

# How to make EPAs WTO compatible?

Reforming the rules on regional trade agreements

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# How to make EPAs WTO compatible?

## *Reforming the rules on regional trade agreements*

By Bonapas Onguglo and Taisuke Ito\*

This report aims to contribute to the preparations by the African, Caribbean and Pacific (ACP) Group of States for the negotiations with the European Union (EU) of new WTO (World Trade Organization)-compatible trading arrangement(s), with flexibility and special and differential treatment for ACP States, as agreed between the two parties to the Partnership Agreement signed in Cotonou, Benin in June 2000. It focuses on the option of economic partnership agreements (EPAs) which provide for the parties to progressively remove barriers to trade between them. An agreed principle governing new ACP–EU trading arrangements is their full conformity with the relevant provisions of the WTO. However, the reciprocity as would be required under prevailing WTO rules on regional trade agreements is likely to pose greater adjustment costs on the part of ACP States that decide to become party to an EPA, either individually or as a group. It is thus recognised in the Partnership Agreement that the ACP States would be provided more flexibility under the EPAs in trade in goods, in particular in relation to the pace of market opening and the product coverage. Also, the ACP States and the EU agreed to ‘closely cooperate and collaborate in the WTO with a view to defending the arrangements reached, in particular with regard to the degree of flexibility available’. This is necessary because such flexibility needs to be appropriately covered under WTO rules, yet the relevant WTO provisions governing regional trade agreements applicable to developed countries, namely Article XXIV of GATT 1994 and the Uruguay Understanding on that Article, do not contain explicit or adequate special and differential treatment for developing countries.

Thus, there exists an important legal lacuna in terms of the availability of special and differential treatment for developing countries in the WTO rules regarding North–South agreements, although it is precisely in such agreements that developing countries would most likely be in need of some flexibility. If future EPAs are to be legally valid and economically viable, it is imperative that special and differential treatment be made available to developing countries that enter into reciprocal trade agreements with developed country trading partners, and that such treatment be firmly incorporated into the relevant WTO rules. This report examines the case for, and draws up some suggestions on ways to, incorporating special and differential treatment into the WTO rules applicable to North–South regional trade agreements, in particular in Article XXIV of GATT1994, that would enable future EPAs to allow greater flexibility for ACP States to meet the test of WTO conformity. Such adjustments could be undertaken in the context of multilateral trade negotiations on WTO rules under the Doha work programme adopted by the Fourth WTO Ministerial Conference. An effort by ACP States and the EU in this respect requires the parties to elaborate their negotiating objectives on the new trading arrangements back-to-back with their participation in multilateral trade negotiations, so that the objectives of WTO-compatible arrangements with flexibility for ACP States can be promoted in a coherent and mutually supportive manner.

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## ABBREVIATIONS

AAD	Agreement on the Implementation of Article VI of GATT 1994 (on anti-dumping,WTO)
ACP	African, Caribbean and Pacific Group of States
AGOA	African Growth and Opportunity Act
ASCM	Agreement on Subsidies and Countervailing Measures
ASEAN	Association of South–East Asian Nations
ASG	Agreement on Safeguards (WTO)
BOP	balance of payments
CBI	Caribbean Basin Initiative
CTG	Council for Trade in Goods (WTO)
CVD	countervailing duties
CARICOM	Caribbean Community and Common Market
COMESA	Common Market for Eastern and Southern Africa
CRTA	Committee on Regional Trade Agreements (WTO)
DCs	developing countries
DDA	Doha development agenda
DDCs	developed countries
DSB	Dispute Settlement Body (WTO)
DSU	Understanding on Rules and Procedures Governing the Settlement of Disputes (WTO)
EAC	East African Community
EBA	Everything but Arms initiative
EIA	Economic Integration Agreement on trade in services
EFTA	European Free Trade Association
EPA	economic partnership agreement
EC	European Commission
ECOWAS	Economic Community of West African States
EU	European Union
FTA	free trade area
FTAA	Free Trade Area of the Americas
GATS	General Agreement on Trade in Services (WTO)
GATT	General Agreement on Tariffs and Trade
GCC	Gulf Cooperation Council
GSP	Generalized System of Preferences among developing countries
GSTP	Global System of Trade Preferences
HS	Harmonized Commodity and Description and Coding System
LDC	least developed country
MERCOSUR	Southern Common Market
MFN	most-favoured-nation
MRA	mutual recognition agreement
NAFTA	North America Free Trade Area
NTB	non-tariff barrier to trade
ORC	other regulations of commerce
ORRC	other restrictive regulations of commerce
PICTA	Pacific Island Countries Trade Agreement
ROO	rules of origin
RTA	regional trade agreement
SAARC	South Asian Association for Regional Cooperation
SACU	South African Customs Union
SADC	Southern African Development Community
SAT	substantially all the trade
SDT	special and differential treatment
SPARTECA	South Pacific Regional Trade and Economic Cooperation Agreement
SPS	sanitary and phytosanitary measures
TBT	technical barrier to trade
UEMOA	West African Economic and Monetary Union
UNCTAD	United Nations Conference on Trade and Development
WTO	World Trade Organization

## EXECUTIVE SUMMARY

The ACP–EU Partnership Agreement signed in Cotonou in June 2000 provides a new framework for economic and trade cooperation between ACP Group of States and the EU, whose specific modalities shall be introduced gradually during a preparatory period between March 2000 and December 2007, and which shall, *inter alia*, ensure full conformity with WTO provisions, including special and differential treatment for ACP States. The new trade and economic framework consists essentially of four pillars: (i) the temporary non-reciprocal preferential treatment for ACP States basically continuing the trade preferences under the Fourth Lomé Convention; (ii) economic partnerships agreements (EPAs) between willing ACP States and the EU; (iii) alternative arrangements to EPAs for ACP States that choose not to adopt EPAs; and (iv) special treatment for least-developed ACP countries in the form of duty-free and quota-free treatment for their exports.

The WTO compatibility of the resultant arrangements is a fundamental condition, albeit juxtaposed against the special and differential treatment (SDT) for ACP States. The pillar pertaining to the temporary continuation of the Lomé-type non-reciprocal trade preferences required a WTO waiver under WTO Agreement Article IX, which was granted in November 2001 by the Fourth WTO Ministerial Conference (two waivers on Article I and Article XIII of GATT 1994). The modalities for the least developed countries (LDCs) have been addressed by the EU's Everything but Arms (EBA) initiative as an extension of its Generalized System of Preferences (GSP) scheme. Such special GSP treatment for LDCs is compatible under the WTO with paragraphs 2(a) and (d) of the Enabling Clause. The modalities for possible alternatives to EPAs, and the attendant WTO compatibility, have yet to be identified as this pillar is scheduled for consideration in 2004 (although some preliminary analyses suggest a 'super-GSP' scheme). The modalities for the EPAs pillar would be defined through consultations and negotiations launched on 27 September 2002. In this respect, the WTO rules applying to regional trade agreements are subject to negotiations under the Doha work programme launched by the Doha WTO Ministerial Conference. Thus, the WTO compatibility aspect of future EPAs, especially as regards SDT for ACP States, needs to be addressed against this background. At the same time, the Doha work programme on WTO rules on RTAs as well as the emphasis placed in the work programme on SDT, provides a unique opportunity for the ACP Group of States to engage actively in the negotiations to introduce reforms that address their specific, common trade and developmental interests in forming EPAs with the EU and to secure their compatibility with WTO rules.

In North–South Regional Trade Agreements (RTAs) such as EPAs, developing countries are likely to need greater policy flexibility to adjust their economies to benefit from freer regional trade. The case is stronger for ACP States, most of which are small and vulnerable, if not LDCs. While future EPAs, being mixed North–South RTAs, would have to be notified under Article XXIV of GATT 1994, the major deficiency of this article is the absence of explicit SDT provisions for developing countries. This constitutes a legal lacuna and inconsistency in existing WTO disciplines, and holds true despite the existence of other GATT provisions that set out SDT for developing countries. While Part IV of GATT 1994 has provided a set of SDT provisions for developing countries since 1964, a WTO dispute settlement case established that Part IV of GATT 1994 is not applicable in conjunction with Article XXIV of GATT 1994. This undermines a possible claim that in a North–South RTA, the reciprocity requirement of Article XXIV of GATT 1994 can be waived for developing countries on the basis of the non-reciprocity exhortation of Part IV of GATT. The Enabling Clause has provided since 1979 a flexible framework of rules for developing countries in forming regional integration agreements among themselves ('South–South RTAs'). However, its current provisions do not cover those RTAs formed between developed and developing countries, as would be the case with future EPAs. Therefore, the result is that no SDT is applicable to developing countries forming North–South RTAs in conforming to requirements as provided under GATT Article XXIV.

The anomaly of the lack of SDT in GATT Article XXIV is most evident if a comparison is made with its counterpart article in the General Agreement on Trade in Services, namely GATS Article V. GATS Article V:3(a) clearly provides and locks in flexibility for developing countries in meeting conditions set out in GATS Article V:1 regarding the substantial sectoral coverage, absence or elimination of discriminatory measures in accordance with the level of development. Furthermore, GATS Article V:3(b) recognises a distinction between North–South RTAs and South–South RTAs by providing additional favourable treatment for developing countries in the case of the latter. This inconsistency in the availability of SDT between goods and services highlights the need for SDT in the context of North–South RTAs.

Although some flexibility is inherent in the current provisions of GATT Article XXIV resulting from the ambiguity in terminology and current permissive practice in the WTO in the application of this article, such *de facto* existing flexibility is inadequate in providing sound legal basis and security for the flexibilities that would be deemed necessary for ACP States under EPAs. First, such inherent *de facto* flexibility might still prove to be insufficient to provide sufficient legal cover for ACP flexibility under EPAs. Since such *de facto* flexibility does not differentiate between the flexibility available to developed and to developing countries, there persists a risk that the needs of developing countries for enlarging the scope of flexibility is curtailed by the systemic need for more stringent and effective disciplines (and thus less flexibility) for all WTO Members. Second such implicit flexibility is not appropriate in effectively providing legal security for, and to pre-empt future legal challenges against, EPAs. Thus, the existing flexibility can not be considered as substitute for SDT.

Therefore, the lack of SDT in GATT Article XXIV, together with the inadequacy of existing flexibility in that article to cater for the needs of developing countries under North–South RTAs, constitutes the case for reforming the relevant WTO rules to render SDT applicable to North–South RTAs in meeting the WTO conformity test. Since SDT is the modality to provide greater flexibility only to developing countries, it also responds to the systemic need for improved and clarified disciplines on RTAs. Three options are conceivable to that effect: (1) reforming Article XXIV of GATT 1994; (2) reforming Part IV of GATT 1994; and (3) reforming the Enabling Clause. Among them, there is the strongest case for the first option, i.e. reforming specifically Article XXIV of GATT 1994.

Reforming GATT Article XXIV translates into introducing elements of flexibility to those key benchmark requirements under GATT Article XXIV for developing countries through SDT, namely the ‘substantially all the trade’ (SAT) requirement, the transitional period, and the ‘not-on-the-whole-higher-or-more-restrictive’ requirements. In this respect, three approaches are conceivable: (i) generic provisions on SDT within Article XXIV of GATT in favour of developing countries; (ii) a review of specific provisions in Article XXIV of GATT; and (iii) a revision of GATT Article XXIV:10 on derogation from substantive requirements therein. Option (i) could consist in inserting a generic paragraph in Article XXIV of GATT 1994, or in the Understanding on the Interpretation of Article XXIV of GATT 1994, stating that the flexibility is to be provided for developing countries in terms of the key requirements stipulated in Article XXIV:5–8 (drawing some guidance from Article V:3(a) of GATS). The flexibility would in particular be applied to seek product and trade coverage and longer and more secure transitional periods. Option (ii) consists in revising and modifying specific provisions on the key requirements of Article XXIV of GATT, particularly Articles XXIV:5(c) and XXIV:8 (a)(i) and (b), so as to allow differentiation for developing countries. The aim of these changes is to allow flexible interpretation of the key requirements of Article XXIV of GATT 1994 for developing countries in the form of SDT, on the basis of which operationally ‘greater flexibility’ is defined specifically for developing countries. Option (iii) is a supplement to the two options and consists in rendering it easier for developing countries to seek derogation from the substantive requirements of GATT Articles 5–8.

The second option is to amend Part IV of GATT 1994 to render it applicable to North–South RTAs in conjunction with GATT Article XXIV. The reform would be geared towards rendering the non-reciprocity principle in multilateral trade negotiations, as provided in GATT Article XXXVI:8,

applicable to negotiations in the regional context. A key difficulty with this option lies in the fundamental irrelevance, as found in a GATT dispute panel ruling, of the non-reciprocity principle in multilateral trade negotiations to the conditions set out in GATT Article XXIV. First, SDT in GATT Article XXXVI:8, by definition, applies only to multilateral trade negotiations, and is thus irrelevant to regional trade negotiations. Second, GATT Article XXIV concerns conditions that individual RTAs have to meet, and not regional trade negotiations.

The third option is to extend the scope of the Enabling Clause beyond South–South RTAs to encompass North–South RTAs like EPAs. This would ensure that the maximum flexibility enjoyed by developing countries under this clause in the formation of South–South RTAs would also apply to North–South RTAs. It would, in effect, exclude future EPAs from the purview of GATT Article XXIV and its more stringent terms (compared with the Enabling Clause). A serious shortfall with this option, however, is that the legal validity of the Enabling Clause and its coverage of agreements formed among developing countries is increasingly being challenged by some WTO Members. Another is that the Enabling Clause, without any formal link to GATT Article XXIV conditions, could not guarantee reciprocity in the exchange of concessions between parties to an RTA, and thus may cover a non-generalised non-reciprocal preferential scheme such as an RTA, thereby circumventing the waiver requirements for such preferential schemes. This has systemic risk to the validity of unilateral preferences such as the GSP as well, since the Enabling Clause condition that unilateral preference is only allowed under the GSP scheme could also be circumvented.

Given the superiority of direct reform of GATT Article XXIV, there would be a further need, depending on negotiations, for operationalising the concept of ‘flexibility’ to be made available to developing countries in respect of the substantive and procedural requirements of GATT Article XXIV. Since the degree of flexibility to be made available specifically to developing countries through SDT would depend critically on the definition of generally applicable existing flexibility as well as concrete terms of ‘flexibility’ for developing countries, both elements may require operational definition and interpretation. The most relevant requirements for developing countries include the ‘substantially all the trade’ requirement for internal trade liberalisation and the transitional period. As to the former, possible modalities include the application of different methodologies for developed and developing countries (including the level of aggregation, subject of measurement, sectoral composition and treatment of non-zero preferential duties) and statistical threshold levels in measuring the SAT requirement for elimination of duties. This would allow for a lesser degree of market opening for developing countries. ‘Other restrictive regulations of commerce’ would need to be interpreted so that preferential application of trade remedy measures and other non-tariff measures by developing countries on intra-RTA trade would not be unduly impeded. The issue of the transitional period pertains both to its legal standing and its duration, including asymmetry. As RTAs are deemed to be ‘interim arrangements’ during the transitional period, securing legal protection from the requirements of GATT Article XXIV would leave significant flexibility for developing countries during that period. A transitional period of longer than 10 years could be secured by loosening the conditions for developing countries to meet the ‘exceptional cases’ test, and possibly by defining a maximum duration of transitional periods longer than 10 years.

This report points to some priority negotiating issues for ACP States under the Doha work programme on WTO rules on RTAs. First, the starting point for negotiations would be to retain the legal validity of the Enabling Clause for those RTAs formed among developing countries, including ACP States. The coverage of South–South RTAs under the Enabling Clause is to be considered *acqui* and not be subject to negotiation. Second, securing agreement among WTO Members on the incorporation of principle of SDT into GATT Article XXIV, possibly in the form of a generic paragraph, may well constitute a negotiating issue independent of other systemic issues. This would ensure special treatment for developing countries in meeting the requirements of GATT Article XXIV relative to generally applicable disciplines. For this purpose, a paragraph similar to GATS Article V:3(a) may prove to be useful. Third, the systemic issue debate on key substantive and procedural requirements on which the actual negotiations would be centred, would need to be geared towards ensuring the most favourable interpretation and operational understanding on the generally applicable flexibility in

respect of each key requirement, so that a sufficient degree of flexibility could be made available to developing countries. Such an exercise may be necessary, as the generally applicable flexibility would form the basis on which to build, as SDT, additional degrees of flexibility for developing countries. This is a way to maximise the degree of flexibility available to ACP States and developing countries in the application of GATT Article XXIV disciplines.

## Chapter I INTRODUCTION AND OVERVIEW

1. The Partnership Agreement between the members of the African, Caribbean and Pacific (ACP) Group of States of the one part, and the European Community and its Members States of the other part, was signed on 23 June 2000 in Cotonou, Benin. The signatories were the 77 ACP States and the 15 Member States of the European Union (EU) (see Box 1). The Partnership Agreement replaces the Fourth Lomé Convention, which expired on 29 February 2000, after being in existence for 10 years. Prior to that there were three other conventions; the first Lomé Convention signed in 1975 (and preceding that were two Yaoundé Conventions).<sup>1</sup> In total the Lomé Conventions provided 25 years of development cooperation between the ACP States and the EU. The expiry of the Lomé Convention necessitated the negotiations for its successor; which were launched in September 1998 and concluded in February 2000.

2. The ACP–EU Partnership Agreement changes and improves upon ACP–EU development cooperation in social, political and economic areas to bring about poverty reduction in the ACP States, sustainable development and their effective integration into the global economy (Article 1). Systemic account will be given to women and gender issues and to sustainable management of national resources and the environment. The political cooperation (Articles 8–13) includes political dialogue to contribute to peace, security and stability; a stable and democratic political environment; respect for all human rights and fundamental freedoms; conflict prevention and resolution; and migration. New instruments are provided for the financing of development cooperation, including debt and structural adjustment support, investment and private sector development support and technical cooperation (Articles 55–83). Special and specific support is provided for least-developed, landlocked and island ACP States (Articles 84–90). Institutional mechanisms for providing policy and political guidance and directions are also established (Articles 14–17). Non-State actors from the private sector, civil society and trade unions are to be involved in the implementing the Partnership Agreement (Articles 4–7).

### **Box 1: Signatories to the ACP–EU Partnership Agreement signed in Cotonou**

The 77 ACP States comprise 48 African, 15 Caribbean and 14 Pacific States. The African States are Angola, Benin, Botswana, Burkina Faso, Burundi, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Congo, Congo (Democratic Republic), Côte d’Ivoire, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, Gabon, The Gambia, Ghana, Guinea, Guinea Bissau, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mauritius, Mozambique, Namibia, Niger, Nigeria, Rwanda, Sao Tomé and Príncipe, Senegal, Seychelles, Sierra Leone, Somalia, South Africa, Sudan, Swaziland, Tanzania (United Republic), Togo, Uganda, Zambia and Zimbabwe. South Africa is qualified member, and provisions on trade and on development finance cooperation under the , Agreement do not apply. Thus, South Africa does not participate in EPA negotiations. The Caribbean States are Antigua and Barbuda, Bahamas, Barbados, Belize, Dominica, Dominican Republic, Grenada, Guyana, Haiti, Jamaica, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, and Trinidad and Tobago. In December 2000, Cuba was admitted into the ACP Group, bringing the number of Caribbean States to 16 and the total ACP Group membership to 78 (Cuba however is not yet a signatory to the Agreement). The 14 Pacific States are Cook Islands, Fiji, Kiribati, Marshall Islands, Micronesia (Federated States), Nauru, Niue, Palau, Papua New Guinea, Solomon Islands, Tonga, Tuvalu, Vanuatu and Samoa. The Democratic Republic of East Timor has requested membership in the ACP Group. The 15 EU Member States are Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden and the United Kingdom.

<sup>1</sup> The development cooperation between the EU and ACP States started in 1963 and was followed by successive conventions with the number of countries involved and scope of cooperation expanded on the part of the EU and ACP States as follows: 1963, First Yaoundé Convention (1963-1969) and 1969, Second Yaoundé Convention (1969-1975) between 6 EU States and 18 African States; 1975, First Lomé Convention (1975-1980) signed between 9 EU States and 46 ACP States, following the formation of the ACP Group in Georgetown (Guyana); 1979, Second Lomé Convention (1980-1985) signed between 9 EU States and 58 ACP States; 1984, Third Lomé Convention (1985-1990) signed between 9 EU States and 58 ACP States; and 1990, Fourth Lomé Convention (1990-2000) signed between 12 EU States and 68 ACP States. The Fourth Lomé Convention was in two periods, 1990-1994 and 1995-2000. Lomé IV *bis* was signed between 15 EU States and 70 ACP States (which became 71 with the addition of South Africa).

3. Regarding economic and trade cooperation, the main objectives under the Partnership Agreement (Article 34) are: (i) to promote smooth and gradual integration of ACP economies into the world economy; (ii) to enhance production, supply and trading capabilities; (iii) to create new trading dynamics and foster investment; and (iv) to ensure full conformity with WTO provisions, *including special and differential treatment* (emphasis added), and active participation in the multilateral trading system. Thus the new trading arrangements shall be built upon the following agreed key principles:

- (1) WTO compatibility (Articles 34:3, 36:1 and 4, 37:7 and 41);
- (2) special and differential treatment (SDT) as well as flexibility for the ACP States (Articles 34:4, 35:3, 37:7, 39:3, and 41:2);
- (3) preserving the *acquis* of the Lomé Conventions (Articles 35:1; 36:4, 37:7 and 9); and
- (4) preserving sub-regional and regional integration processes as the building blocks for ACP–EU trade relations (Articles 28, 29, 35:2, 37:3 and 5).

