving APEC economies can best support the achievement of the APEC Bogor Goals by having the following characteristics:

Consistency with APEC Principles and Goals

- They address the relevant areas in Part I (Liberalization and Facilitation) of the Osaka Action Agenda (OAA) and they are consistent with its General Principles. In this way they help to ensure that APEC accomplishes the free trade and investment goals set out in the 1994 Bogor Leaders Declaration.
- They build upon work being undertaken by APEC.
- Consistent with APEC goals, they promote structural reform among the parties through the implementation of transparent, open and nondiscriminatory regulatory frameworks and decision-making processes.

Consistency with the WTO

- They are fully consistent with the disciplines of the WTO, especially those contained in Article XXIV of the GATT and Article V of the GATS.
- Regional Trade Arrangements (RTAs), Free Trade Agreements (FTAs), and other Preferential Arrangements.

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 When they involve developing economies to whom the Enabling Clause applies, they are, whenever possible, consistent with Article XXIV of the GATT and Article V of the GATS.

Go beyond WTO Commitments

In areas that are covered by the WTO, they build upon existing WTO obligations. They also explore commitments related to trade and investment in areas not covered, or only partly covered, by the WTO. By so doing, APEC economies are in a better position to provide leadership in any future WTO negotiations on these issues.

Comprehensiveness

- They deliver the maximum economic benefits to the parties by being comprehensive in scope, and providing for liberalization in all sectors.
 They therefore eliminate barriers to trade and investment between the Parties, including tariffs and non-tariff measures, and barriers to trade in services.
- Phase-out periods for tariffs and quotas in sensitive sectors are kept to a minimum, and take into account the different levels of development among the parties. Thus, they are seen as an opportunity to undertake liberalization in all sectors as a first step towards multilateral liberalization at a later stage.

Transparency

- By making the texts of RTAs/FTAs, including any annexes or schedules, readily available, the Parties ensure that business is in the best position to understand and take advantage of liberalized trade conditions. Once they have been signed, agreements are made public, in English wherever possible, through official websites as well as through the APEC Secretariat website.
- Member economies notify and report their new and existing agreements in line with WTO obligations and procedures.

Trade Facilitation

 Recognizing that regulatory and administrative requirements and processes can constitute significant barriers to trade, they include practical measures and cooperative efforts to facilitate trade and reduce transaction costs for business consistent with relevant WTO provisions and APEC principles.

Mechanisms for Consultation and Dispute Settlement

 Recognizing that disputes over implementation of RTAs/FTAs can be costly and can raise uncertainty for business, they include proper mechanisms to prevent and resolve disagreements in an expeditious manner, such as through consultation, mediation or arbitration, avoiding duplication with the WTO dispute settlement mechanism where appropriate.

Simple Rules of Origin that facilitate Trade

- To avoid the possibility of high compliance costs for business, Rules of Origin (ROOs) are easy to understand and to comply with. Wherever possible, an economy's ROOs are consistent across all of its FTAs and RTAs.
- They recognize the increasingly globalized nature of production and the achievements of APEC in promoting regional economic integration by adopting ROOs that maximize trade creation and minimize trade distortion.

Cooperation

 They include commitments on economic and technical cooperation in the relevant areas reflected in Part II of the OAA by providing scope for the parties to exchange views and develop common understandings in which future interaction will help ensure these agreements have maximum utility and benefit to all parties.

Sustainable Development

 Reflecting the inter-dependent and mutually supportive linkages between the three pillars of sustainable development – economic development, social development and environmental protection – of which trade is an integral component, they reinforce the objectives of sustainable development.

Accession of Third Parties

• Consistent with APEC's philosophy of open regionalism and as a way to contribute to the momentum for liberalization throughout the

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APEC region, they are open to the possibility for accession of third parties on negotiated terms and conditions.

Provision for Periodic Review

• They allow for periodic review to ensure full implementation of the terms of the agreement and to ensure the terms continue to provide the maximum possible economic benefit to the parties in the face of changing economic circumstances and trade and investment flows. Periodic review helps to maintain the momentum for domestic reform and further liberalization by addressing areas that may not have been considered during the original negotiations, promoting deeper liberalization and introducing more sophisticated mechanisms for cooperation as the economies of the Parties become more integrated.