The emphasis given to the WTO compatibility of future trading arrangements between the EU and the ACP States derives from various factors. First, as WTO members the concerned majority of ACP States and the EU are under obligation to ensure the conformity of their trade policies with WTO obligations. Second, WTO compliance is necessary to avoid the past difficulties experienced by the EU (and ACP States) in securing GATT/WTO approval of the compatibility of the Lomé Conventions. The same rationale arises from the successive legal challenges made by some GATT/WTO Members on the EU's regime for the importation, distribution and sales of bananas. Third, the creation of WTO in 1995 with its rule-based nature, together with an enhanced dispute settlement mechanism, increased further the need for compatibility with the multilateral trading rules.

4. The multilateral rules face changes that may affect the outcome of ACP–EU trade negotiations and the flexibility for ACP States. The Fourth WTO Ministerial Conference held in Doha, Qatar, from 9–14 November 2001, agreed to launch new multilateral trade negotiations under the Doha work programme.<sup>2</sup> The Ministerial Declaration adopted on 14 November sets out various areas for negotiations, among which are 'rules' and 'special and differential treatment', to be completed as part of a single undertaking by 2005.<sup>3</sup> The Ministers agreed to 'negotiations aimed at clarifying and improving disciplines and procedures under the existing WTO provisions applying to regional trade agreements' while taking into account 'the developmental aspects of regional trade agreements' (paragraph 29). They also agreed that SDT 'are an integral part of the WTO Agreements' and that 'all special and differential treatment provisions shall be reviewed with a view to strengthening them and making them more precise, effective and operational' (paragraph 44).

5. This report aims to contribute to ACP States' preparation for negotiations with the EU, which started in September 2002, of new WTO-compatible trade arrangements. In particular, the report provides some suggestions on incorporating special and differential treatment into the WTO rules, taking advantage of the Doha multilateral negotiations to give concrete expression to the mandate that such negotiations 'take into account development aspects of regional trade agreements'. These suggestions are made pursuant to the request by ACP Trade Ministers to investigate possibilities for amending the relevant WTO rules to accommodate future WTO-compliant ACP–EU trading arrangements yet with flexibility for ACP States. The Declaration by the Third Meeting of ACP Ministers of Trade (ACP/61/903/00Rev.5, Brussels, 11–12 December 2000), mandated 'ACP representatives in Geneva to identify and examine those WTO provisions which should be modified to facilitate flexibility to be injected into the negotiations between the ACP and the EU'.

6. The report focuses on the negotiation and legal issues of ACP–EU trade arrangements and the relevant WTO rules and negotiations. It does not deal with the issue, although important, of the possible economic impact on ACP States of various trade arrangements especially reciprocity; nor

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<sup>2</sup> For a discussion of negotiating issues for developing countries, see UNCTAD (2000a).

<sup>3</sup> Ministerial Declaration adopted on 14 November 2001 (WT/MIN(01)/DEC/1), 20 November 2001.

does it address the specific design of each trading arrangement across different geographical regions.<sup>4</sup> Furthermore, the scope of the analysis is limited to trade in goods, hence the focus on Article XXIV of GATT 1994 although reference is made to trade in services and the requisite WTO provisions.

7. Chapter II reviews the options for new trading arrangements provided under the ACP–EU Partnership Agreement, and links these alternatives to possible WTO disciplines under which they would have to be notified by the parties and examined by the WTO Membership. These options relate to: (i) the continuation of non-reciprocal preferences for ACP States during a preparatory period lasting until December 2007; (ii) negotiations of economic partnership agreements (EPAs) to enter into effect from January 2008 or earlier; (iii) determination of alternative arrangements to EPAs for non-LDC ACP States that choose to remain outside of EPAs in 2004; and (iv) the provision of special preferential treatment for LDCs and also for small, landlocked and island ACP States.

8. Chapter III assesses the adequacy of existing WTO provisions in providing flexibly for developing countries under North–South RTAs constructed between developed and developing countries, and examines options for incorporating SDT provisions within such WTO rules. Among the possible options are reforming GATT Article XXIV, Part IV of GATT 1994 and the Enabling Clause. It is argued that there is compelling case for reforming Article XXIV of GATT 1994 to incorporate SDT in the form of either a generic paragraph and/or a specific redefinition of individual substantive and procedural requirements. Suggestions in this direction are provided.

9. Chapter IV explores the specific elements of ‘flexibility’ to be made available specifically for developing countries to enable them to meet the substantive and procedural requirements of GATT Article XXIV. It also examines possible modalities for reform in respect of individual requirements, particularly for: ‘substantially all the trade’ in internal trade liberalisation for which duties; the elimination of ‘other restrictive regulations of commerce’ (ORRCs); and the ‘reasonable length of time’ within which interim arrangements leading to free trade areas or customs unions ‘should exceed 10 years only in exceptional cases’. Since the overall degree of flexibility available to developing countries in respect of these and other requirements of GATT Article XXIV would depend critically on the definition of generally applicable flexibility (for all WTO Members) as well as concrete terms of ‘flexibility’ to be made available specifically to developing countries as SDT, both flexibilities would require operational definition through clarification and reinterpretation of relevant provisions.

10. In this report, the term ‘flexibility’ refers to a degree of policy discretion or deviation entitled explicitly or implicitly to parties to a trade agreement with regard to a given norm or rule under the agreement. ‘Flexibility’ is a generic term and does not presume asymmetry in the degree of discretion based on the level of development of individual parties to the agreement. It can therefore be applicable to developed countries as well. Special and differential treatment (SDT) refers to the modality of asymmetry, by granting a greater degree of flexibility, or differentiated and more favourable treatment for developing than for developed countries.

11. Chapter V summarises the key issues addressed in each chapter and highlights the main conclusions. The Doha work programme, with its ‘development focus’, provides a major opportunity for ACP States, together with the EU, to negotiate SDT into the WTO rules on RTAs, especially Article XXIV of GATT 1994. A change from non-reciprocal to reciprocal trade relations means that SDT for developing countries in WTO rules, such as ACP States, has to be defined in terms of asymmetric and differentiated application of some of the criteria for free trade areas (FTAs) and customs unions. Defining the modality and the level of ‘asymmetry’ would hold the key for the incorporation of a development dimension into WTO rules on RTAs. It should enable ACP States and

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<sup>4</sup> These will have to be addressed as the negotiations take place. The ACP ‘Negotiation Guidelines for EPAs’ advocates that such horizontal issues be addressed in a first phase of negotiations between September 2002 and September 2003; the actual tariff negotiations will take place thereafter. The guidelines were endorsed by the Third ACP Summit of Heads of State and Government in July 2002, Nadi, Fiji. For an assessment of the necessity of a two-stage approach to the ACP–EU negotiations, see ‘Non-Paper II on Negotiations on Economic Partnership Agreements’ by Mauritius, 17 May 2002.

their regional integration groupings to benefit from the future ACP–EU EPAs with flexibility for ACP States. It would also allow WTO members to update WTO rules on the phenomenon of North–South RTAs, and bridge the current lacuna in the WTO architecture with respect to special and differentiated treatment for developing country parties to such RTAs.

## Chapter II NEW ACP–EU TRADING ARRANGEMENTS AND WTO COMPATIBILITY

### II.1 THE LOMÉ CONVENTION AND WTO COMPATIBILITY

12. In agreeing on future trading arrangements, a major issue considered by ACP States and the EU has been the controversy with other GATT (1947) contracting parties over the compatibility with the GATT of the non-reciprocal trade preferences for ACP States extended by the EU under the Lomé Conventions.<sup>5</sup> The EU, supported by ACP States, consistently sought legal coverage of the First, Second and Third Lomé Conventions under Article XXIV of GATT 1947 (free trade areas and customs unions) read in conjunction with Part IV of GATT (trade and development), arguing that the trade provisions of the Lomé Convention provides a free trade area in the meaning of GATT Article XXIV, with special and differential treatment provided to ACP States in the meaning of GATT Article XXXVI:8 in Part IV on non-reciprocity (see Box 2).

#### **Box 2: Provisions of GATT Articles XXIV:8(b) and XXXVI:8**

Article XXIV:8 (b): ‘A free trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories’;

Article XXXVI:8: ‘The developed contracting countries do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of less-developed contracting parties’.

Interpretative note to Article XXXVI:8: ‘This paragraph would apply in the event of action under Article XVIII:A, Article XXVIII, Article XXVIII *bis*..., Article XXXIII, or any other procedures under this Agreement’.

13. In the GATT Working Party established to examine the First Lomé Convention, the parties invoked Part IV of GATT 1947 as the justification for not requesting reverse preferences from ACP States. They argued that the Lomé trading arrangements were compatible with their obligations under the GATT ‘in particular provisions of Articles I:2, XXIV and XXXVI, which had to be considered side by side and in conjunction with one another’.<sup>6</sup> Other GATT contracting parties did not share this view, arguing that the trade regime of the Lomé Convention was not consistent with GATT rules. They argued that the non-reciprocal preferences were neither extended to all developing countries and thus did not fulfil the obligations of generalised preferences (Part IV of GATT does not allow for discrimination among developing countries); nor could they be considered as free trade agreements because they were not reciprocal, i.e. they did not include reverse preferences extended by the ACP States for imports from the EU. These countries counter-argued that the trade provisions of the Lomé Convention were not consistent with Article XXIV and Part IV of GATT 1947 taken together or separately; the preferences were neither reciprocal in the sense of GATT Article XXIV, nor generalised in the sense of GATT Part IV (which incorporates the ‘most-favoured-nation’ (MFN) principle of GATT Article I:1).

<sup>5</sup> The Convention is typical of trade relations between developed and developing countries that have historically been built on four main pillars: (a) provision through preferences for improved market access into developed countries for products of developing countries; (b) non-reciprocity or less than full reciprocity in exchange of trade concessions; (c) flexibility in the application of trade rules and disciplines; and (d) maintenance of the value of commodity exports. These have often been provided under the coverage of special and differential treatment. The Convention is distinct from other preferences, however, in that it is contractually negotiated and agreed between the parties, normally for a duration of several years.

<sup>6</sup> GATT document BISD 23S/53 quoted in WTO (1995), p.15.

14. The legality of the Lomé Convention and the EU's thesis on the Convention's conformity with the GATT was further questioned in the 1990s in the context of a series of disputes concerning the EC's import regime for bananas (see Box 3). In the GATT dispute settlement case, *EEC-Member States' import regimes for bananas*, initiated by Colombia, Costa Rica, Guatemala, Nicaragua and Venezuela as claimants in February 1993 ('Bananas II'), the GATT Panel found that Part IV of the GATT was not intended to subtract from other GATT obligations – through discriminatory treatment, for example – and concluded that a legal cover for the tariff preferences (on bananas imported from ACP countries) under consideration could not be found in Article XXIV of GATT, or in Article XXIV of GATT read in conjunction with Part IV.<sup>7</sup> The Panel stated that the Convention could not be seen as a 'free trade area' in the sense of Article XXIV:8(b), as the subparagraph defines free trade area as 'a group of two or more customs territories in which the duties and other restrictive regulations of commerce ... are eliminated on substantially all the trade *between the constituent territories* in products originating in such territories' (emphasis added), with the plural of the term 'territories' and the word 'between' implying reciprocity in exchange of preferences. The panel also found that GATT Article XXXVI:8, read in conjunction with its endnote, is not applicable to trade negotiations undertaken outside the framework of GATT, as the endnote limits the applicability of the article to those procedures 'under this agreement'. The panel therefore recommended that the contracting parties, acting jointly, request the EEC to bring its measures into conformity with the GATT. The banana dispute led the EU to attempt various re-adjustments to its regime for the importation into and sales of bananas in the EU.

### Box 3: Background to the banana disputes

The EU banana dispute involved three separate GATT/WTO cases. The first two cases ('Bananas I and II') were initiated under GATT 1947 by five Latin American banana-supplying countries (Colombia, Cost Rica, Nicaragua, Venezuela and Guatemala). The Panel Report on Bananas I was published in May 1993 and that on Bananas II in January 1994, but neither report was adopted. The EC, under the positive consensus rule of GATT 1947, blocked the adoption of the first report, while discussions on the second report were suspended when GATT 1947 expired. The third dispute was raised in February 1996 under the WTO by Guatemala, Ecuador, Honduras, Mexico and the United States ('Bananas III'). The Panel Report was adopted in May 1997 and the Appellate Body Report in September 1997. The Bananas III case subsequently underwent a variety of steps foreseen under the Understanding on Rules and Procedures Governing the Settlement of Disputes (i.e. Article 21.3 (c) arbitration on implementation period, Article 21.5 panel on EU implementation measures, Article 22.6 arbitration on the level of suspension of concessions). It resulted in retaliation measures by the US and Ecuador being authorised by the Dispute Settlement Body in 1999 and 2000, respectively.<sup>8</sup>

15. Disagreement also persisted in the Working Party established to examine the Fourth Lomé Convention. Some countries not party to the Convention claimed that that the Convention would be in conformity with the provisions of the GATT only if the parties to the Convention were granted a waiver from their contractual obligations under the provisions of GATT Article XXV (joint action of contracting parties including granting of waiver), as was done for the United States' Caribbean Basin Initiative and Canada's CARIBCAN programme.<sup>9</sup> Historically, since the adoption of the Enabling Clause in 1979 that provided a permanent derogation for the Generalized System of Preferences (GSP) from GATT MFN principle (Article I:1),<sup>10</sup> most non-reciprocal and non-generalised preferential trading schemes, at the request of the preference-giving countries, have been waived by the GATT/WTO as legal exceptions to the basic GATT MFN principle of non-discrimination (GATT Article I).

16. Most waivers have been granted for periods of several years, subject to annual reviews. The waivers were requested and granted under GATT Article XXV and, after the formation of WTO, in

<sup>7</sup> GATT, *European Economic Communities – Import regime for bananas* (DS38/R), paragraphs 158-159.

<sup>8</sup> The banana dispute has stimulated a wealth of analyses and commentaries. See, for example, Komuro (2000).

<sup>9</sup> GATT document, 'Working Party on the Fourth ACP–EEC Convention of Lomé', (L/7502), 19 July 1994.

<sup>10</sup> Decision of 28 November 1979, 'Differential and more favourable treatment, reciprocity and fuller participation of developing countries' (L/4903).

accordance with the Understanding in Respect of Waivers and Article IX of the WTO Agreement. For example, the waiver duration for the United States' Caribbean Basin Economic Recovery Act (Caribbean Basin Initiative) is from 15 November 1995 to 31 December 2005; that of the US Andean Trade Preference Act (ATPA) was from 19 March 1992 to 4 December 2001; and that of the Canadian Trade, Investment and Industrial Cooperation programme (CARIBCAN) ran from 26 November 1986 to 15 June 1998, and was extended in October 1996, to 31 December 2006.

17. The EU and ACP States subsequently resorted to a GATT waiver to allow the EU to maintain the Lomé trade arrangements.<sup>11</sup> The GATT waiver from the obligation under Article I:1 of GATT was granted to the EU to apply the Fourth Lomé Convention from 9 December 1994 until 20 February 2000,<sup>12</sup> the expiry date of the Convention. The decision to grant the waiver noted that the parties to the Convention made the request for a waiver without prejudice to their position that the Convention was entirely compatible with their obligations under GATT Article XXIV in the light of Part IV of GATT.

18. In the course of ACP–EU negotiations on the successor agreement to the Fourth Lomé Convention, attempts were made to find solutions that were WTO compatible and sufficiently flexible for ACP States, accompanied by adjustment measures. Several suggestions on the new ACP–EU trading arrangements were provided by the EC in its Green Paper in 1996.<sup>13</sup> These options primary characteristics centred on compliance with the relevant provisions of WTO, and on building ACP regional integration processes.<sup>14</sup> The EU also conducted a series of impact studies of possible regional economic partnership agreements, involving reciprocal trade preferences, between selected ACP regions (Eastern, Western, Southern and Central Africa; the Caribbean; the Pacific) and the EU.<sup>15</sup>

19. The emphasis on WTO compatibility in the search for alternative trade regimes was shaped, *inter alia*, by the difficulties encountered by the EU in justifying the Lomé Convention as compatible with GATT rules and the banana disputes. They were also shaped by the assessment in the Green Paper and other studies that despite preferences and apart from the beneficiaries of the commodity protocols, ACP States in general had not achieved substantial market penetration in the EU nor substantial transformation of their economies based on the exploitation of their preferred status in the EU market. Nonetheless, the debate and controversy over the impact of non-reciprocal preferences and their effective utilisation by beneficiary countries is far from conclusively established.<sup>16</sup> The contribution of the unique system of development cooperation under the Lomé Conventions, including trade preferences and commodity protocols, may have been modest in that it had not promoted industrial transformation in all ACP States. However, it is not certain either whether, without Conventions, the trade and development performance of ACP States would have been better, especially given the magnitude of structural supply and demand constraints faced by ACP economies.

## II.2 THE ACP–EU PARTNERSHIP AGREEMENT AND WTO COMPATIBILITY

### II.2(a) Continuation of non-reciprocal preferences and commodity protocols

20. At the conclusion of the ACP–EU negotiations on a successor agreement to the Fourth Lomé Convention, the parties could not agree on a completely new and WTO-compatible trading regime to replace the system of non-reciprocal trade preferences and commodity protocols. As an interim

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<sup>11</sup> For a discussion of the waiver granted to the Fourth Lomé Convention, see Grynberg (1998).

<sup>12</sup> GATT, The fourth ACP–EEC Convention of Lomé: Decision of 9 December 1994 (L/7604), 19 December 1994.

<sup>13</sup> European Commission, *Green Paper on relations between the European union and the ACP countries on the eve of the 21st century - Challenges and options for a new partnership* (COM(96)570 final), Brussels, 20 November 1996.

<sup>14</sup> For an initial assessment of the EC's proposal, see Lecomte (1998).

<sup>15</sup> For an assessment of the results of these impact studies, see for example McQueen (1999).

<sup>16</sup> See, for example, EC, 'Analysis of Trends in the Lomé Trade Regime and the Consequences of Retaining It', mimeo; Tangermann (2000), and Onguglo (1999).

measure, the parties agreed under the Partnership Agreement (Article 36) to continue for a *preparatory period* that is scheduled to last until 31 December 2007, the system of non-reciprocal preferences.<sup>17</sup> Thus the continuation of non-reciprocal trade preferences constitutes one pillar, although a transitory one, of the economic and trade cooperation under the ACP–EU Partnership Agreement.

21. The Lomé Convention provided that all ACP industrial products and most agricultural products could enter the EU duty free. Specifically, all industrial products under chapters 25–97 of the Combined Nomenclature are exempted from customs duties, and 80% of agricultural products under chapters 1–24 of the Combined Nomenclature are totally liberalised. Together, around 92% of products originating in ACP States enter the EU without duty and with quota.<sup>18</sup> For agricultural products, some improvements were agreed upon under the new Partnership Agreement.<sup>19</sup> The special protocols for sugar and beef also remain in force, while the rum protocol expired. The banana protocol was not renewed and the EU has established a new banana regime. In respect of the future of the arrangements for sugar, beef and bananas, it was agreed that they would be reviewed in the context of the new ACP–EU trading arrangements with a view to ensuring their compatibility with WTO rules.<sup>20</sup> What this will mean in practice needs to be examined closely by ACP States.

22. To continue the Lomé-type non-reciprocal tariff preferences, the EU required a WTO waiver (see Table 1 on different trade preferences and respective GATT/WTO provisions). Thus the EU, with the support of the United Republic of Tanzania and Jamaica acting on behalf of the ACP States, submitted a new waiver request to the WTO in March 2000 under Article IX of the WTO Agreement<sup>21</sup> (see Box 4 on the stringency of waiver provisions under the WTO as compared to GATT 1947). The waiver was initially requested only for GATT Article I:1 derogation, as was done for the Fourth Lomé Convention. Given the legal ambiguity as to whether the waiver from Article I:1 of GATT 1994 would effectively cover also the preferential treatment in quota allocation in the EU's new banana regime, as agreed at the end of disputes with the US and Ecuador (upon mutual agreement with the two countries on 11 and 30 April 2001, respectively),<sup>22</sup> in June 2001 the EU also requested another waiver for its banana import regime until 2005, when it would be converted into a tariff-only system, from obligations under Article XIII of the GATT 1994 (non-discriminatory administration of quantitative restriction).<sup>23</sup> There followed a long delay in launching the examination of the waiver requests owing to both procedural and substantive matters raised by some WTO members, such as the translation of the entire Partnership Agreement into all three official languages

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<sup>17</sup> The relevant text in the Cotonou Agreement (Article 36:3) provides that 'in order to facilitate the transition to the new trading arrangements, the non-reciprocal trade preferences applied under the Fourth ACP–EC Convention shall be maintained during the preparatory period for all ACP countries, under the conditions defined in Annex V to this Agreement'.

<sup>18</sup> EC, *op. cit.* ('Analysis of Trends in the Lomé Trade Regime and the Consequences of Retaining It', mimeo).

<sup>19</sup> See Tangermann (2000), *op. cit.*, and Shirotori (2000).

<sup>20</sup> The relevant text in the Cotonou Agreement (Article 36:4) is: 'In this context, the Parties reaffirm the importance of the commodity protocols, attached to Annex V of this Agreement. They agree on the need to review them in the context of the new trading arrangements, in particular as regards their compatibility with WTO rules, with a view to safeguarding the benefits derived therefrom, bearing in mind the special legal status of the Sugar Protocol'.

<sup>21</sup> Request for a WTO waiver: New ACP–EC Partnership Agreement (G/C/W/187), 2 March 2000.

<sup>22</sup> In requesting a waiver for the Partnership Agreement's transitional trade arrangement it was also important to ensure that all preferential treatment and measures in favour of ACP States applied by the EU be effectively covered by the waiver, so as to preclude any legal challenge under the dispute settlement mechanism as has been the case with the EC banana disputes. In this dispute case on the *EC–Regime for importation, sale and distribution of bananas*, the scope of the GATT waiver for the Lomé Convention was the subject of dispute. While the EC argued that all preferential measures provided for ACP bananas in terms of tariff treatment (GATT Article I), tariff quota allocation (GATT Article XIII) and import licence allocation should be justified by the waiver, the Appellate Body found that the waiver could only cover the derogation from GATT Article I:1 obligation and not other provisions (see Report of the Appellate Body, *EC–Regime for importation, sale and distribution of bananas*, WT/DS27/AB/R, 9 September 1997).

<sup>23</sup> *Requests for a GATT Article I and a GATT Article XIII waiver: New ACP–EU Partnership Agreement* (G/C/W/269), 27 June 2001.

of the WTO. Moreover, the rapidly evolving convention of arriving at all WTO decisions through consensus had increased the uncertainty regarding the outcome of the waiver requests.

**Table 1.** Preferential trading schemes and their coverage under WTO provisions

	<b>NON-RECIPROCAL</b>	<b>RECIPROCAL</b>		
<b>GENERALIZED</b>	<u>Generalised non-reciprocal preferences</u> → <b>Enabling Clause: 2(a) (d)</b> - <i>GSP*</i> <i>Special LDC preferences (e.g. Everything-but-arms, EBA)</i>	<u>Generalised (i.e. multilateral) reciprocal tariff reduction</u> → <b>GATT I:1 (MFN) and GATT XXVIII bis</b>		
<b>NON-GENERALIZED</b>	<u>Non-generalised non-reciprocal preferences</u> → <b>Waiver</b> - <i>ACP–EU Partnership Agreement (during preparatory period up to 2007)</i> - Fourth Lomé Convention - US CBI - US ATPA - CARIBCAN - LDC preferences granted by developing countries**	<u>Non-generalised reciprocal preferences = FTAs, CUs and interim arrangements</u> <b>GATT XXIV or Enabling Clause: 2(c) (d)</b>		
			DDCs	DCs
		DDCs	<b>GATT XXIV</b>	<b>GATT XXIV EPAs</b>
	DCs	<b>GATT XXIV EPAs</b>	<b>Enabling Clause</b>	

**Note:** Options provided under the ACP–EU Partnership Agreement are indicated in *italics*. DDCs stands for developed country members of a regional trade agreement (FTA or CU); and DCs for developing country members.

\* The proposed ‘enhanced GSP option’ may violate the Enabling Clause if preferences are ‘enhanced’ only for ACP countries in a discriminatory manner, without being extended to non-ACP developing countries.

\*\* Special LDC preferences given by developing countries have been granted a GATT waiver (‘Preferential Tariff Treatment for Least-Developed Countries’ Decision on Waiver adopted on 15 June 1999 (WT/L/304)), since coverage of such preferences under the Enabling Clause proved to be contentious.

#### **Box 4: Waiver provisions under WTO**

The use of waivers has been circumscribed by the Uruguay Round Understanding in Respect of Waivers of Obligations under the GATT 1994 and Article IX: 3-4 of the Marrakesh Agreement establishing the WTO. Members requesting a waiver must justify it with sound economic analysis and arguments, undergo a complex process of requesting WTO authorisation, and abide by stringent conditions for maintaining the waiver if it stretches over several years, including annual reviews by the WTO. The waiver under WTO has to be approved by three-fourths of WTO members, as compared to two-thirds under GATT 1947. This procedure for obtaining a waiver under WTO rules is a good deal more onerous than was the case under GATT 1947 when the Lomé Convention waiver was obtained. Thus, in general, WTO members will not be able to easily obtain waivers. A multi-year waiver until December 2007 has been secured from the Doha WTO Ministerial Conference for the continuation of the Lomé-type preferences, so that annual reviews apply. This introduces an element of uncertainty over the longevity of the preferences, which is not conducive to investor and trader confidence.

23. The two waiver requests were considered and finally granted by the Fourth WTO Ministerial Conference on 14 November 2001.<sup>24</sup> The two decisions on the GATT waivers, namely ‘European Communities – the ACP–EC Partnership Agreement: Decision of 14 November’ (GATT 1994 Article I Waiver)<sup>25</sup> and ‘European Communities – Transitional Regime for the EC Autonomous Tariff Rate Quotas on Imports of Bananas: Decision of 14 November 2001’ (GATT 1994 Article XIII waiver),<sup>26</sup>

<sup>24</sup> For a review of the ACP Group’s initiatives in securing the WTO waiver, see for example, Julian (2001).

<sup>25</sup> *European Communities – The ACP–EC Partnership Agreement: Decision of 14 November 2001* (WT/MIN(01)/15), 14 November 2001.

<sup>26</sup> *European Communities – Transitional Regime for the EC Autonomous Tariff Rate Quotas on Imports of Bananas: Decision of 14 November 2001* (WT/MIN(01)/16), 14 November 2001.

were adopted following strong lobbying by the ACP States, in coordination with the EU. They waive obligations accruing to the EU under Article I:1 and Article XIII:1 and 2 of GATT 1994, respectively. The GATT Article I waiver exempts the EU from its MFN obligation under paragraph 1 of Article I of GATT 1994 until 31 December 2007, to the extent necessary to permit the EU to provide preferential tariff treatment for ACP products as provided under relevant provisions of the ACP–EU Partnership Agreement (Article 36.3, Annex V and Protocol). The EU and ACP States would enter into consultation, upon request, promptly with any interested WTO Members with respect to any difficulty that may arise as a result of the implementation of preferential tariff treatment. In the event that mutually satisfactory solutions failed to be agreed, the concerned Members may bring the matter to the WTO General Council, which will examine the case and formulate recommendations promptly. Such a consultation mechanism does not, however, preclude the right of affected Members to have recourse to the dispute settlement mechanism pursuant to Articles XXII and XXIII of GATT 1994.

24. The reform of the EU banana import regime as a result of the agreement reached with the US and Ecuador contains special provisions as set out in the two waiver decisions adopted by the Doha Ministerial Conference. The aspects relating to discriminatory quantitative restrictions under the current EU banana regime are covered by a GATT Article XIII waiver as of 1 January 2002 until 31 December 2005, when the EU banana regime will be converted into a tariff-only regime. The preferential tariff treatment for ACP bananas is covered by GATT Article I waiver until 31 December 2007, like other products, although such treatment would be subject to a special arbitration system set forth in an annex to the waiver (see Box 5). The waiver of the banana regime exempts the EU from its obligations under paragraphs 1 and 2 of Article XIII of GATT 1994 during that period with respect to the EU's separate tariff quota of 750,000 tonnes (designated quota 'C') for bananas of ACP origin. As a part of its reform process, the EU would negotiate with interested parties by 31 December 2005 new MFN tariffs and the rebinding of the tariffs in accordance with GATT Article XXVIII (modification of schedules). In this respect, the GATT Article I waiver noted that the tariffs applied to bananas imported under quotas 'A' and 'B' shall not exceed EUR 75 per tonne until 2006, that preferential treatment for ACP bananas might be affected as a result of the GATT Article XXVIII negotiations, and that the EU and ACP States had given the assurance that the rebinding of the EU tariff on bananas under GATT Article XXVIII procedures would result in at least maintaining total market access for MFN banana suppliers. This means that the EU had agreed to put in place such new MFN tariff rates on bananas that would guarantee current market access opportunities for non-ACP banana exporters no less favourable than those currently available to them.<sup>27</sup>

25. During the preparatory period until 2007, the ACP States need to build up their capacity for competitiveness and regional integration (Article 37:3, Partnership Agreement). In respect of competitiveness, their enterprises have to make effective use of the preferences, build up production and capture more market share in the EU. This can be encouraged by means of removing residual non-tariff barriers on agricultural exports, liberalising the rules of origin, simplifying the procedures for applying such rules, and raising awareness among ACP economic operators about the

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<sup>27</sup> Following a mutual understanding reached in April 2001 between the EU on the one hand, and Ecuador and the US on the other, in the context of the protracted banana dispute, and against the backdrop of the trade sanctions imposed by the US and Ecuador on EU exports since April and May 1999, respectively, the EU has instituted a new interim regime for importation of bananas based on three tariff rate quotas, designated 'A', 'B' and 'C', for the period up to 31 December 2005. The interim regime will be replaced by a tariff-only regime as of 1 January 2006 at the latest, upon negotiations with interested parties under GATT XXVIII. The tariff quota A of 2,200,000 tonnes at a MFN rate of EUR 75 per tonne is bound in the WTO. An autonomous quota B of 353,000 tonnes at the rate of EUR 75 per tonne is opened to cater for the increase in consumption in the EU resulting from its enlargement in 1995. The two quotas are managed as one and is open to bananas from all sources. The third autonomous tariff quota C of 850,000 tonnes is reserved for bananas of ACP origin. The interim regime is being implemented in two stages. In Phase I, a modified banana regime based on historical allocation of licences started on 1 July 2001 with the adoption of the Commission Regulation No. 896/01. Phase II started as from 1 January 2002, wherein 100,000 tonnes were transferred from the C quota to the B quota, and the remaining 750,000 tonnes of the C quota were reserved for ACP bananas. The reservation of the C quota for ACP bananas necessitated Article XIII waiver to be granted to the arrangement. With the implementation of phase II, the US and Ecuador lifted trade sanctions.

preferences.<sup>28</sup> In addition, greater emphasis needs to be placed on strengthening the quality and efficiency of their production and on diversification into agro-based industries and other dynamic export sectors including services. These are conditions *sine qua non* for benefiting from the maintaining the status quo during the preparatory period between 2000 and 2007. They should also be considered as integral elements of any adjustment programme to be developed under the ACP–EU Partnership Agreement in support of ACP States in moving from the system of non-reciprocal trade preferences to reciprocal preferences.

#### **Box 5: Arbitration system on banana under GATT 1994 Article I waiver**

The GATT 1994 Article I waiver applies to preferential tariff treatment for all products including bananas. For bananas, the waiver applies to preferential tariff treatment provided under the current tariff quota system, as well as to the future tariff-only regime. In order to ensure the orderly transition to the tariff-only regime, the Article I waiver sets forth a special arbitration mechanism in the application by the EU of a tariff-only regime, which is to be implemented no later than 1 January 2006. The purpose of the arbitration mechanism is to ensure that the market access opportunities for MFN suppliers be guaranteed at least at the presently prevailing level. The EU and ACP States would initiate consultations with MFN banana exporters to the EU ‘early enough’ to finalise the process at least three months before the entry into force of the new EU tariff-only regime (i.e. 30 September 2005). This process would start 10 days after the conclusion of GATT 1994 Article XXVIII negotiations, when EU would inform interested parties of its intention regarding the EU’s tariff rebinding on bananas. Within 60 days of such an announcement, any interested party could request arbitration (first arbitration). The arbitrator would be appointed within 10 days following the request subject to agreement by the two parties, or by the Director-General of the WTO following consultations within 30 days. The mandate of the arbitrator would be to determine, within 90 days of his appointment, whether the envisaged rebinding of the EU’s tariffs on bananas would result in at least maintaining total market access for MFN banana suppliers. If the arbitrator finds the negative, the EU would be required to rectify the matter. Within 10 days of the arbitration award to the WTO General Council, the EU would enter into consultation with interested parties that requested the arbitration. In the event that no satisfactory solution is found, the same arbitrator would be requested to determine within 30 days whether the EU had rectified the matter (second arbitration). The second arbitration award would be notified to the WTO General Council. If the EU fails to rectify the matter, the GATT Article I waiver would cease to apply to bananas upon entry into force of the new EU tariff regime. Both the GATT Article XXVIII negotiations and the arbitration procedures should be concluded before the entry into force of the new EU tariff-only regime on 1 January 2006.

26. There are additional considerations for ACP States with respect to the trade preferences. First, the competitive advantages enjoyed by ACP States in the EU market are being progressively diluted over the medium term owing to the erosion of margins of preferences as the EU implements and deepens its MFN tariff liberalisation under the WTO, including under the reform process necessitated by the WTO Agreement on Agriculture. Second, textile and clothing exporters should expect strong competition from non-ACP producers, especially low-cost Asian producers, as the programmed elimination of the EU’s multi-fibre arrangement is effected over the 10 years up to the year 2005, in accordance with the WTO Agreement on Textiles and Clothing. Third, ACP States should be prepared to face direct competition from the non-ACP LDCs that would benefit from the preferential EBA market access into the EU and potential trade diversion in products like clothing and processed fish. Fourth, a similar concern arises from the EU’s GSP scheme, which has adopted a ‘positive incentive scheme’ whereby an additional margin of preference is granted to those beneficiary countries that meet non-trade criteria related to international labour standards, the environment and fight against illegal narcotic drug production. Fifth, ACP States could face greater competition from countries in Latin America, North Africa and elsewhere with whom the EU is negotiating or has concluded free trade agreements, allowing competitive products from these countries to enter duty-free into the EU.

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<sup>28</sup> For a discussion of measures to increase utilisation of preferences, see, for example, UNCTAD (2001a).

## II.2(b) Economic Partnership Agreements (EPAs)

27. During the preparatory period described above, ACP States and the EU would negotiate new and permanent trading arrangements to take effect at the end of the preparatory period. The parties agreed on a general framework for new economic and trade relations, whose modalities would be defined through consultations and negotiations. *Thus a second pillar of the framework provided by the ACP–EU Partnership Agreement is a built-in agenda for the ACP States and the EU to establish new trading arrangements within a preparatory period of 8 years, starting from March 2000* (Articles 36 and 37, Partnership Agreement). These new WTO-compatible and appropriately flexible trading arrangements are broadly defined as ‘*economic partnership agreements*’ (EPAs). The EPAs would be comprehensive in scope, covering trade in goods (Articles 37 and 38, Partnership Agreement), and would be extended to cover the liberalisation of services and the building of service supply capacity of ACP States relating to labour, business, distribution, finance, tourism, culture, and construction and related engineering services (Article 41:4 and 5, Partnership Agreement). The parties would also promote the liberalisation of maritime transport (Article 42, Partnership Agreement). ACP–EU cooperation is also mandated in trade-related areas such as competition policy, protection of intellectual property rights, standardisation and certification, sanitary and phytosanitary measures, trade and environment, and trade and labour standards (Articles 44–52, Partnership Agreement).

28. The EPAs will be negotiated during the preparatory period and take effect from 1 January 2008 (Article 37:1, Partnership Agreement). The formal negotiations on the EPAs commenced on 27 September 2002. They are to be undertaken by ACP States that consider themselves in a position to do so, i.e. not necessarily all ACP States, and primarily the non-LDC ACP States; at a level they consider appropriate and in accordance with the procedures set by the ACP Group (Article 37:5, Partnership Agreement). These procedures have not yet been defined, but the possibilities include bilateral EU–individual ACP State EPAs, regional EPAs between the EU and ACP sub-regional economic communities, or an EU and ACP-wide arrangement. Such EPAs aim at progressively removing barriers to trade between the concerned ACP States and EU, i.e. reciprocal free trade in line with relevant WTO provisions, namely on RTAs. However, the EPAs would also be as flexible as possible in establishing the duration of a sufficient transitional period, the final product coverage, taking into account sensitive sectors, and the degree of asymmetry in the timetable for dismantling tariffs (Article 37:7, Partnership Agreement). This flexibility is not a withdrawal from reciprocity; it merely provides for differentiated application of reciprocal trade liberalisation commitments. Thus the EU would be expected to offer immediate liberalisation to ACP States while the latter would grant reciprocal liberalisation to EU exports after a certain transitional period.<sup>29</sup> The EU and ACP States are committed to defending the ‘flexibility’ aspects of the EPAs in the WTO (Article 37:8, Partnership Agreement).

29. As the EPAs imply the formation of free trade agreements, and the EU being a ‘developed’ territory is a party, the relevant WTO rule is Article XXIV of GATT 1994 on free trade agreements, customs unions and interim arrangements leading either to a free trade area or customs union, and the Understanding on the Interpretation of Article XXIV of the GATT 1994 (hereinafter the 1994 Understanding). While RTAs comprising only developing countries are under the purview of the Enabling Clause, the involvement of at least one developed country would place the RTA under the scope of Article XXIV of GATT 1994 (see Tables 1 and 2). Indeed, recent mixed North–South agreements have been notified under Article XXIV of GATT 1994.<sup>30</sup>

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<sup>29</sup> Some EU States have suggested that the initial offer to ACP States would be an extension of EBA to all ACP States, but through negotiations.

<sup>30</sup> These include FTAs concluded by EU with Algeria, Egypt, Jordan, Lebanon, Morocco, the Palestinian Authority, certain Overseas Countries and Territories, Syria, and Tunisia; those concluded by EFTA with Morocco and the Palestinian Authority; US–Jordan FTA; Canada–Chile FTA; and those formed by Singapore with Japan, EFTA and New Zealand. For a discussion of issues arising from trends towards North–South RTAs, see UNCTAD (2001b).

**Table 2.** GATT/WTO coverage of regional trade agreements (RTAs) by membership

Types of RTA	GATT/WTO coverage
<b>RTAs among developed countries only</b> - EU, EFTA, etc.	<b>Article XXIV</b>
<b>RTAs involving both developed and developing countries ('Mixed RTAs')</b> - EPA ; EU-Morocco ; EU-Tunisia ; EU-Mercosur; EU-Gulf Cooperation Council (GCC), EU-South Africa; US-Jordan; Canada-Chile, etc.	<b><u>Article XXIV</u></b>
<b>RTAs among developing countries only</b> - Mercosur ; GCC ; COMESA; UEMOA ; Melanesian Spearhead Group, etc.	<b>Enabling Clause</b>

30. This has an important implication in determining the WTO-compatibility of EPAs, as the substantive and procedural requirements of GATT 1994 Article XXIV are significantly more stringent than those of the Enabling Clause. As shown in Table 3, the main WTO requirements for free trade areas stipulated by Article XXIV of GATT are substantial trade coverage (Article XXIV:8), no raising of trade barriers against third countries (Article XXIV:5), a 10-year transitional period for interim agreements leading to the creation of the free trade area or customs union (XXIV:5(c), as clarified by the 1994 Understanding), notification to the WTO and examination of conformity, and biennial reporting on the operation of the concerned entity. The WTO Council for Trade in Goods receives the notified agreement and transmits it to the Committee on Regional Trade Agreements (CRTA) to undertake the examination of such agreements in terms of their conformity with the relevant WTO rules.

**Table 3.** Comparison of requirements under GATT Article XXIV and the Enabling Clause

	<b>ARTICLE XXIV of GATT 1994</b>	<b>ENABLING CLAUSE</b>
Purpose	To facilitate trade between members and not to raise barriers to the trade of third countries. (XXIV:4)	To facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties of trade of third country (para. 3). To respond positively to the development, financial and trade needs of developing countries (in the case of preferences given by developed countries)
Trade Coverage	Duties and other restrictive regulations of commerce (ORRC) should be eliminated on 'substantially all the trade' among parties. (XXIV:8 (a)(i) and (b))	Not applicable.
Level of barriers to third countries	Duties and other regulations of commerce (ORC) shall not 'on the whole be higher or more restrictive' than those applicable prior to the formation of an RTA (XXIV:5(a) (b))	Not applicable. [Not to constitute an impediment to tariff reduction or elimination on a MFN basis.]
Interim agreement/ Transitional period	Interim agreement should include a plan and schedule for the formation of an FTA or CU, and should exceed 10 years only in 'exceptional cases' ('reasonable length of time') (XXIV:5(c) and 1994 Understanding, para. 3)	Not applicable.
Compensation to third countries	GATT Article XXVIII procedure is required for modification of schedule in the case of customs unions (XXIV:6 and 1994 Understanding, paras. 4-6)	Not applicable
Notification	Notification to the Council for Trade in Goods (XXIV:7(a)) Any change in an interim agreement is to be notified to the CTG. Consultation may be undertaken upon request (XXIV:7(c))	Notification to the Committee on Trade and Development (CTD) when created, modified or withdrawn.
Examination and recommend	Examination by the CRTA that would report to the CTG. The CTG may make recommendations. (XXIV:7(a) and 1994 Understanding, para. 7). The	The CTD may establish a working party (or refer to the CRTA) to examine a RTA notified thereunder.

ation	CTG may, if deemed necessary, make recommendations for interim agreements, in particular on the proposed timeframe and on measures required (XXIV:7(b)(c) and 1994 Understanding, paras. 8-10)	
Periodical reporting	Biennial reporting is required on the operation of regional trade agreements (1994 Understanding, para. 11)	Not applicable.
Dispute settlement	The DSU* is applicable to any matter relating to GATT Article XXIV (1994 Understanding, para. 12)	Prompt consultations are to be afforded at the request of any country (DSU applicable as part of GATT 1994)

\* DSU: Understanding on Rules and Procedures Governing the Settlement of Disputes.

### **Box 6: Coverage of the Enabling Clause and a WTO waiver for South–South trade preferences**

The Enabling Clause, formally the ‘Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries – Decision of 28 November 1979’ adopted in the context of the GATT Tokyo Round negotiations, was not affected by the Uruguay Round and continues to operate as part of GATT 1994 in its original form. It provides legal coverage for both reciprocal and non-reciprocal preferential trade arrangements involving developing countries. Paragraph 1 of the Enabling Clause allows WTO members to provide differential and more favourable treatment to developing countries without according such treatment to other WTO members, thus deviating from the MFN principle of non-discrimination (GATT Article I). Paragraph 2 identifies specific situations in which this permission is granted. These include: (i) preferences provided by developed countries under GSP (paragraph 2(a)); (ii) ‘regional trade arrangements among developing countries on a regional or global basis involving the preferential reduction or elimination of tariffs’ (paragraph 2(c)); and (iii) special treatment of LDCs ‘in the context of any general or specific measures in favour of developing countries’ (paragraph 2(d)).

On the basis of paragraph 2, GSP schemes are permanently derogated from the GATT MFN clause, as are various South–South regional trade agreements as well as the Global System of Trade Preferences (GSTP) among developing countries. Paragraph 2(d) also authorises the special treatment for LDCs in so far as they are provided ‘in the context of any general or specific measures in favour of developing countries’: i.e. either within the framework of the GSP or any regional and global arrangements among developing countries like the GSTP. Questions arise in this regard as to whether special treatment of LDCs granted outside the context of ‘general or specific measures in favour of developing countries’ is permitted under paragraph 2(d) of the Enabling Clause. This issue was raised when the WTO membership considered extending enhanced market access conditions for LDCs in the context of the High-Level Meeting on Integrated Initiatives for LDCs’ Trade Development, held in Geneva on 27-28 October 1997. The grant of special LDC preferences by some advanced developing countries, which avail themselves of neither GSP scheme nor regional or global trade arrangements, were considered not covered by the Enabling Clause. A waiver from the MFN clause (GATT I:1) was thus deemed necessary. The waiver was adopted on 15 June 1999 to allow for developing country Members to provide preferential tariff treatment to products of LDCs until 30 June 2009 on a non-discriminatory basis.<sup>31</sup> It was significant that the decision noted that the waiver was granted ‘without prejudice to Members’ rights in their actions pursuant to the provisions of’ the Enabling Clause. This implies that developing countries are still free to provide special preferences only to the selected LDCs with whom they have a regional or global trade arrangement.

31. In contrast with GATT Article XXIV, the requirements of the Enabling Clause are significantly less stringent in both substantive and procedural terms. The only substantive requirement is that the developing country trade agreements shall be designed to facilitate and promote the trade of members, and not raise barriers or create undue difficulties for the trade of third countries, and that they shall not constitute an impediment to the reduction or elimination of tariffs and other restrictions

<sup>31</sup> ‘Preferential Tariff Treatment for Least-Developed Countries: decision on waiver adopted on 15 June 1999’ (WT/L/304)). For initiatives taken under this waiver, see *GSP Newsletters* Nos. 1–5, which are posted on the UNCTAD website: [www.unctad.org/Templates/Page.asp?intItemID=1418&lang=1](http://www.unctad.org/Templates/Page.asp?intItemID=1418&lang=1)

to trade on an MFN basis. The procedural requirement involves notification to the Committee on Trade and Development under the WTO when they are created, modified or withdrawn. The Committee may (or may not) establish a working party upon the request of any interested member to examine the trade agreement in the light of the relevant provisions of the Enabling Clause.<sup>32</sup> These provisions clearly offer more flexibility than those of GATT Article XXIV; there is no corresponding requirements as in GATT Article XXIV on ‘substantially all the trade’, time limitations for interim agreements, or biennial reporting requirements. This is in large part because the purpose of the Enabling Clause is to operationalise and provide legal cover to the principle of SDT, including ‘non-reciprocity (or lesser market opening)’ in trade negotiations, as provided in Article XXXVI:8 in Part IV of GATT, whether it relates to reciprocal (regional agreements) or non-reciprocal preferential schemes (GSP) involving developing countries (see Box 6). Since the adoption of the Enabling Clause, ACP sub-regional groupings have been notified under its provisions.<sup>33</sup>

32. Economic integration agreements concerning trade in services are notified to the Council for Trade in Services, which refers them to the Committee on Regional Trade Agreements (CRTA) for examination. The ACP–EU Partnership Agreement also foresees that the services sector will eventually be integrated into the EPAs and, accordingly, the relevant integration agreement(s) must conform to Article V of the General Agreement on Trade in Services (GATS). The requirements under Article V of GATS parallel those articulated in Article XXIV of GATT 1994, namely ‘substantial sectoral coverage’ (GATS V:1(a)) and ‘the absence or elimination of substantially all discrimination’ (GATS V:1(b)).<sup>34</sup> However, Article V:3(a) of GATS provides scope for SDT for developing countries by recognising that flexibility shall be provided to developing countries with regard to both criteria.

33. EPAs would be negotiated between the EU on the one hand, and individual ACP States, or the ACP States as a group, or ACP sub-regional groupings on the other. The formation of bilateral free trade areas between the individual ACP States and the EU thus is a possibility, which may emerge for especially large ACP economies. The EU and South Africa already have an agreement including bilateral free trade. However, such a series of separate ACP–EU bilateral negotiations would place the ACP States in a disadvantageous bargaining position; it would deprive the ACP of its political weight as a distinct negotiating group. The ACP Group identity could become a casualty and with it there is an increased potential for unequal treatment and trade and investment diversion between the different ACP–EU agreements. It may also lead to complex debate among the involved parties over the balancing of the spread of benefits and costs of free trade within and between the different agreements (and regions). In addition, the extensive GATT Article XXIV review process in the WTO for the 70-plus separate agreements would represent a major administrative and costly burden for all parties and the EU in particular. A major negotiation burden would be faced by the EU

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<sup>32</sup> MERCOSUR was notified under the Enabling Clause but is being examined in the CRTA under both the Enabling Clause and GATT Article XXIV. This is a unique situation that has not been applied to any other notified developing country grouping since 1979. During discussions in the fourth session of the CRTA on 28 April 1997, MERCOSUR stated that it was willing to review the application of, and undertake consultations thereon, the common external tariff adopted in December 1993, pursuant to paragraph 4 of the Enabling Clause and Article XXVIII of GATT 1947 (i.e. modification of the schedule of concessions) at that time. The choice of Article XXVIII was presumably to engage in compensatory negotiations with third parties as a result of the establishment of common external tariff. The US, however, contested the claim that the Enabling Clause did not provide sufficient legal basis to launch Article XXVIII negotiations, in contrast with Article XXIV, which provides in its paragraph 6 for such compensation negotiations (WT/COMTD/1/Add.10, 28 April 1997).

<sup>33</sup> Sub-regional ACP groupings notified under the Enabling Clause include COMESA, the Trade Agreement among the Melanesian Spearhead Group Countries and the West African Economic and Monetary Union (UEMOA). The Caribbean Community and Common Market (CARICOM) was notified under GATT Article XXIV in 14 October 1974, most likely because the Enabling Clause did not yet exist.

<sup>34</sup> For a discussion of services trade liberalisation in regional context, see Mattoo and Fink (2002).

(and ACP States) in defending the numerous bilateral agreements and to secure, ideally, the adoption of positive conclusive reports on their WTO conformity.<sup>35</sup>

34. There is the possibility for the ACP States to negotiate and conclude a single free trade agreement at the ACP level, under the Enabling Clause conditions as a South– South RTA before concluding the same with the EU. The ACP Trade Ministers and Heads of State and Government (including at their Third Summit) have called for further examination of this option. It allows ACP States to negotiate with the EU as a single group (notwithstanding the absence of a common external tariff), thereby strengthening the group’s bargaining position in seeking better conditions from the EU while maintaining the homogeneity of the ACP Group and defending more effectively the EPA in the WTO. However, it will be difficult for the ACP States to agree on a single plan and schedule for mutual free trade with similar commitments for each partner country in view of the wide differences in their levels of development and factor endowments. Moreover, the expected benefits of free trade are not likely to be seen in all ACP States, considering the wide geographical dispersion of these countries and their costly and weak transportation links.

35. Another option is the formation and consolidation of regional and sub-regional free trade agreements and customs unions within the ACP Group, which could become the building block for negotiation of EPAs with the EU.<sup>36</sup> Such agreements already exist in all ACP regions, but at varying stages of development. These include CARICOM in the Caribbean; CEMAC, COMESA, EAC, ECCAS, ECOWAS, IOC, UEMOA and SADC in Africa as well as at the continental level, the African Economic Community which has been subsumed into the newly created African Union and its New Partnership for Africa’s Development (NEPAD) programme; and the Melanesian Spearhead Group among some Pacific ACP countries as well as the initiation of the Pacific Island Countries Trade Agreement (PICTA). These groupings, with fully-fledged free trade agreements or customs unions, would then be in a stronger bargaining position to enter into free trade agreements with the EU. This option combines the advantages of consolidating sub-regional integration processes within ACP regions as a first step (which is also one of the key objectives of the ACP–EU Partnership Agreement), and between these groups and the EU as a second step. The definition of ACP regions for the purpose of EPAs is complicated, especially in Africa, due to the existence of several overlapping regional groupings, and by the exercise to define ACP ‘geographical regions’ for the purposes of receiving EU development assistance under the new partnership. This option suffers from the reduced bargaining power on the part of individual ACP sub-regional groupings compared with those of the ACP as a single negotiating body.

36. It needs also to be noted that under a free trade agreement, as distinct from a customs union, each member maintains its own external trade policy *vis-à-vis* third countries without common external tariffs in place at the sub-regional/regional level. In such a situation, the market access negotiations may have to be conducted with the EU on an individual country-by-country basis.<sup>37</sup> Therefore, a customs union would be in a better position in ensuring better bargaining power arising from collective bargaining as a group. Indeed, most sub-regional/regional groupings with which the EU has been undertaking negotiations with a view to forming free trade agreements are customs

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<sup>35</sup> The CRTA has so far failed to adopt recommendations on the WTO-conformity of notified RTAs whose examinations it has completed. The ineffectiveness of the CRTA examination procedure was a major reason for the inclusion of WTO rules on RTAs in the WTO Doha work programme.

<sup>36</sup> In this alternative, greater EU financial and technical support would be provided to the ACP FTAs to assist their member States in implementing the agreements and, as necessary, customs union programmes in an expeditious manner and notifying them to the WTO. Such assistance should be forthcoming under the Partnership Agreement (Articles 29 and 29).

<sup>37</sup> EFTA is a notable example of an FTA extending the network of FTAs as a group with third countries. Regarding agricultural products, each EFTA Member State concluded separate country-specific bilateral agreements with third parties, which were then incorporated into the main FTA agreements, as agricultural policies differ across EFTA members.

unions (i.e. MERCOSUR and the Gulf Cooperation Council, GCC).<sup>38</sup> In the ACP Group, UEMOA member States have succeeded in creating a customs union and operate a common external tariff.

37. In order to compensate disadvantages associated with each of the above three options in terms of the reduced bargaining power of the ACP Group, and technical difficulties in negotiating a single ACP free trade area, a possible option is to negotiate as a package a ‘single umbrella agreement’ between the ACP Group and the EU. Such an umbrella agreement would provide general principles and guidance for all individual EPAs, as well as the enhanced GSP or special LDC preferences. It would serve to avoid the marginalisation in the negotiation of any ACP country or region, while leaving market access negotiations to either individual ACP States or sub-regional groupings.<sup>39</sup> The strategy may run the risk of delaying negotiations pending the conclusion of the last single economic partnership agreement between the EU and ACP country or region as a single undertaking. This approach is apparent in the agreement between the EU and ACP States on a two-phase negotiation structure, with cross-cutting issues to be addressed in the first phase from September 2002, and the second phase from September 2003 to focus on regional-based negotiations.

38. In the case of EPAs being formed between the EU and a series of ACP sub-regional groupings, which as South–South RTAs, are or will be formed under the Enabling Clause conditions, a legal question arises with regard to the WTO compatibility of the resulting EPAs. Since South–South RTAs, be they free trade agreements or customs unions, would very likely not fulfil the requirements provided under GATT Article XXIV, the question is whether the resulting EPAs that include such ‘GATT Article XXIV-minus’ features could be considered as conforming to the stringent provisions of GATT Article XXIV.

39. Almost by definition, the WTO-compatibility of an EPA involving a ‘GATT Article XXIV-minus’ group on the one hand, and a GATT Article XXIV group on the other is contestable under current GATT Article XXIV provisions unless the EPAs would undertake thorough liberalisation among those ACP States party to the agreement, as well as with the EU. The EU is currently negotiating free trade agreements with MERCOSUR, GCC and the Southern African Customs Union (SACU). Since MERCOSUR and GCC have been notified under the Enabling Clause, the examination of EU–MERCOSUR/GCC agreements by the CRTA upon conclusion and notification to the WTO would provide some indication of the WTO compatibility of future mixed RTAs involving South–South sub-regional groupings. In the interim, it can be surmised that if the approach of utilising sub-regional ACP groupings (i.e. GATT Article XXIV-minus agreements) as a building block for negotiating EPAs with the EU (GATT Article XXIV agreement) is to be WTO consistent, it may be necessary to reform some of the provisions relating to Article XXIV of GATT 1994 to include elements of flexibility through SDT (see Chapter III).

## II.2(c) Alternative Trading Arrangements

40. The EPAs may not be accepted by all ACP States. The ACP–EU Partnership Agreement thus provides that in 2004 the EU ‘will assess the situation of the non-LDCs which, after consultations with the Community decide that they are not in a position to enter into economic partnership agreements and will examine all alternative possibilities, in order to provide these countries with a new framework for trade which is equivalent to their existing situation and in conformity with WTO rules’ (Article 37:6). Thus, *a third pillar of the trade framework in the ACP–EU Partnership Agreement is a built-in provision for the EU to elaborate, via consultations, alternative trading arrangements for non-LDC ACP States that decide not to enter into EPAs.* This rendezvous clause takes effect two years after the start of EPA negotiations, coinciding with the EU’s review of its GSP scheme.

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<sup>38</sup> MERCOSUR and the Unified Economic Agreement among Member States of the GCC (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates) were notified to the GATT/WTO under the Enabling Clause on 5 March 1992 and 11 October 1984, respectively.

<sup>39</sup> For details, see Bernal (2000).

41. One likely alternative is that these non-LDC ACP countries could be accorded preferences under an enhanced GSP scheme of the EU, to offset the lost preferences. The GSP scheme is offered to all developing countries, including those not members of the ACP Group (except for those excluded or graduated from the schemes for a variety of reasons), subject to meeting certain conditions. This is a unilateral measure, whereas the Lomé Conventions and the ACP–EU Partnership Agreement are negotiated contractual undertakings between the two parties. GSP preference-giving countries are free to provide, modify or withdraw unilateral preferences. They have also practised selective granting of preferences in a non-generalised manner, instituted various ‘graduation’ clauses to exclude more competitive beneficiaries, and have often attached non-trade conditionalities (related to environmental, public health and social concerns) for granting additional margins of preferences (i.e. ‘positive incentive schemes’). GSP schemes are permitted by the 1979 Enabling Clause (paragraph 2(a), as noted in Table 1). The preferences are allowed under WTO to the extent that they are provided on a generalised basis without discrimination among developing countries. The only exception permitted is special preferences for LDCs (paragraph 2(d)). The Enabling Clause therefore provides a negative right for preference-giving developed countries (and some transition economies) to derogate from the MFN clause of GATT Article I:1 to the extent that preferences are given in a generalised manner within the framework of the GSP. It does not create a positive legal obligation to preference giving countries to do so.

42. The application of the GSP option to non-LDC ACP States raises policy and legal issues as to its modalities. If a level of trade ‘equivalent to their existing situation’ (Article 37.6, Partnership Agreement) is to be provided to those ACP States that choose this option, the GSP preference would need to be enhanced as the GSP offers a lesser degree of preferences than are currently available under the Partnership Agreement in terms of preference margin and product coverage. However, the difficulty arises in reconciling EU’s legal obligations under the Partnership Agreement and the WTO.<sup>40</sup> Two modalities are conceivable.

43. The first modality would consist of a general enhancement of EU’s GSP scheme, whereby the ACP States would receive under the GSP ‘enhanced’ preferential treatment together with other non-ACP developing countries in such a way that there is no difference between ACP and non-ACP countries in terms of the level of preferential treatment, in conformity with the non-discrimination obligation under WTO. In this case, the ACP States receiving enhanced GSP would lose their competitive edge *vis-à-vis* non-ACP GSP-eligible developing countries, as the latter would receive the same preferences. It is questionable whether the EU would be deemed to have fulfilled its legal obligation *vis-à-vis* ACP States under the terms of Article 37:6 of the Partnership Agreement, as the situation involves the loss of preference edge *vis-à-vis* non-ACP GSP beneficiary countries, and could be deemed by ACP States as a market access situation that is not ‘equivalent to their existing situation’.

44. The second modality would consist of differentiated enhancement of GSP preferences in favour of ACP States that opt for the option, so as to preserve eventually the competitive edge they have enjoyed *vis-à-vis* non-ACP GSP beneficiary countries. However, the problem with this modality is that it is incompatible with WTO rules on generalised treatment for GSP schemes. In practice, the EU has provided non-generalised preferences under its GSP scheme for countries meeting certain non-economic criteria such as combating drug production and trafficking, environmental and core labour standards. However, non-ACP GSP-beneficiary developing countries are increasingly sensitive to the adverse effects accruing from such differentiation of GSP preferences, and have started to contest their WTO-compatibility.

45. The EU GSP scheme has recently experienced a multitude of complaints launched by non-ACP developing countries. The first WTO dispute procedure on the GSP was launched by Brazil against the EU’s GSP scheme, which granted discriminatory preferential treatment to soluble coffee

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<sup>40</sup> Huber (2000).

imported from Andean countries under the positive incentive scheme for combating drug production (see Box 6).<sup>41</sup> Although this dispute ended with a mutually agreed solution between the two parties, the concern over the WTO consistency of such positive incentive schemes seems to have led the EU to seek a WTO waiver from Article I:1 of GATT 1994 for its scheme applicable to countries combating drug production and trafficking, effective from January 2002 to December 2004.<sup>42</sup> Another dispute involved tuna products from Thailand. During discussions for the granting of the two waivers regarding the Partnership Agreement at the Doha Ministerial Conference, Thailand and the Philippines expressed concerns over the discriminatory treatment of their tuna exports under the EU's GSP scheme. Subsequently, Thailand launched the dispute settlement procedure on 6 December 2001 by requesting consultations with the EU.<sup>43</sup> India launched another complaint on 5 March 2002 with regard to the EU's positive incentive schemes for combating drug production and trafficking, and promoting labour and environmental standards.<sup>44</sup> Both Thailand and India argued that the discriminatory provision of preferences under EU's positive incentive scheme violated Article I of GATT 1994 and the Enabling Clause (paragraphs 2(a), 3(a) and 3(c)). After failing to reach a mutually satisfactory solution through consultations, on 9 December 2002 India requested the establishment of panel to examine, *inter alia*, 'whether (i) the provisions of the EC GSP scheme granting tariff preferences under the special arrangements for combating drug production and trafficking and the special incentive arrangements for the protection of labour rights and the environment' are compatible with Article I:1 of GATT 1994 and the above provisions of the Enabling Clause.<sup>45</sup> It is therefore highly probable that enhancing the GSP benefits only to non-LDC ACP States will be challenged as WTO incompatible by other countries, including the beneficiaries of the ordinary GSP scheme.

46. The contractual nature of the preferences is another issue relating to the 'equivalence' of the Lomé Conventions/Partnership Agreement tariff preferences and the enhanced-GSP option. The unilateral character of GSP preferences might not be seen *a priori* as 'equivalent' to those of the Lomé Conventions/Partnership Agreement even if the level of preferences in terms of margins and coverage are such as to be deemed essentially equivalent under both schemes. The contractual nature of the Lomé Conventions and now the Partnership Agreement have guaranteed predictability and legal security in the preferential market access for ACP State products, thus allowing long-term production and investment planning. From the users' point of view, a major deficiency of GSP schemes has been their unilateral and time-bound character, which has rendered it difficult for beneficiaries to utilise effectively the preferences available under the scheme. If 'equivalence' is to be attained substantially between the current situation of ACP States and the enhanced-GSP option, some sort of 'contractuality' or 'binding' has to be introduced in the enhanced GSP scheme. However, the modality for binding unilateral preferences, including enhanced preferences for some countries, as well as its status under the WTO, is yet to be explored. The enhanced-GSP option thus has to be carefully considered by those non-LDC ACP States that decide to avoid the EPA option.

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<sup>41</sup> *European Communities – Measures affecting soluble coffee: Request for consultations by Brazil*, WT/DS209/1, 19 October 2000.

<sup>42</sup> *Request for a WTO waiver - New EC special tariff arrangements to combat drug production and trafficking* (G/C/W/328). Proposed eligible countries include Bolivia, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Pakistan, Panama, Peru and Venezuela.

<sup>43</sup> *European Communities – Generalized System of Preferences: Request for consultations by Thailand*, WT/DS242/1, 12 December 2001.

<sup>44</sup> *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries: Request for consultations by India*, WT/DS246/1, 12 March 2002.

<sup>45</sup> *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries: Request for establishment of a panel by India*, WT/DS246/4, 9 December 2002.

**Box 7: Challenge by Brazil of the EU's GSP scheme:  
'Measures affecting soluble coffee'**

On 12 October 2000, Brazil requested consultations with the European Commission regarding measures applied under the EC's GSP scheme that affects imports of soluble coffee originating in Brazil, contained in Council Regulation (EC) No. 1256/96, dated 20 June 1996, and current Council Regulation (EC) No. 2820/98, dated 21 December 1998. The measures in question included, first, the 'graduation' mechanism, which progressively and selectively reduces or eliminates preferences granted to specific products and/or beneficiary countries under the GSP scheme; in the case of Brazilian soluble coffee, preferential treatment has been progressively reduced and finally eliminated on 1 January 1999. Second, the 'drugs regime', which confers special preferential treatment for products originating in the Andean and Central American Common Market countries that are conducting campaigns to combat drugs. In the case of soluble coffee, this special preferential treatment currently amounts to duty-free access of exports originating in those countries into the EU market.

The first measure, the graduation mechanism, is applied in most GSP schemes, whereby those beneficiary countries that are considered to have attained a certain level of economic development (often linked with a set of indicators such as GDP) are excluded from the preferential treatment of their exports on a product-by-product basis, or in total. The second, 'positive incentive measures', are specific to the EC's GSP scheme, and are designed to promote non-trade policy objectives such as improvements in labour rights, the environment or public health by providing additional margins of preferences to those GSP beneficiary countries that meet the conditions. As a result of these two measures, Brazil is the only major supplier facing 9% duty instead of the 0 and 3.5% duties applicable to other major suppliers. Brazil considered that the above measures, both separately and jointly, adversely affected the importation into the EU of soluble coffee originating in Brazil, and claimed that they were inconsistent with the obligations of the EC under the 1979 Decision of the GATT Contracting Parties on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries (Enabling Clause), as incorporated in GATT 1994, and under Article I of GATT 1994. Brazil also held the view that these measures nullified or impaired the benefits accruing to Brazil directly or indirectly under the cited provisions. Later, Ecuador requested to join the consultations (WT/DS209/2).

The dispute was settled in July 2001 via bilateral consultations with an agreement that the EU provides greater access to Brazilian and others' soluble coffee by creating another tariff quota under which imports from all sources are given duty-free treatment, thereby reducing the duty applicable to Brazilian coffee from the current 9%. The level of quota would be gradually increased, to 10,000 tonnes in the first year, 12,000 tonnes in the second year and 14,000 tonnes in third year. Other preferential regimes would not be affected by the tariff rate quota. Brazil then withdrew its complaint.

47. Finally, in 2006 (i.e. two years prior to the official closure of the EPA negotiations), a formal and comprehensive review of the new trading arrangements will be carried out by ACP States and the EU, although regular reviews could be conducted in the interim period (Article 37:4, Partnership Agreement). By 31 December 2007, the negotiations on EPAs will have been concluded. So, starting in 2002 with the launch of official negotiations, and every two years thereafter, the ACP States and the EU will jointly review and adjust the negotiations on EPAs and any alternative trading arrangement.

#### **II.2(d) Special treatment for LDCs**

48. A fourth pillar of the ACP-EU Partnership Agreement covers special provisions for ACP LDCs and, in fact, all other LDCs. In this regard, the ACP States and the EU have agreed that they will 'start by the year 2000, a process which by the end of the multilateral trade negotiations and at the latest 2005 will allow duty free access for essentially all products from all LDCs, building on the level of the existing trade provisions of the Fourth ACP-EC Convention' (Article 37:9, Partnership Agreement). In addition, the new regime for LDCs will simplify and review the rules of origin, including the cumulation provisions that apply to LDC exports. This LDC initiative seeks to avoid the problem of WTO consistency by extending unilateral EU trade preferences to all LDCs, including

those that are not members of the ACP Group (there are at present nine LDCs that are not ACP States).<sup>46</sup>

49. Subsequently, in September 2000, the European Commission tabled a major market access initiative for LDCs entitled 'Everything but Arms' (EBA).<sup>47</sup> The initiative was discussed, revised and finally adopted by the EU Council of Ministers and entered into force on 5 March 2001. The EBA was enacted by Council Regulation No. 416/2001 of 28 February 2001, amending EC Regulation No. 2820/98, applying a multi-annual scheme of generalised tariff preferences for the period 1 July 1999 to 31 December 2001. The EBA is an improvement on the EU's GSP scheme and has to be notified under the Enabling Clause. Under the EBA, the EU would provide duty-free market access without any quantitative restrictions for all goods exported by all the 49 LDCs established by the United Nations, with the permanent exception of arms and munitions (25 tariff lines), and temporarily excluding three sensitive agricultural products – bananas, sugar and rice.<sup>48</sup> The liberalisation concerns agricultural products, primarily meat and daily products, beverages and milled products.<sup>49</sup>

50. The EBA, like the GSP scheme, allows for diagonal cumulation of local contents between the LDCs and ASEAN, SAARC and the EU. The EBA, unlike the time-bound GSP scheme, will be maintained indefinitely, although the EU will undertake a review in 2005 to introduce amendments as necessary. The EBA is an extension of the GSP scheme, and is thus subjected similar non-trade conditions with respect to the temporary withdrawal, in part or in whole, of the preferences, and to a safeguard clause against a surge of imports that causes or threatens to cause injury to an EU producer of a like product. However, in the EBA initiative the safeguard clause has been modified to allow the European Commission to react swiftly when the Community's financial interests are at stake, such as in the event of massive import surge, and to suspend the preferences provided for rice, sugar and bananas under the EBA in the event of serious disturbances caused by imports.

51. The EBA initiative is an enlightened step in providing market access for LDCs. However, the initiative has important implications for the trade of the commodity-dependent ACP States which under the present arrangement benefit from carefully crafted systems of tariffs, quotas and licensing regimes. Furthermore, the EBA initiative is a unilateral act of the EU, undertaken without prior consultation with the ACP States. Indeed, non-LDC ACP States have argued that the EBA initiative should not lead to the erosion of the market access conditions they already enjoy. For example, the declaration adopted by the Third ACP Trade Ministers Meeting in December 2000, stated that ministers '*welcome and support* the initiative of the Commission of the European Community to grant from 2001 duty and quota free access to all products, except arms, from all LDCs (EBA Initiative), *respecting existing Agreements*' (emphasis added); and '*urge* that the EBA Initiative takes into account the vulnerability of Small, Landlocked and Island ACP States'. Additional complications will arise from the intended reform of the EU's Common Agricultural Policy, which will focus on a generalised lowering of guaranteed prices rather than on restricting imports.

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<sup>46</sup> Unilateral trade preferences extended by developed countries to LDCs (but not in the same form to other developing countries) are WTO legal under paragraph 2(d) of the 1979 Enabling Clause, which allows for 'special treatment of the least developed among the developing countries in the context of any general or specific measures in favour of developing countries' (GATT, BISD, 26th Supplement, p.203, Geneva, March 1980).

<sup>47</sup> See the EU Commission's website, [www.europa.eu.int/comm/trade/miti/devel/eba.htm](http://www.europa.eu.int/comm/trade/miti/devel/eba.htm), for details of the EBA.

<sup>48</sup> The LCD market access conditions for sensitive products will be gradually liberalised as follows. Duties on bananas will be gradually eliminated, with annual reductions of 20%, starting on 1 January 2002 and reaching full liberalisation by 1 January 2006. Duties on rice will be phased down between 1 September 2006 and 1 September 2009. Similarly, duties on sugar will be fully liberalised between 1 July 2006 and 1 July 2009. Specifically, EU duties on rice will be reduced by 20% on 1 September 2006, by 50% on 1 September 2007 and by 80% on 1 September 2008. During this period, LDCs can export rice duty free to the EU within the limits of a tariff quota. The initial quantities of this quota will be based on best LDC export levels to the EU in the recent past, plus a growth factor of 15%. The quota will grow every year, from 2,517 tonnes (husked-rice equivalent) in 2001/2002 to 6,696 tonnes in 2008/2009 (September to August marketing year). With regard to sugar during the transitional period, LDCs can export raw sugar duty free to the EU within the limits of a tariff quota, which will be increased from 74,185 tonnes (white-sugar equivalent) in 2001/2002 to 197,255 tonnes in 2008/2009. The provisions of the ACP-EC Sugar Protocol remain valid.

<sup>49</sup> For an assessment of EBA, see UNCTAD and the Commonwealth Secretariat (2001).

52. Apart from the content of the LDC preferences, their actual utilisation by LDCs raises two key issues. First, issues pertaining to the real value and stability of the market access concessions will have to be analyzed in-depth, taking into account a variety of factors. These factors include: (a) product coverage, longevity and applicable rules of origin; (b) assessment of the possible increase in market access opportunities in contrast with those already available to LDCs under various arrangements; and (c) consideration for other measures that could hinder LDCs from effectively utilising the increased market access conditions such as stringent sanitary and phytosanitary (SPS) measures and technical product standards.<sup>50</sup>

53. Second, the legal framework that would bind the trade preferences for the LDCs and provide stable market access conditions within the WTO has yet to be considered by WTO members. The LDC unilateral preferences in terms of WTO compatibility is covered, as noted, by the Enabling Clause. Moreover, they are consistent with the decision taken by the WTO First Ministerial Conference in 1996 on a Plan for LDCs, which was followed up with the High-Level Meeting on Integrated Initiatives for Least-Developed Countries' Trade Development held in October 1997 in Geneva. However, LDCs continue to demand the binding of these unilateral preferences within the WTO to ensure the stability and longevity of the preferences. Thus some new legal instrument is needed to provide coverage for the special preferences for the LDCs that would render special LDC preferences legally binding contractual obligation for developed countries.<sup>51</sup>

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<sup>50</sup> For a discussion on the effective utilisation of unilateral preferences, see UNCTAD (2001a).

<sup>51</sup> For a discussion of possible instruments see Onguglo and Ito (2001), and Inama (2002).

### Chapter III

## SPECIAL AND DIFFERENTIAL TREATMENT IN THE WTO PROVISIONS ON REGIONAL TRADE AGREEMENTS

54. The option of EPAs under the ACP–EU Partnership Agreement presents a key challenge for ACP States. The challenge is particularly significant with regard to the design of the adequate terms of reciprocity and flexibility *vis-à-vis* the EU (in contrast with the traditional system of non-reciprocal preferences), while ensuring compliance with prevailing WTO disciplines. This chapter focuses on EPAs and the flexibility therein, and examining ways to cater for such flexibility through adequate SDT provisions in relevant WTO rules. The question it seeks to address is whether existing WTO rules on regional trade agreements provide adequate legal coverage for the degree of flexibility required by ACP States under EPAs and, if not, how the WTO rules could be best modified to provide special and differential treatment (SDT) applicable to developing countries in the context of North–South RTAs. The reform of the WTO rules also needs to respond to the systemic need for disciplining RTAs so that they serve as building (and not stumbling) blocks for international trade.

### III.1 FLEXIBILITY FOR ACP STATES UNDER EPAS

55. The ACP–EU Partnership Agreement provides with respect to EPAs that these shall be WTO compatible. The negotiations on EPAs shall aim notably at establishing the timetable for the progressive removal of barriers to trade between the parties, in accordance with the relevant WTO rules (Article 37:7, Partnership Agreement). It is implicit in these provisions that the core of EPAs will comprise reciprocal free trade agreements that would fully conform to prevailing WTO disciplines. Full reciprocity and the resulting liberalisation of trade on the part of ACP States, however, would place higher economic, fiscal and social adjustment costs on ACP States given their level of development. In particular, given their generally high level of tariff structure and dependence on tariffs for government revenue on the part of ACP States, it has been estimated that EPAs would entail a risk of major tariff revenue shift (loss) from ACP governments to EU producers.<sup>52</sup> Thus it may be unsustainable for a number of ACP States to open their markets in full reciprocity with the EU, without any accompanying adjustment measures, as the adjustment costs would be the greatest for them, particularly for LDCs (that chose the EPA option over the EBA), and small and vulnerable States.

56. Accordingly, in the area of economic and trade cooperation, the ACP–EU Partnership Agreement recognises that special and differential treatment is a key principle for ACP States in general (Article 34:4, Partnership Agreement), and for ACP LDCs, taking due account of the vulnerability of small, landlocked and island countries (Article 35:3, Partnership Agreement). Specifically in respect of EPAs, ‘negotiations shall take account of the level of development and the socio-economic impact of trade measures on ACP countries, and their capacity to adapt and adjust their economies to the liberalisation process. Negotiations will therefore be as flexible as possible in establishing the duration of a sufficient transitional period, the final product coverage, taking into account sensitive sectors, and the degree of asymmetry in terms of timetable for tariff dismantling, while remaining in conformity with WTO rules *then prevailing*’ (Article 37:7, Partnership Agreement; emphasis added).<sup>53</sup> SDT in the context of EPAs is hence defined in terms of the ‘flexibility’ of the transitional period (both duration and asymmetry) and the final product coverage, taking into account sensitive sectors.

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<sup>52</sup> Winters (2002); Davenport (2002).

<sup>53</sup> As defined in Chapter I, ‘flexibility’ refers to a degree of policy discretion entitled to parties to a trade agreement with regard to its provisions and does not presume asymmetrical treatment between parties to the agreement. However, when applied to the modality of trade negotiations, where reciprocity is the norm, it may amount to SDT as the deviation from reciprocity would lead to certain asymmetry between the negotiating parties in the level of rights and obligations.

57. Under the ACP–EU Partnership Agreement, the concrete and detailed terms of EPAs, including greater flexibility for ACP States, are to be negotiated between the two parties. EPAs that provide greater flexibility for ACP States may or may not be WTO compatible depending, first, on how the terms of the flexibility are defined and agreed under the EPAs; and second, how the maximum scope of flexibility permissible under an RTA is defined in the WTO rules. The first element pertains to ACP–EU negotiations, and the second to WTO rules. Both the elements of flexibility in EPAs for ACP States and WTO rules on RTAs are presently the subject of parallel negotiations with the multilateral disciplines. This situation poses a major challenge for both ACP States and the EU.

58. The Doha multilateral negotiations are scheduled to be concluded by December 2004, whereas those for EPAs are scheduled for conclusion by December 2007. In this light, there is uncertainty with regard to the form and the level of (regional) flexibility needed for ACP States under EPAs, which would eventually be covered under the multilateral disciplines. The ACP States and the EU could be in a situation whereby they are faced with multilateral negotiations without knowing *a priori* the detailed features and the degree of (greater) flexibility and SDT deemed necessary for ACP States under EPAs, and which would finally be adopted by the two parties for the EPAs (unless such determination has been agreed upon by the parties prior to the conclusion of the Doha negotiations). In addition, such flexibility might entail measures that may not be strictly WTO-compatible under the existing terms of WTO provisions, such as much longer transitional periods for a significant number of products, or trade coverage significantly lower than average for other RTAs excluding major sensitive sectors. If this is the case, then the parties would have to defend these SDT provisions under EPAs in the WTO, as well as modify the WTO rules to allow for flexibility for ACP States under EPAs. In view of this possibility, under the ACP–EU Partnership Agreement there is agreement that, ‘(t)he Parties shall closely cooperate and collaborate in the WTO with a view to defending the arrangements reached, in particular with regard to the degree of flexibility available’ (Article 37:8). The need therefore arises to ensure that any flexibility deemed necessary for ACP States under EPAs would be appropriately covered under WTO rules ‘then prevailing’ (i.e. by 2008).<sup>58</sup> In the same vein, in a paper on ‘Implications of Multilateral Trade Rules for the Cotonou Partnership Agreement’, Ambassador Ali Said Mchumo of the United Republic of Tanzania argued the case as follows:<sup>54</sup>

‘As for the EPA option, the main rules relating to the formation of regional preferential arrangements in the area of trade in goods are contained in Article XXIV of the GATT, which requires participating countries to conform to two conditions. First, that the arrangements should cover ‘substantially all the trade’ between the constituent countries. Second, that imports from third parties be subject to tariffs no higher than those prevailing prior to the arrangement. The rules also allow gradual and progressive removal of tariffs and other barriers, over a period that would ‘exceed 10 years only in exceptional cases’. These rules were adopted at a time when such arrangements were being negotiated mainly between developed countries. Acknowledging the rigidity of the rules, developing countries that form regional groups among themselves have been allowed to do so under the Enabling Clause instead. Deliberations in the CRTA suggest that the legal situation on RTAs is not fully clear. Consequently, ACP countries must participate more actively in the work of the Committee to safeguard their interests. If REPAs (regional economic partnership agreements) are to be viable trading arrangements between the EU and the ACP, their legal basis (Article XXIV) must be revisited to, *inter alia*, allow non-reciprocity between developed and developing countries, and a set of corollary conditions created. These would include the development of supply-side and export capacity, human resource development and improvement of ACP competitiveness’.

59. At the political level, ACP Trade Ministers have taken the view that WTO provisions on RTAs require adjustment to incorporate the SDT required by ACP States in forming new trade agreements with the EU. The Third Meeting of ACP Trade Ministers in December 2000 reiterated the principle of flexibility in the ACP–EU new trade arrangements, and called for such flexibility to be reflected in the WTO rules governing RTAs, i.e. Article XXIV of GATT and Article V of GATS. The Ministers directed the ACP Group to seek to ‘modify’ these

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<sup>54</sup> Mchumo (2000).

WTO provisions to provide coverage for the flexibility required by ACP States. The Fourth ACP Trade Ministers Meeting, in preparation for the Fourth WTO Ministerial Conference, reiterated on 7 November 2001 that ‘multilateral rules should provide adequate flexibility to enable the ACP States to advance their interests when concluding WTO compatible trading arrangements with the European Union or any country or group of countries’.<sup>55</sup> Likewise, a High-Level Brainstorming Meeting for African Trade Negotiators Preparatory to the Fourth WTO Ministerial Conference in June 2000 recommended that ‘Co-operation in international fora is one of the main avenues of economic and trade co-operation in the ACP/EU Partnership Agreement. Accordingly, the ACP and EU countries should work together at the WTO on matters of mutual concern, including a review of GATT Article XXIV, to make it more development friendly’.

### III.2 DOHA DEVELOPMENT AGENDA ON WTO RULES ON RTAS

60. At the Fourth WTO Ministerial Conference, Ministers agreed *inter alia* to launch new multilateral ‘negotiations aimed at clarifying and improving disciplines and procedures under the existing WTO provisions applying to regional trade agreements. The negotiations shall take into account the developmental aspects of regional trade agreements’.<sup>56</sup> The Ministers also ‘reaffirm that provisions for special and differential treatment are an integral part of the WTO Agreements.... We therefore agree that all special and differential treatment provisions shall be reviewed with a view to strengthening them and making them more precise, effective and operational’.<sup>57</sup> The negotiations are to be completed as part of a single undertaking by early 2005.

61. A major rationale for opening negotiations on WTO rules on RTAs has been to enhance the supervisory function of the WTO to discipline RTAs, rather than to institute more flexibility in the WTO rules. This arose from the experience under the previous GATT 1947 and the WTO in that the rules on RTAs have been highly ineffective in disciplining the formation and operation of an ever-increasing number of RTAs. More RTAs have been created in the eight years following the formation of the WTO than in the 50 years of the existence of the former GATT. Between 1945 and 1995, some 125 RTAs were notified to the GATT, of which some 50 agreements are still operational. In contrast, between 1995 and 2002, some 250 agreements were notified to the WTO, about 168 of which are currently in force. Moreover, the examination of WTO compatibility of RTAs is proceeding slowly in the CRTA, the WTO body responsible for the task. More seriously, there has been a deadlock in respect of issuing reports on the conformity or not of examined RTAs.

62. Given the ambiguity in some of these key requirements and the resulting inability of Members to conclude on the WTO compatibility of notified RTAs that were exhaustively examined, proposals were made during the preparatory process for the Third WTO Ministerial Conference in 1999 with a view to clarifying Article XXIV of GATT 1994. Those include proposals by Australia, Hong Kong (China), Hungary, Jamaica, Japan, Korea, Romania and Turkey (for summaries of these proposals, see Annex 1).<sup>58</sup> Most of these proposals, with the exception of the one by Jamaica, call for instituting more transparent and stringent multilateral rules governing RTAs. This is because those WTO Members that attach primary importance to the process of multilateral liberalisation – notably Hong Kong-China, Japan, Korea, and Australia – have been pursuing the approach of clarifying the meaning of ambiguities in the WTO rules with a view to affirming the supremacy of the multilateral

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<sup>55</sup> Declaration by the Ministers Responsible for Trade of the African, Caribbean and Pacific Group of States on the Fourth World Trade Organization (WTO) Ministerial Conference (ACP/61/132/01[final]), Brussels, 7 November 2001.

<sup>56</sup> Ministerial Declaration adopted 14 November 2001 (WT/MIN(01)/DEC/1), 20 November 2001, paragraph 29.

<sup>57</sup> *Ibid.*, paragraph 44.

<sup>58</sup> As of December 2002, five proposals were submitted to the Negotiating Group on Rules by four WTO Members: Australia (2 proposals), the EC, Chile and Turkey (see Annex 1).

trading system.<sup>59</sup> Conversely, WTO Members party to a multitude of RTAs sought to safeguard their interest through, for instance, ‘grandfathering’ existing agreements and de-linking the examination of the agreements from the consideration of systemic issues in the CRTA (Hungary, Turkey and Romania). Jamaica’s proposal calls for a re-examination of Article XXIV of GATT 1994 for RTAs that involve developing country members with a view to providing these countries with adequate scope for absorbing the adjustment costs of trade liberalisation and for rendering a sustained contribution to their economic development.

63. The Doha agenda for multilateral negotiations on RTAs is approached by some WTO members to address the uncertainties in the WTO rules that contribute to delaying the conclusion of examination of notified RTAs by rendering the rules and examination process more explicit and stringent. They aim to enhance the supervisory function of the WTO in disciplining RTAs. Any effort aimed at introducing SDT for developing countries in RTAs as a realisation of the ‘development dimension’ would most likely face opposition from such Members concerned about the effectiveness of multilateral disciplines on RTAs. In this light the ACP Group’s negotiating strategy to introduce SDT also has to incorporate the wider universal, systemic case for reforming WTO rules to effectively discipline RTAs as supported by other WTO members. The rationale for this is twofold; first, as a negotiating strategy and, second, as part of the effort to develop effective and equitable rules for ensuring that RTAs, especially those formed by major trading nations and excluding ACP States, contribute to the strengthening of the multilateral trading system.

### III.3 THE CASE FOR SDT IN WTO RULES APPLYING TO NORTH–SOUTH RTAS

64. To ascertain the adequacy of multilateral disciplines over RTAs in catering for greater flexibility for developing countries in the context of North–South RTAs, two questions need to be asked. *First, do the WTO rules explicitly entitle a greater degree of flexibility to be granted to developing countries than to developed countries as a form of SDT in the context of North–South RTAs?* Given that SDT is an integral part of the multilateral trading system, the absence thereof constitutes a *prima facie* case for reforming and injecting SDT provisions into the WTO rules applying to RTAs for the purpose of North–South RTAs. *Second, if there is no explicit SDT in the WTO rules for North–South RTAs, then is the flexibility inherent in WTO rules (‘existing flexibilities’) adequate in nature and sufficient in degree in providing the necessary legal coverage for flexibility for developing countries under North–South RTAs, including EPAs?*<sup>60</sup> The absence of formal SDT in WTO rules could be justified only if other instruments, namely the flexibility inherent in Article XXIV of GATT 1994, already entitle RTAs to provide a form and degree of flexibility deemed necessary for developing countries. Otherwise, a case necessarily arises for reforming the WTO rules to incorporate SDT.

65. With regard to the first question, it can be concluded that there are no explicit SDT provisions applicable under the current WTO rules to developing countries in North–South RTAs. With regard to the second question, it can be concluded that existing flexibility under current WTO rules is likely to be insufficient in view of the degree of flexibility for ACP States. Moreover, the existing flexibilities cannot be relied upon as an adequate defence against possible legal challenges. Therefore, it can generally be concluded that there is a case for reforming the WTO rules to incorporate formal SDT provisions within GATT Article XXIV for the purpose of North–South RTAs.

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<sup>59</sup> Australia’s proposal (WT/GC/W/183) exemplifies views in favour of stringent disciplines. These included ‘decide whether the various WTO rules on RTAs should be integrated into a single framework, including “substantially-all-the-trade” should be measured in terms of goods and services together’; ‘decide whether agreements covered by the Enabling Clause should be subject to the disciplines of GATT Article XXIV’; and ‘clarify whether other thresholds for RTAs need to be introduced, for example, linking the extension of preferences under a proposed RTA to a reduction in trade barriers on an MFN basis’.

<sup>60</sup> It is worth recalling that, as defined previously, two kinds of flexibilities are at issue: flexibility inherent in the existing rules and applicable to all countries irrespective of the level of development (‘existing flexibilities’), and ‘additional’ flexibilities to be made available specifically to developing countries through SDT.

### III.3(a): SDT in WTO rules applying to North–South RTAs

66. The lack of explicit SDT provisions in WTO disciplines for North–South RTAs is evident.<sup>61</sup> North–South RTAs, including EPAs, would be subject to disciplines under Article XXIV of GATT 1994, which currently lacks explicit SDT for developing countries, as discussed previously. The Enabling Clause, which contains SDT, is not applicable as it applies only to RTAs formed among developing countries. On the other hand, the applicability to RTAs of Part IV of GATT, which provides for the principle of non-reciprocity in trade negotiations, has been denied under a dispute settlement finding. The result is that from among the possible WTO provisions pertaining to RTAs, no formal explicit SDT is applicable to developing countries forming RTAs with developed countries. This constitutes a legal lacuna, and it is particularly odd given that it is precisely in such RTAs that developing countries would need a higher degree of policy discretion.

67. The lack of formal SDT within GATT 1994 Article XXIV is in part a reflection of the fact that the original Article XXIV of GATT 1947 was negotiated and agreed at a time when development concerns were not as prevalent as they are today. The article presumes that RTAs will be formed between countries with similar levels of development, namely developed countries. This deficiency was not addressed in subsequent multilateral trade negotiations, until the adoption of the Enabling Clause in the Tokyo Round, and of the 1994 Understanding in the Uruguay Round, due primarily to that fact that there were few North–South RTAs. As a result, Article XXIV of GATT has in some sense become obsolete in effectively addressing North–South RTAs at a time when such RTAs are becoming an increasingly common feature of the post-Uruguay Round international trading system.

68. The absence of SDT in Article XXIV of GATT 1994 is most apparent when a comparison is made with counterpart provisions in the General Agreement on Trade in Services (GATS) (see Table 4). The notion of SDT has been explicitly recognised in GATS Article V:3(a), which in respect of economic integration agreements (EIAs) provides that ‘where developing countries are parties to an agreement’, ‘flexibility shall be provided for regarding conditions set out in GATS Article V:1 ((a) substantial sectoral coverage, and (b) absence or elimination of discriminatory measures) to be provided either at the entry into force of that agreement or on the basis of a reasonable time-frame’ (see Box 8). Under GATS V:3(a), SDT is provided in terms of meeting the requirements on internal trade liberalisation within EIAs and the transitional period.

**Table 4. Comparison of SDT provisions on RTAs in GATT 1994 and GATS: Internal trade and transitional periods**

	<b>GATT 1994</b>	<b>GATS</b>
Non-SDT ‘existing’ flexibilities	XXIV:8 (a)(i) and (b); XXIV:5(c)	V:1
SDT for North–South Agreements	<i>Not applicable</i>	V:3(a)
SDT for South–South Agreements	*Enabling Clause	V:3 (a) and (b)
<i>Memo</i>		
SDT in multilateral trade negotiations	XXXVI:8 (Part IV)	XIX:2

\* The Enabling Clause assumes no formal link to GATT Article XXIV requirements.

69. Furthermore, it is significant that GATS Article V:3(b) recognises a distinction between EIAs involving both developed and developing countries (i.e. North– South EIAs) and EIAs involving only developing countries (i.e. South– South EIAs) by stipulating that ‘more favourable treatment’ is to be accorded to legal persons of developing countries in the case of EIAs ‘involving only developing countries’. Thus, the provision not only recognises the need for SDT in general for EIAs involving developing countries, but also presumes the need for the degree of flexibility under such EIAs to be

<sup>61</sup> Although paragraph 10 of GATT Article XXIV allows WTO members to approve, by two-thirds majority, proposals that do not fully comply with the requirements of paragraphs 5–9, the provision contains no reference to developing countries.

greater in South–South EIAs than in North–South EIAs. An application of this distinction to trade in goods necessarily raises the need for the inclusion of SDT provision within Article XXIV of GATT as distinct from those available under the Enabling Clause.

**Box 8: GATS Article V and ‘flexibility’**

The term ‘flexibility’ used in GATS V:3(a) is rather confusing. Since the conditions set out in GATS V:1 are articulated in a manner similar to (or even more flexible than) GATT Article XXIV:8, there does exist a sort of flexibility applicable to all WTO Members party to EIAs (as they are not required to cover all sectors or to eliminate all discriminatory measures). These flexibilities can be termed ‘existing flexibilities’. Flexibility to be provided for developing countries under GATS V:3 (a) is indeed a form of SDT, as it applies only to developing countries, and thus should mean an *additional* degree of flexibility to developing countries in their coverage of fewer sectors or elimination of lesser degree of discriminatory measures than would be required for developed countries. This extra degree of flexibility (or differentiated and more favourable treatment) is at issue in the context of GATT Article XXIV. The distinction between these ‘extra flexibilities’ and ‘existing flexibilities’ is important, as there is the argument that GATT Article XXIV is already flexible enough and that developing countries’ needs should be dealt with within the scope of such ‘existing flexibilities’.<sup>62</sup> The problem with this assumption is that it cannot cater for such cases where undeniably legitimate developing countries’ needs exceed the scope of ‘existing flexibilities’. The ‘extra flexibility’ as provided in GATS V:3(a) is the recognition of such an eventuality. In the case of GATT XXIV, this ‘extra’ flexibility for developing countries in North–South agreements is missing.

70. The absence of SDT in GATT 1994 Article XXIV also seems to lack symmetry with GATS Article V in terms of the degree of ‘existing flexibilities’ inherent in both provisions, as the requirements of GATS Article V:1 are already more flexible than those under GATT Article XXIV:8, even without the additional flexibilities made available by GATS Article V:3(a) as SDT (see table 5). GATS Article V:1 allows for the sectoral coverage of EIAs to be ‘*substantial*’ as compared to ‘*substantially all* the trade’ required under GATT Article XXIV:8; GATS also leaves the possibility for the members of an EIA the choice between eliminating existing discriminatory measures (i.e. ‘rollback’) and prohibiting new or more discriminatory measures (i.e. ‘standstill’), as compared with the unambiguous requirement for the ‘elimination’ of duties and ORRCs under GATT Article XXIV:8. Similarly, the choice is left to members of EIAs as to the timing for meeting the requirements of GATS V:1(b) ‘either at the entry into force of that agreement or on the basis of a reasonable time-frame’ without any determined ‘reasonable time-frame’, as compared with the 10-year time-frame limitation under the 1994 Understanding on GATT Article XXIV. GATS Article V:3(a) builds upon these existing flexibilities to provide additional degree of flexibility to developing countries as SDT in meeting requirements on international trade liberalisation as well as the transitional period.

71. It could thus be expected that the case for such SDT provision is stronger for GATT Article XXIV. Even though such a discrepancy in the level of existing flexibilities is in large part explained by the peculiarity of regulation and liberalisation of trade in services, it highlights at the very least the case that there is no *a priori* reason why SDT could not be incorporated into GATT Article XXIV. The lack of SDT in GATT Article XXIV, and the resulting imbalance in the degree of flexibilities available to developing countries between GATT Article XXIV and GATS V constitutes a legal inconsistency in the architecture of WTO rules on trade in goods and services.

<sup>62</sup> See, for instance, EC submission (TN/RL/W/14), which proposes for WTO rules negotiations on RTAs for the purpose of the ‘development dimension’ ‘to clarify the flexibilities *already provided* for within the existing framework of WTO rules’ (emphasis added), which would involve ‘examination of the extent to which WTO rules already takes into account discrepancies in development levels between RTA parties’.

**Table 5.** Comparison of requirements (and ‘existing flexibilities’) on RTAs under GATT 1994 and GATS: Internal trade and the transitional period

	<b>GATT XXIV: 8 (a)(i) (b)&amp; 5(c)</b>	<b>GATS V:1</b>
Coverage	<i>Substantially all</i> the trade	(a) <i>Substantial</i> sectoral coverage in terms of number of sectors, volume of trade affected and modes of supply (no <i>a priori</i> exclusion of any mode of supply)
Obligation	Duties and ORRCs are <i>eliminated</i> .	(b) Absence or elimination of substantially all discrimination (i.e. national treatment) in the sectors covered under (a) through: (i) elimination of existing discriminatory measures; <i>and/or</i> (ii) <i>prohibition of new or more discriminatory measures</i> .
Transitional period	Reasonable length of time understood to exceed 10 years <i>only in exceptional cases</i>	Requirements in (b) to be met either at the entry into force of that agreement or on the basis of a <i>reasonable time-frame</i>

### III.3(b) Flexibility inherent in GATT 1994 Article XXIV

72. The case for SDT in WTO rules applying to North–South RTAs, however, is partly contingent upon whether flexibility for developing countries is *de facto* adequately and sufficiently covered under existing provisions of Article XXIV of GATT (‘existing flexibilities’). If the current rules already provide adequate and sufficient coverage for flexibility for developing countries as would be required under EPAs, the case for SDT in WTO rules is weakened, if not redundant. Indeed, it has been argued that GATT Article XXIV is already flexible enough to cover the special needs of developing countries. This is the case of the second question, namely, the availability of implicit flexibility inherent in GATT Article XXIV.

73. Some flexibility is available in the existing provisions of GATT Article XXIV. The current articulation of the article allows some degree of flexibility for an RTA to be WTO compatible in terms of the intra-group liberalisation of trade and the level of external trade barriers. The ‘substantially-all-the-trade’ and ‘not-on-the-whole-higher-or-more-restrictive’ requirements allow by virtue of their qualification in non-specific terms (‘substantially’ and ‘on the whole’), for parties to an RTA not to dismantle barriers to all trade among them, to maintain certain restrictive non-tariff measures (quantitative restrictions for general exceptions or reasons such as balance of payments (BOP), etc.), or to raise the level of protection against third countries on certain products provided that those measures do not constitute an infringement of other WTO provisions. There is also flexibility in the provision that in ‘exceptional cases’ the transitional period could exceed 10 years.

74. These flexibilities are seen to be *de facto* tolerated owing to the interpretative ambiguity inherent in key benchmark provisions of Article XXIV of GATT 1994, as well as the resulting inconclusive nature of examinations of compatibility of notified RTAs by the Committee on Regional Trade Agreements<sup>63</sup> (see Box 9). Indeed, very few RTAs have liberalised completely their internal trade, measured either by trade volume, product sector or product items. Moreover, the issue of trade/product coverage has never been subjected directly to dispute under dispute settlement procedures.<sup>64</sup>

<sup>63</sup> The CRTA has a four-fold mandate: (1) carry out the examination of agreements referred to it by Council for Trade in Goods, Council for Trade in Services and Committee on Trade and Development; (2) consider how the required reporting on the operations of RTAs should be carried out; (3) develop procedures to facilitate the examination process; and (4) consider the systemic implications of RTAs.

<sup>64</sup> In one case on *Canada - certain measures affecting the automotive industry*, the panel ruled that the Canadian measure of granting preferential treatment to the importation of automotive products by certain eligible manufacturers established in Canada could not be seen as part of an obligation arising from NAFTA, and thus could not be covered by Article XXIV of GATT. See *Report of the Panel, Canada-Certain Measures Affecting the Automotive Industry* (WT/DS139/R, WT/DS142/R), 11 February 2000.

### Box 9: Deadlock in the CRTA and ‘systemic issues’

The CRTA has so far failed to reach a consensus on the WTO compatibility of notified RTAs whose factual examinations it has concluded. As of October 2002, 255 RTAs (covering goods and services) had been notified to the GATT/WTO, of which 213 were notified under GATT Article XXIV, 21 under GATS and 20 under the Enabling Clause. Of those 213 RTAs notified under GATT Article XXIV, 131 are in force. While the CRTA has a total of 125 agreements under examination, the factual examination of 74 RTAs have been completed and the draft examination reports are in order for those RTAs.<sup>65</sup> However, the CRTA has not been able to adopt final reports on its examinations to date. This is in large part due to the very limited progress made by WTO members in resolving ‘systemic issues’ concerning WTO rules on RTAs.<sup>66</sup> Given the stalemate in the CRTA, several countries proposed in March 2001 that the status of work in the CRTA be placed on the agenda of the WTO General Council so as to be monitored more closely by the high policy body. Consequently, in July 2001, the chairperson of the CRTA reported on the deadlock to the WTO General Council. The Chairperson’s report noted that the deadlock was in part a logical consequence of the rule-based multilateral trading system with its strengthened dispute settlement mechanism, which induced Members not to agree on any matter that may be invoked in possible dispute cases.<sup>67</sup> The failure of the CRTA to fulfil its mandate on the examination of notified RTAs was a major rationale behind the inclusion of the WTO rules on RTAs in the agenda for negotiations under the Doha agenda.

Systemic issues of contention with regard to the GATT 1994 Article XXIV include the following: the interpretation of ‘substantially all the trade’, the ‘not on the whole higher or more restrictive’, ‘other regulations of commerce’ (ORC), including the treatment of preferential rules of origin, ‘other restrictive regulations of commerce’ (ORRC), such as the mode of application of contingent measures, and obligations during transitional periods. The relationship between RTAs notified under the Enabling Clause and GATT Article XXIV has also been raised. Links between RTA preferences and the extension of MFN reduction of duties is another issue. Systemic issues with regard to GATS include the interpretation of ‘substantial sectoral coverage’; ‘absence or elimination of substantially all discrimination’, ‘and/or’ language in V:1(b) and the ‘reasonable time frame’.<sup>68</sup>

75. Even when a relatively high degree of internal trade is liberalised, a significant number of tariff lines where little trade is taking place among RTA partners due to the prohibitively high tariff rates or non-tariff barriers (NTBs) are often excluded from internal liberalisation. A survey undertaken by the WTO Secretariat on ‘Coverage, liberalisation process and transitional provisions in regional trade agreements’ confirms this practice.<sup>69</sup> The survey noted that the coverage of RTAs was marked by discrepancies between product coverage (on tariff line basis) and trade coverage (trade actually happening). Also, the treatment of industrial and agricultural products is significantly different. RTAs usually cover higher than 75% of actual intra-RTA trade but the share of duty-free treatment becomes considerably lower when measured on a tariff line basis. As to the treatment of industrial versus agricultural products, industrial products are usually covered under an RTA on the basis of a negative list, while a positive list approach is used for agricultural products, which significantly contributes to the lower coverage of agricultural products. Often the agricultural sector is treated in a separate protocol or annex in the legal texts. When agricultural trade is included in the coverage of an RTA, the concessions tend to consist of duty reductions, rather than duty elimination. Also, MFN tariff peaks generally persist under RTA tariff schedules.

76. The scope of ‘existing flexibilities’ is in large part left for each WTO Member’s interpretation, and no consensus exists. If the length of transitional period, for which a relatively clear definition of a 10-year time-frame (with the possibility of a longer period in ‘exceptional cases’) is

<sup>65</sup> Report of the Committee on Regional Trade Agreements to the General Council (WT/REG/47), 4 November 2002.

<sup>66</sup> Among the draft reports pending in the CRTA include NAFTA, the EFTA-Hungary FTA, and the Protocol on Trade in Services for ANZCERTA based on a new format for drafting of reports adopted in February 2001.

<sup>67</sup> WT/GC/W/43.

<sup>68</sup> WTO(2000) and WTO (2002c).

<sup>69</sup> WTO (2002a).

provided under the 1994 Understanding on GATT Article XXIV, is taken as a measure of ‘existing flexibilities’, the extent to which the transitional period is deviated and exceeded could be considered as an approximate measurement of the scope of ‘existing flexibilities’. In this respect, several North–South RTAs have provided transitional periods of longer than 10 years for developing countries (and for developed countries in some instances).<sup>70</sup> These precedents include the following:

- Under the Euro-Mediterranean Agreements between the EU and Tunisia, 1509 tariff lines at seven-digit HS levels are to be liberalised over a period of 12 years for Tunisia, while all but some agricultural products are subject to immediate liberalisation on the part of the EU.<sup>71</sup> At the same time it is reported that the EU has undertaken, in 1999 value terms, a lesser degree of market opening (92.9%) than Tunisia (96.7%). This is also the case for EU trade agreements with Egypt, Hungary and Turkey, with the degree of trade freed of duty for the EU ranging from 84% to 94% and for its partners from 96% to 100%.<sup>72</sup>
- The Trade, Development and Co-operation Agreement between the European Community and South Africa allows a longer transitional period for South Africa (12 years) than for the EU (10 years), while requiring the EU to eliminate tariffs on a higher percentage of currently traded goods (95%) than is the case for South Africa (86%).<sup>73</sup>
- The FTA between EFTA and Morocco provides a transitional period of 12 years for certain products for Morocco, while no transitional period is provided for EFTA.<sup>74</sup>
- The FTA between Canada and Chile (CCFTA) provides a phase-out period of 15 years for over-quota tariff for Canadian beef imported into Chile. Other Chilean agricultural tariffs to be phased out over ten years include potato products, cornflour and certain sugar products. A longer phasing applies to sugar (16 years), milled wheat and wheat flour (17 years).<sup>75</sup>
- NAFTA provides a transitional period of up to 15 years for certain products for all three members i.e. Canada, Mexico and the United States.<sup>76</sup>

77. In terms of the transitional period, among the above examples, a maximum of 7 years (i.e. a total 17-year period) has been claimed for the coverage under ‘exceptional circumstances’. These precedents have led to an interpretation of Article XXIV:5(c) of GATT 1994 and its Understanding that a transitional period of longer than 10 years could exceptionally be permitted for some products if such products constitute a very small percentage of trade.<sup>77</sup> In the CRTA consideration of notified RTAs, the provision to developing countries of a transitional period of longer than 10 years in some cases has been justified by the parties on the basis of ‘the sharp difference between the respective level of development’ of parties to the RTA and the need to allow developing country member to deal progressively with the economic and social consequences linked to the process of economic liberalisation and market opening under the FTA’.<sup>78</sup> Thus, in the absence of SDT, the development needs of developing countries are being addressed by such ‘existing flexibilities’.

78. It can therefore be argued that ‘existing flexibilities’ under GATT Article XXIV provide an adequate basis for coverage for the future EPAs involving asymmetric undertakings, and greater flexibility for ACP developing countries in terms of, *inter alia*, trade coverage or transitional period. This argument, however, is weak for two reasons.

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<sup>70</sup> For a discussion, see Laird (1999).

<sup>71</sup> *Euro-Mediterranean Agreement between the European Communities and their Member States and Tunisia*, (WT/REG69/1).

<sup>72</sup> Davenport (2002), table 1, p.11.

<sup>73</sup> *Trade, Development and Co-operation Agreement between the European Community and South Africa* (WT/REG113/1).

<sup>74</sup> *Free-Trade Area between EFTA and Morocco*, WT/REG91/1.

<sup>75</sup> Free Trade Agreement between Canada and Chile, WT/REG38/1.

<sup>76</sup> A transitional period of longer than 10 years is foreseen for 15 products that ‘only counts small volume of trade’ (WT/REG4/W/1). It is reported that the US requested a longer phase-out period for certain products during the negotiations. See Estevadeordal (2000).

<sup>77</sup> WTO (2000).

<sup>78</sup> For example, the Euro-Mediterranean Agreement between EC and Tunisia, WT/REG69/4, 2 May 2000.

79. First, it is uncertain whether the scope of the existing flexibilities available under GATT Article XXIV is sufficient in degree to cover the flexibility that may be deemed necessary for (low-income) developing countries under North– South RTAs. In the case of EPAs, some ACP States may require a greater degree of flexibility than is currently (presumably) within the scope of existing flexibilities. For instance, in terms of transitional periods, the above example of 7 years (i.e. 17 years total) could be insufficient for some low-income developing countries given that their level of development that is significantly lower than middle/high-income developing countries that have so far concluded North–South RTAs and to which longer-than-10-year transitional periods have been accorded (e.g. the Maghreb countries, Chile, Costa Rica and South Africa). Thus, it may be the case that the degree of flexibility deemed necessary for ACP States under EPAs may prove to be considerably greater than that applied so far under any North–South RTAs. The existing flexibility under GATT Article XXIV may be insufficient in providing an appropriate legal basis for flexibilities for ACP States under EPAs. If ACP flexibilities under EPAs are to be appropriately covered under existing flexibilities of GATT Article XXIV, there may be a need to extend the scope of the existing flexibility altogether, which from a systemic perspective will be considered undesirable; hence the need for SDT.

80. Indeed, the current flexibility in GATT Article XXIV arising from ambiguity in the standards has been challenged. A WTO panel on *Turkey - Restrictions on Imports of Textile and Clothing Products case (Turkey - textiles)* pointed out that the flexibility inherent in Article XXIV of GATT 1994 would perform important functions in avoiding conflict among different WTO provisions and enabling ‘harmonious interpretation’. The panel found that Turkey’s imposition of quantitative restriction on imports of textile products from India upon its formation of a customs union with the EC could not be justified simply because Article XXIV of GATT requires a customs union to adopt substantially the same external trade policy among constituent members. The panel pointed out that the ‘flexibility’ inherent in Article XXIV of GATT allows for certain WTO-compatible restrictions to be maintained in respect of the intra-group trade (e.g. import restriction by EC Member States of textiles from Turkey or origin requirements) to ensure, for instance, that the protection provided by pre-existing import quota of a constituent party (i.e. EC quota on textile from India) would not be circumvented by not adopting the same external quota in another member of the RTA (i.e. Turkey).<sup>79</sup> This finding of the panel was modified by the Appellate Body which, while sustaining the Panel’s conclusion that ‘flexibility’ should enable an RTA party to abide by WTO rules with regard to third parties, rejected the Panel’s legal reasoning on the ‘harmonious interpretation’ so as to limit the scope of ‘flexibility’ in the light of the chapeau paragraph of GATT Article XXIV:5, read in the context of ‘purposive’ language of paragraph 4, as well as operative requirements on ‘substantially all the trade’ set out in Article XXIV.8(a)(i).<sup>80</sup> The practical policy implication of such a finding is that, although a country could maintain some restrictive regulations of commerce internally, such as quantitative restrictions, to the extent that they are required for the formation of an FTA or customs union in order to ensure that the levels of barriers *vis-à-vis* third countries are not on the whole higher or more restrictive, the extent to which a member of an RTA is entitled to do so (‘scope’) would be limited, as the purpose of a customs union or FTA should be ‘to facilitate trade between the constituent territories’. This logic would also hold relevance to the lesser product or trade coverage of an RTA, as, even if an RTA may wish to limit the degree of internal liberalisation, for whatever reason, its ability to do so would be significantly constrained by the purposive language of paragraph 4, as well as the substantive requirements in Article XXIV:8(a)(i) or (b) on ‘substantially all the trade’.

81. Second, and more fundamentally, a legal uncertainty arises from an excessive reliance on the *de facto* tolerance by WTO Members under the cover of existing flexibilities in GATT Article XXIV. This constitutes a major problem with the current operation of the WTO. Such legal ambiguity would

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<sup>79</sup> Panel Report on *Turkey - Restrictions on Imports of Textile and Clothing Products*, adopted on 19 November 1999 (WT/DS34/R).

<sup>80</sup> *Turkey – Restrictions on imports of textile and clothing products: Report of the Appellate Body*, 22 October 1999 (WT/DS34/AB/R), paragraph 48 and 57.

provide an opening that could be challenged under the WTO Dispute Settlement Mechanism. The 1994 Understanding on GATT Article XXIV made it explicit that the Dispute Settlement Understanding procedures are applicable ‘with respect to any matters arising from the application of those provisions’. A test case involved the *Turkey – Textile dispute case* in 1999. Citing a previous GATT panel report on *EEC - Imports from Hong Kong*, it was ruled that the mere fact that a certain measure taken pursuant to a regional trade agreement has not been subject to dispute settlement proceedings under the WTO should not be interpreted as being tantamount to its tacit acceptance by WTO Members.<sup>81</sup> Thus, the existence of precedents on ‘tolerated’ flexibility does not rule out the possibility of a legal challenge.

82. This inability so far of WTO members to pronounce on the WTO compatibility of RTAs notified under Article XXIV of GATT has given rise to questions concerning the legal status of those RTAs.<sup>82</sup> The absence of a clear determination by the CRTA on the conformity of a notified RTA with relevant WTO rules has given rise to doubts as to whether, in the case of a dispute, a member of the concerned RTA can invoke Article XXIV of GATT or GATS Article V as a defence against its presumed violation of the MFN principle. The test case in point is the aforementioned *Turkey-Textile case*. The Appellate Body established conditions for a defending party to be able to invoke Article XXIV of GATT 1994 as a defence. First, the defending party has the burden to demonstrate that the measure at issue is introduced upon the formation of a customs union that fully meets the requirements of Article XXIV of GATT. Second, it has to demonstrate that the formation of a customs union would be prevented if it were not allowed to introduce the measure at issue.

83. Thus to the extent that the WTO compatibility of an RTA is not pronounced by the WTO through the CRTA process, uncertainty will persist regarding its legal status and its defence in the event of a dispute. For parties to an RTA, this means that it has become very important to secure a positive recommendation by the CRTA, as a presumption has been created that an RTA cannot be assumed to be WTO-compatible in so far as no conclusive decision is taken through the CRTA examination process.

84. The legal ambiguity also raises an institutional issue relating to the jurisdiction of the CRTA and the Dispute Settlement Body (DSB). Since the 1994 Understanding clarified that the DSB has jurisdiction over all matters relating to the operation of Article XXIV of GATT, the practical implication of such an institutional distribution of power is that the DSB may override the jurisdiction of the CRTA in the event that the CRTA continues to be unable to pronounce on the WTO compatibility of an RTA. While such activism by the judicial body may encounter strong opposition from many WTO Members, legal uncertainty continues to prevail regarding the conformity of RTAs, and thus the legal and economic interests of the members of North–South RTAs. A similar institutional concern has been raised with regard to the relative jurisdiction of the DSB and the Committee on Balance of Payments. In the *India-Quantitative restriction case*, the Appellate Body recognised the jurisdiction of the DSB to review the justification of balance-of-payments (BOP) restriction under Article XVIII:B of GATT 1994, although this is the assigned mandate of the Committee on BOP, and this intervention may take place even if the deliberation in the Committee is still ongoing.<sup>83</sup>

85. It would appear to be the case that the existing flexibilities inherent in current Article XXIV of GATT 1994 and the tacit tolerance by WTO Members of certain borderline-case practices cannot be relied upon indefinitely as an adequate defence against possible legal challenges under WTO dispute settlement procedures. From the ACP–EU perspective, the legal uncertainty raises

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<sup>81</sup> *EEC – Imports from Hong Kong*, paragraphs 28 and 29, quoted in the Panel Report on *Turkey– Textiles*, *op cit*, paragraph 9-173.

<sup>82</sup> *Turkey - Restrictions on imports of textile and clothing products* (WT/DS34/AB/R), paragraph 58.

<sup>83</sup> Within the framework of the implementation-related issues and concerns, India and others have proposed that Article XVIII of GATT 1994 be clarified ‘to the effect that only the Committee on Balance of Payments shall have the authority to examine the overall justification of BOP measures’ (WT/GC/W/354).

considerable risks for their legal interests in the WTO in relation to future EPAs. For them there is the need to pre-empt possible future legal challenges against measures taken to construct EPAs. Such a need would arguably be more acute for the EU than for ACP States, since its large market is subject to more intense competition and is thus more prone to legal claims by third exporting countries (see Box 10).

**Box 10: Possible challenge against the EU import regime under EPA**

In the absence of an agreed understanding on the scope of flexibility (possibly extended through SDT) under GATT Article XXIV, as well as the effective examination by the CRTA of notified RTAs, there remains the possibility of WTO dispute settlement cases being launched by non-ACP (developing) countries against the EU import regime under future EPAs that would grant preferential duty-free treatment of, say, canned tuna originating in a group of ACP States party to an EPA. The complainants might argue: that the preferential tariff treatment of canned tuna in favour of certain ACP States violates the MFN obligation under GATT Article I:1; that the EU is not entitled to invoke GATT Article XXIV as a defence unless it demonstrates that the EPA is indeed an FTA in the meaning of GATT Article XXIV:8(b); that the EPA at issue, falling short of the criteria set out therein due possibly to greater flexibility provided for ACP partner States under the EPA (e.g. lower trade coverage), could not be considered as an FTA in the sense of GATT Article XXIV:8(b); and, therefore, that the discriminatory tariff treatment of canned tuna is in violation of the MFN obligation under Article I:1 and could not be justified under GATT Article XXIV. In the absence of a positive recommendation by the CRTA on its GATT conformity, the burden is on the EU to prove that the EPA has indeed met the requirements of GATT Article XXIV, and that the measures in question is necessary for the formation of the FTA. Therefore, without some formal understanding as to the form and degree of flexibility permissible under GATT Article XXIV, such justification may be highly difficult. The recent experience of recurrent legal challenges discussed in chapter II against the EU GSP scheme points to the potential of similar cases being raised under EU's preferential schemes, including future EPAs.

86. Hence, there is a general case (1) for rendering SDT applicable to developing countries in the context of North–South RTAs including, but not limited to, the possibility of incorporating formal SDT into GATT 1994 Article XXIV, or (2) for enlarging the scope, and redefining formally the legal nature, of existing flexibilities generally permissible under GATT Article XXIV (as the existing flexibilities appear insufficient in scope and inappropriate in nature). The incorporation of SDT should take precedence, as the lack of SDT provision in GATT Article XXIV is the primary cause of the deficiency in WTO rules applying to North–South RTAs. SDT is indeed superior to the second approach of enlarging the scope of existing flexibilities for all WTO Members, as SDT would limit the availability of the greater flexibility thereby instituted only to developing countries. Under the Doha work programme on WTO rules applying to RTAs, SDT is all the more important if the multilateral negotiations are to lead to more ‘stringent’ disciplines. The approach would thus be compatible with the systemic need for ‘clarification and improvement’ of GATT Article XXIV. Hence, the case for SDT is not only based upon the imperative to redress the lack of SDT in GATT Article XXIV, but also the usefulness in reconciling the development needs of developing countries and the systemic need for an open, non-discriminatory trading system.

#### **III.4 OPTIONS FOR INCORPORATING SDT INTO WTO PROVISIONS ON RTAS IN THE CONTEXT OF NORTH–SOUTH RTAS**

87. In order to render SDT applicable to developing countries in the context of North–South RTAs, three options are conceivable, namely:

- (1) reforming GATT 1994 Article XXIV to incorporate SDT provisions;
- (2) reforming Part IV of GATT 1994 to render it applicable to GATT 1994 Article XXIV; or
- (3) reforming the Enabling Clause to render it applicable to North–South RTAs.

88. All options would aim to introduce SDT in WTO rules governing North–South RTAs so that less stringent requirements are applied to developing countries parties to such RTAs. The first option

aims to institute SDT in terms of key requirements of GATT 1994 Article XXIV. The second option seeks to incorporate SDT by linking the SDT provisions for trade negotiations under Part IV of GATT 1994 to the provisions of GATT 1994 Article XXIV. The third option consists in excluding altogether North– South RTAs from the scope of GATT Article XXIV and including them within the scope of the Enabling Clause, so that the SDT provided for South– South RTAs is also applicable to North– South RTAs. Among these three options, the first proves to be the most viable.

#### **III.4(a) Reforming Article XXIV of GATT 1994**

89. Any reform for the inclusion of SDT within GATT Article XXIV could aim at instituting less stringent requirements for developing countries than those generally applicable for the assessment of WTO conformity, so as to enable developing countries party to North–South RTAs to undertake less stringent obligations than developed countries. SDT is needed for developing countries in the application of the substantive and procedural requirements of GATT Article XXIV in terms of (1) ‘substantially all the trade’ (SAT) requirements for internal trade liberalisation in terms of duties and other restrictive regulations of commerce (ORRC) (Article XXIV:8(a)(i) and (b)); (2) the transitional period (‘should exceed 10 years only in exceptional cases’) (Article XXIV:5(c) and the 1994 Understanding); and (3) the level of barriers to third countries (‘not-on-the-whole-higher-or-more-restrictive’ requirement) (Article XXIV:5(a) and (b)); and (4) procedural requirements.

90. Reforms could be based upon the codification and/or redefinition of the existing flexibilities applicable to all countries.<sup>84</sup> Once the scope of such flexibility for all WTO members is formalised and redefined under the examination of ‘systemic issues’, the scope of ‘additional flexibilities’ to be made available for developing countries through SDT, differentiated and more favourable treatment could be defined relative to the generally applicable flexibility for all countries. The effective introduction of SDT into Article XXIV of GATT 1994 may be facilitated by agreeing multilaterally upon some quantitative criteria for key requirements, including the ‘substantially-all-the-trade (SAT)’ requirement.<sup>85</sup> Once agreed, the level of ‘additional flexibilities’ to be made available through SDT could be quantitatively defined relative to the generally applicable level of flexibilities. For instance, if coverage of 90% of total volume or tariff lines is deemed necessary for the purpose of meeting the SAT requirement, then SDT for developing countries could provide additional flexibilities so that a coverage of, say, 70% would suffice for meeting the SAT requirement (see section IV.1(a) below).

91. Three possibilities are conceivable for a reform of GATT Article XXIV, namely (1) generic SDT; (2) specific SDT through redefinition of substantive and procedural requirements in Article XXIV:5-8; and (3) SDT in derogation from GATT Article XXIV requirements through a revision of Article XXIV:10. The former two approaches are basically alternative to each other and equivalent to the extent that the same degree of flexibility is made available to developing countries. The choice between the two would depend largely on negotiations. However, the specific terms of flexibilities to be made available to developing countries under the generic SDT may need specific definition. In such a case, the two approaches could be complementary. The third possibility is only complementary to the former of the two approaches. A possible, but highly contestable, fourth option is outlined in Box 11.

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<sup>84</sup> The EC proposal in the Negotiating Group on Rules calls for the examination and clarification of ‘flexibilities already provided for within the existing framework’ through examination of relationship between GATT Article XXIV and the Enabling Clause; the extent to which WTO rules already take into account discrepancy (or asymmetry) in development levels between RTA parties; and the flexibilities available during the transitional period (length, level of final trade coverage, degree of asymmetry; TN/RL/W/14). It does not mention the need for special and differential treatment in the application of GATT Article XXIV requirements for North–South RTAs.

<sup>85</sup> See, for example, Mathis (2002). Setting quantitative criteria for SAT purpose has been the subject of systematic debate in the CRTA, but no agreement has been reached.

### Box 11: Special case for ACP–EU trade relations

Paragraph 11 of GATT Article XXIV provides in respect of India and Pakistan as follows: ‘...the contracting parties agree that the provisions of this Agreement shall not prevent the two countries from entering into special arrangements with respect to the trade between them’. Furthermore, an endnote to that paragraph (ad Article XXIV:11) stipulates that ‘measures adopted by India and Pakistan ... might depart from particular provisions of this Agreement, but these measures would in general be consistent with the objectives of the Agreement’. Therefore, another possibility for reform for ACP States might consist in inserting a new paragraph on the special case of ACP–EU trade relations, in line with special trade arrangement provided for in Article XXIV:11. This would have the advantage of limiting the exceptional case only to ACP–EU trade relations, thus distorting the primacy of the multilateral trading system to the least extent possible. However, the proposal of such an amendment is most likely to be contested, and thus untenable, on the ground that such a case could not be agreed only for ACP–EU RTAs. There are numerous other similar cases of North– South RTAs, such as the Free Trade Area of the Americas.

92. Changes could be made either through an amendment of the Article itself, or through a reinterpretation by way of the revision of the interpretative understanding contained in the 1994 Understanding on GATT Article XXIV. Given the practical difficulty in formally reopening, renegotiating and amending Article XXIV of GATT 1994 itself, which would need the consensus of the Ministerial Conference (Article X of the Marrakesh Agreement), it might appear that adopting a new interpretation through a revision of the 1994 Understanding – which may be agreed by three-fourths majority – would prove to be more feasible option (Article IX:2).<sup>86</sup> In practice, however, in the context of the Doha work programme, the issue is not likely to be particularly sensitive, as consensus is required in any event under the ‘single undertaking’. The approach adopted in the Uruguay Round also consisted in clarifying the meaning of articles by way of agreeing on their authoritative interpretation in the form of understandings and various substantive agreements, which were ultimately adopted as a ‘single undertaking’.<sup>87</sup>

#### (i) *Generic paragraph on SDT*

93. The first possibility consists in addressing the flexibility concept in a general manner by incorporating generic paragraphs on SDT in favour of developing countries in meeting the requirements of paragraphs 5-8 of GATT Article XXIV in the case of North–South RTAs, in line with GATS Article V:3(a). Given the overwhelming importance of requirements related to internal trade liberalisation (Article XXIV:8(a)(i) and (b)) and the transitional period (Article XXIV:5(c)) for developing countries in North–South RTAs, the reference to SDT might be centred on these subparagraphs.

94. Specifically, the following text can be proposed for consideration for insertion into GATT Article XXIV or the 1994 Understanding (with reference to the original paragraph numbers):

‘Where developing countries are parties to an agreement for the formation of a customs union, a free trade area, or an interim arrangement leading to either a customs union or a free trade agreement, flexibility shall be provided for regarding the conditions set out in paragraphs 5 to 9 inclusive, in

<sup>86</sup> The scope of Article IX is limited by its paragraph 2, which stipulates that interpretation under the Article does not undermine Article X procedure of amendment.

<sup>87</sup> The approach adopted in the Uruguay Round was to reach a new agreement in the form of an ‘understanding’ distinct from GATT 1947, thus the provisions relating to amendment (Article XXX) or interpretation through joint action of the contracting parties (Article XXV) under the old GATT 1947 were not followed. Various understandings contained in Annex IA of the WTO Agreement constitute integral parts of GATT 1994, which forms a part of a ‘Multilateral Agreement on Trade in Goods’. It is not clear, therefore, whether the modification brought in the 1994 Understanding amounts to the adoption of a new ‘interpretation’ or to the ‘amendment’ of the existing agreement, since the procedural requirements differ.

particular with reference to subparagraph 5(c) and paragraph 8(a)(i) and (b), in accordance with the level of development of the countries concerned, both overall and in individual sectors and sub-sectors’.

95. This option has the advantage of being able to incorporate SDT as a modality for differentiating the GATT Article XXIV requirements based on the level of development of the parties to an RTA, without specifically addressing *a priori* each and every element of the requirements, which may prove to be contentious among WTO Members.<sup>88</sup> A generic provision could guarantee a relatively more favourable treatment for developing countries with regard to the key requirements of GATT Article XXIV.<sup>89</sup>

96. In practice and eventually, however, the overall degree of flexibilities to be made available through SDT to developing countries in this manner depends critically on how the generally applicable requirements of GATT Article XXIV (i.e. ‘existing flexibilities’), as well as the concrete terms of ‘flexibility’ (i.e. ‘additional flexibilities’) to be made available to developing countries, are defined, as the generic SDT would be geared towards individual substantive and procedural requirements and thus would be built upon existing flexibilities.<sup>90</sup> Therefore, the option may necessitate a redefinition of the scope of existing flexibilities, as well as of the concrete terms of ‘flexibility’ (i.e. ‘additional flexibilities’) to be made available to developing countries.<sup>91</sup>

(ii) *Redefinition through SDT of GATT 1994 Article XXIV:5-8*

97. The second possibility is to incorporate SDT in a specific manner by individually redefining each substantive and procedural requirement under GATT Article XXIV. This approach directly addresses the manner in which the Article is interpreted, thereby seeking to redefine the scope of the existing flexibilities under the article and enlarge them through SDT for developing countries only.

98. This approach represents in itself a fully fledged alternative to the first approach on generic SDT, but could be complementary to it. As noted, the incidence of generic SDT would depend on the scope of generally applicable existing flexibilities under GATT Article XXIV, and negotiations may further require the definition of concrete terms of ‘additional flexibilities’ to be made available to developing countries. Indeed, the actual negotiations under the Doha agenda on the WTO rules applying to RTAs could focus on the clarification and redefinition of specific requirements under Article XXIV of GATT 1994 as systemic issues. Thus, while the two approaches are equivalent to the extent that the same degree of flexibilities are made available to developing countries, this second approach is complementary to the first one in that it operationalises the generic notion of ‘flexibility’ in concrete terms. Possible elements of ‘additional flexibilities’ to be made available through SDT for developing countries in respect of each requirement are discussed in chapter IV.

(iii) *Revision of GATT Article XXIV:10*

99. The third possibility differs from the former two approaches in that it seeks to provide derogation under more favourable terms for developing countries from the substantive requirements

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<sup>88</sup> For example, a contentious issue such as the definition of SAT may fail to be addressed in the actual negotiations. If SDT needs to be defined on each and every single requirement of GATT Article XXIV:5-8 in a specific manner, it may result in no SDT being formally introduced in respect of the requirement if the negotiations fail. In contrast, a generic provision, if agreed, could then guarantee at least a greater flexibility for developing countries relative to the prevailing level of flexibility even if there is no agreement on the definition of a given requirement.

<sup>89</sup> GATS Article V:3(a) does not contain a specific definition of ‘flexibility’.

<sup>90</sup> For instance, assuming that ‘flexibility’ is understood as a 10% discount from the generally applicable threshold level, if the ‘substantially-all-the-trade’ requirement is defined generally as the trade coverage of 80%, then ‘flexibility’ would entitle developing countries the coverage of 72%. If the general threshold level is set at 95%, then the threshold level for developing countries would rise to 85.5%.

<sup>91</sup> Maximising the overall degree of flexibilities available to developing countries would thus require maximisation of the degree of generally applicable ‘existing flexibilities’.

of GATT Article XXIV. As such, the option is only complementary to the above two approaches. GATT Article XXIV:10 reads as follows:

‘The CONTRACTING PARTIES may by a two-thirds majority approve proposals which do not fully comply with the requirements of paragraphs 5 to 9 inclusive, provided that such proposals lead to the formation of a customs union or a free-trade area *in the sense of this Article*’. (Emphasis added)

100. One way to incorporate SDT in GATT Article XXIV is to amend this paragraph to the effect that special treatment be provided to those proposals on RTAs involving developing countries by allowing less stringent procedural requirements such as a simple, rather than two-thirds, majority. However, the substantive requirement that such a proposal should lead to the formation of customs union or FTA ‘in the sense of this Article’ limits the scope of derogation only to the transitional period leading to the formation of GATT-compatible RTAs.<sup>92</sup> Thus, if SDT is provided for developing countries on a permanent basis, there still remains the need to incorporate SDT in the substantive requirements of GATT Article XXIV:5-9 through either of the former two options. Hence, the option is not substitute for the above two approaches.

101. In the alternative, the revision could be made to delete the qualification attached to the paragraph (‘in the sense of this Article’) so that the final ‘RTAs’ not fully meeting the requirements of paragraphs 5-9 could also be authorised specifically for developing countries, possibly under certain other conditions. Without reform of the substantive requirements of GATT Article XXIV, however, this could result in only a minimum degree of flexibility (among the three options) being made available to developing countries, as the option would only entitle derogation from current general rules subject to approval by WTO Members, which in procedural terms would be similar to the granting of a waiver (even with less stringent procedural requirements such as a simple majority). Combined with substantive reform, this option could provide additional elements of flexibility for developing countries by opening the possibility for derogation from even reformed rules that would contain SDT in substantive and procedural requirements. In this case, however, the question is to what extent it would be appropriate to authorise derogation from general rules on a permanent basis for developing countries.

#### **III.4(b) Reforming Part IV of GATT 1994**

102. Another conceivable option is to amend Part IV of GATT 1994 to make it applicable to regional trade negotiations. This could also be taken up in the context of a broader review of the concept of SDT under the WTO, as mandated by paragraph 44 of the Doha Declaration wherein it was provided that ‘all special and differential treatment provisions shall be reviewed with a view to strengthening them and making them more precise, effective and operational’. GATT Article XXXVI (principles and objectives), paragraph 8, stipulates that:

‘(t)he developed contracting parties *do not* expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of less-developed contracting parties’ (emphasis added).

103. The paragraph is supplemented by an endnote (ad Article XXXVI) as follows:

‘This paragraph would apply in the event of action under Section A of Article XVIII, Article XXVIII, Article XXVIII *bis*, Article XXXIII or any other procedure *under this Agreement*’ (emphasis added).

104. As discussed in Chapter II, one of the reasons why the panel established in the dispute settlement case, ‘EEC-Member States’ import regimes for bananas’ (‘*Bananas II*’) initiated in 1993, did not accept the EC’s claim that the Lomé Convention was covered under GATT Article XXIV read

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<sup>92</sup> Since during a transitional period it is normal for an RTA not to fulfil all the requirements of Article XXIV:5-9, and such practices have presumably been tolerated under existing flexibilities, paragraph 10 has in some sense been redundant on ‘interim arrangement’, and of little use in practice.

in conjunction with Part IV lies in its determination that the above-mentioned endnote limits the applicability of Article XXXVI:8 to negotiations undertaken within the framework of the GATT, and not those undertaken outside it, such as in a regional context.<sup>93</sup> Thus, possibly some modification could be made to this endnote in order to render the article applicable to regional trade negotiations involving developing countries.<sup>94</sup> Alternatively, a reference could be made in GATT Article XXIV to Article XXXVI:8 to the effect that the non-reciprocity principle of the latter would be taken into consideration when assessing the conformity of North–South RTAs to GATT Article XXIV requirements.

105. The above-mentioned panel’s conclusion on the Lomé Convention, however, points to the fundamental irrelevance of SDT as defined in GATT Article XXXVI:8 to the application of the GATT Article XXIV requirements to RTAs in two respects. First, GATT Article XXXVI:8 applies specifically to the *conduct of multilateral trade negotiations*, whereas negotiations for the formation of an RTA are outside the scope of GATT 1994. Thus, GATT Article XXXVI:8 could not be made applicable to regional trade negotiations by definition. Second, GATT Article XXIV does not define the conduct of regional trade negotiations; it merely sets out multilateral conditions that WTO Members must fulfil when they choose to form an RTA at their discretion. This requires SDT in the context of GATT Article XXIV to apply to the *application of WTO rules*, namely Article XXIV conditions in assessing the GATT conformity of RTAs.<sup>95</sup> However, the non-reciprocity principle in GATT Article XXXVI:8 applies to the conduct of multilateral trade negotiations and would thus be irrelevant to the consideration of whether an RTA has fulfilled the conditions set out in GATT Article XXIV. Thus, this option is likely to prove to be less sustainable in the Doha negotiations on RTAs.

#### III.4(c): Reforming the Enabling Clause

106. A third option is to exclude the North–South RTAs from the purview of Article XXIV of GATT 1994 by amending the Enabling Clause in such a way that it also covers North–South RTAs formed between developed and developing countries. At present, the Enabling Clause covers only RTAs formed among developing countries. To the extent that the legal validity of the Enabling Clause is not contested, this would appear an option, as it would exempt more the ACP States from obligations they would have to incur under Article XXIV of GATT 1994. For instance, its paragraph 2(c) could be modified to read as follows (the suggested texts are underlined):

‘1. Notwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties.

2. The provisions of paragraph 1 apply to the following: [...]

(c) Regional or global arrangements entered into involving (‘amongst’ in the original text) less-developed contracting parties for the mutual reduction or elimination of tariffs and ... non-tariff measures, on products imported from one another. Such arrangements include those formed among developing countries as well as those between developing countries on the one hand, and developed countries on the other, whether they be negotiated or concluded individually or collectively (no reference made in the original text)’.

107. As the Enabling Clause foresees the ‘review of operation’ of its provisions, and the review of all existing SDT provisions has been mandated in the Doha Ministerial Declaration in its paragraph 44, the possible inclusion into the scope of the Enabling Clause those trade agreements formed between developing and developed countries may well be taken into account in such a review.

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<sup>93</sup> Panel report, *EEC-Member States’ import regimes for bananas* (DS38/R), *op. cit.*

<sup>94</sup> Given that future EPAs, unlike the Lomé Convention, would presumably enjoy substantially full reciprocity with the EU, they could more credibly claim legal coverage under Article XXIV of GATT read in conjunction with Part IV of GATT as free trade areas even without any reform linking the two articles.

<sup>95</sup> This could also be inferred from the design of different provisions on SDT in GATS. While GATS contains an SDT comparable to GATT Article XXXVI:8 applicable to multilateral trade negotiations, namely GATS Article XIX:2, it also provides specifically an SDT applicable to conditions set out in GATS Article V:1 (GATS V:3(a)).

108. One serious shortfall with this option is that the legal validity of Enabling Clause in general, and its coverage of agreements formed among developing countries in particular, is increasingly being subjected to pressure from some WTO Members. For instance, it has indeed been contested whether the Enabling Clause covers RTAs formed among developing countries at all.<sup>96</sup> Also Australia has proposed to bring those RTAs formed pursuant to the Enabling Clause under the disciplines of Article XXIV of GATT 1994 and the purview of the Committee on Regional Trade Agreements. Thus, in opening negotiations on the reform of the Enabling Clause there is a risk that it may lead to the weakening of the clause in its coverage of South–South RTAs.

109. A reform of the Enabling Clause in this manner would also have wider systemic implications. Without any formal link to GATT Article XXIV conditions, the option may provide scope for legalising non-reciprocal, unilateral preferences under the cover of a ‘regional trade agreement’, thereby allowing them to circumvent the waiver requirements for non-generalised, non-reciprocal preferential schemes like the Cotonou preferences for which WTO waivers are necessary. Furthermore, the Enabling Clause requirement that unilateral preferences are only allowed under GSP schemes (paragraph 2(a)) could then be bypassed, and the viability of the GSP would be put into question.

110. Against this background, it can be concluded that, among the three options examined, reforming GATT Article XXIV through the incorporation of generic paragraph on SDT and/or specific SDT provisions in respect of individual requirements of GATT Article XXIV:5-8 would be the most viable option for modification of the WTO rules on RTAs to introduce differential and more favourable treatment for developing countries.

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<sup>96</sup> A WTO publication notes that the omission in the Enabling Clause of any reference to Article XXIV of GATT has ‘left unclear whether the Enabling Clause applies in situations where that Article does not, or affects the terms of application of that Article, or represents, for developing countries, a complete alternative to the Article’, WTO (1995), *op. cit.* p.18. The formation of MERCOSUR and its notification under the Enabling Clause to the then GATT 1947 gave rise to intense debate as to whether it should be subject to the requirements of Article XXIV of GATT 1994.

**Chapter IV**  
**ELEMENTS OF 'FLEXIBILITY' FOR DEVELOPING COUNTRIES**  
**IN ARTICLE XXIV OF GATT 1994**

111. The analysis in the previous chapter concluded that the direct incorporation of SDT provisions within the substantive and procedural requirements of GATT 1994 Article XXIV would be the most sound and viable option for reforming the WTO rules on RTAs to make them more development friendly, while also meeting the systemic need to minimise the inward-looking, exclusive trading blocs. Whether SDT is defined in generic or specific terms, ensuring the appropriate overall degree of flexibility for developing countries would necessitate operational definitions of both generally applicable 'existing flexibilities' and 'additional flexibilities' specifically for developing countries in terms of the requirements of GATT Article XXIV. This chapter focuses on the 'additional flexibilities', namely SDT, for developing countries, and examines the modalities for rendering them operationally available to developing countries in respect of each condition of GATT Article XXIV.

112. Annex 2 provides a tentative summary of possible elements of 'additional flexibilities' likely to be required by developing countries and possible modalities for reform in terms of the key requirements of GATT Article XXIV:5-8. In principle, it is assumed that these elements of flexibilities are to be applicable to all developing countries without discrimination. If deemed appropriate, however, given the particular situation of LDCs and small vulnerable economies in the context of economic partnership agreements (EPAs), all or parts of the elements of flexibilities might be selectively applied to LDCs and (low-income) small and vulnerable developing countries based on some objective criteria, in line with Annex VII of Agreement on Subsidies and Countervailing Measures (ASCM), where special treatment is granted to a group of selected countries.<sup>97</sup> In such cases the definitional issue of country groups has to be addressed.<sup>98</sup>

#### **IV.1 SAT REQUIREMENT (GATT ARTICLE XXIV:8(a)(i) AND (b))**

113. As a result of negotiations during the Uruguay Round, clarifications were made by the 1994 Understanding specifically to the paragraphs 5, 6 and 12 of GATT Article XXIV. However, the most controversial notion of the 'substantially all the trade' (SAT) requirement (GATT Article XXIV:8(a) and (b)) failed to be tackled within the 1994 Understanding.

##### **IV.1 (a) Duties**

114. The interpretation of the term 'substantially all the trade', for which duties and other regulations of commerce should be eliminated between the parties to an RTA, has long been the most controversial of all the 'systemic' issues arising from multilateral disciplines under Article XXIV of GATT. Apart from the desirability of having such a fixed interpretation, the disagreement has pertained to methods for measuring empirically the SAT requirement, as well as the objective criteria for evaluating the threshold level for meeting that requirement. The measurement issue pertains to the methodology to be used for calculating the SAT requirement, in particular (1) the level of aggregation, (2) the subject matter of measurement, (3) sectoral composition, and (4) treatment of non-zero, less-than-MFN duties, and (5) the setting of objective, fixed statistical criteria.

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<sup>97</sup> Annex VII of ASCM derogates prohibition under Article 3:1(a) of export subsidies for certain developing countries, together with LDCs, as long as their per capita GDP does not exceed US\$1,000 per annum.

<sup>98</sup> The WTO Work Programme on Small Economies may prove to be relevant for this purpose. However, its mandate under Doha Ministerial Conference in its paragraph 35 specifies that its aim is 'not to create a sub-category of WTO Members'.

(i) *Level of aggregation*

115. The level of aggregation concerns whether the SAT requirement is to be measured at the aggregate intra-regional trade or individual country level. If measured at the aggregate regional level, there is no guarantee that a minimum level of reciprocity is struck between the partners, especially if there is a wide imbalance in bilateral trade flows. Thus, measurement of the SAT requirement at the aggregate intra-regional trade level would allow greater flexibility for developing countries.

116. In the case of a new RTA that is formed between two or more pre-existing RTAs, assessing the SAT requirement in terms of an individual member's percentage share of import volume free of duty from each and every partner in the other side of pre-existing RTAs would pose an unnecessarily stringent requirement. For this type of RTA, it should be sufficient that the SAT requirement applies only to the trade aggregated at the subregional level so as to treat each pre-existing RTA as a unit for the purpose of measurement, irrespective of whether they are an FTA or a customs union.<sup>99</sup> The trade of these units could be measured, like individual countries, either at the aggregate overall RTA level, or at the individual pre-existing RTA (unit) level. This latter approach is particularly pertinent to EPAs comprising pre-existing ACP subregional groupings. If the SAT requirement is measured at the individual country level, it would be extremely difficult for ACP States party to such EPAs to meet the criterion, even if the ACP subregional groupings had undertaken a thorough liberalisation among themselves in advance of forming an EPA with the EU. As ACP subregional groupings are often formed under the Enabling Clause conditions, they may be enjoying lower trade coverage than would have been required under Article XXIV of GATT conditions ('WTO-minus'). Thus, measurement of intra-RTA trade based on aggregated trade at each subregional grouping level would prove to be most appropriate for developing country groupings.

(ii) *Subject matter of measurement*

117. As to the subject matter of measurement for the purpose of the SAT requirement, it has been well documented that there exist two different, not mutually exclusive, measurement approaches – quantitative and qualitative.<sup>100</sup> The quantitative approach measures the volume of trade actually taking place within RTAs and evaluates the SAT requirement in terms of a statistical benchmark, that is, the total percentage share of trade volume free of duty.<sup>101</sup> This approach has been subject to criticism<sup>102</sup> on the ground that it does not appropriately take into account the impact of prohibitive duties on internal trade. Since the quantitative approach only measures actual trade, it may not capture the potential trade that could have taken place but which has been impeded because of residual prohibitive tariffs or other restrictive trade measures. This may result in a major sector being entirely excluded from the RTA coverage because there is little or no internal trade in that sector. Indeed, the quantitative approach has an incentive to increase prohibitive barriers to trade.

118. The qualitative approach measures not trade actually happening but products that are subject to internal liberalisation programmes based on, *inter alia*, a product classification for tariff purposes. In this approach, the SAT requirement is measured in terms of the total percentage share of those tariff lines with zero duty under an RTA.<sup>103</sup> The approach can address the perceived deficiencies of the quantitative approach by capturing those tariff lines in which no or little trade is actually happening. The approach, however, may fail to gauge actual trade flows if the initial intra-regional trade is concentrated in a narrow range of products.

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<sup>99</sup> Davenport (2002), *op.cit.* In principle, the issue does not arise in the case of customs unions that adopt common external tariffs, and hence there is no need for country-level measurement.

<sup>100</sup> WTO (2000) and (2002b).

<sup>101</sup> A refined version of this approach is to measure the percentage share of intra-RTA trade undertaken under preferential rules of origin over all intra-RTA trade.

<sup>102</sup> Australia's position exemplifies this view. See, for example, *Submission by Australia* (TN/RL/W/15), 9 July 2002.

<sup>103</sup> It has been proposed to measure product coverage at HS 6-digit level. See, for example, *Submission by Australia*, *ibid*, WT/REG/W737 and TN/RL/W/15, *op. cit.*

(iii) *Sectoral composition*

119. In addition, if the SAT requirement is measured across the board without regard to sectoral composition, a significant proportion of a major sector (e.g. agriculture) may be excluded altogether from the internal liberalisation programme. The coverage of 90% of HS 6-digit level tariff lines, for instance, would still exclude more than 500 headings. One way to address this shortfall is to measure the percentage of tariff lines freed from duty, instead of across the board, within each sector, such as at the HS 2-digit chapter level.<sup>104</sup> In the context of EPAs, since the export structure of ACP States is highly concentrated on a small number of commodities, it is important that EPAs cover on the EU-side commodities of export interest to ACP States beyond the multilateral SAT requirement.<sup>105</sup>

(iv) *Non-zero preferential duties*

120. Another issue relating to the SAT requirement is the treatment of residual non-zero, less-than-MFN, preferential tariffs. Under existing RTAs, non-zero preferential duties are often maintained in the agricultural sector, where the exchange of concessions tends to consist in preferential reduction, instead of elimination, of duties.<sup>106</sup> Whether trade/products subject to non-zero preferential duties should be included in the SAT requirement is an unresolved systemic issue. Since the major concerns of developing countries, in particular the small and vulnerable among them, in internal trade liberalisation pertain as much to competitiveness and protection of domestic industries as to fiscal contraction, some provision under individual RTAs for tariff harmonisation instead of elimination may facilitate the transition to liberalisation and help to minimise distortive incentives arising from the tariff structure. In this regard, the SAT requirement could, as SDT, take into account the reduced non-zero preferential tariffs in the calculation of SAT for developing countries, possibly under certain conditions (e.g. a requirement to reduce base rates by a certain percentage and/or to below a certain percentage, possibly harmonised across the board). This could facilitate meeting the SAT requirement for developing countries while maintaining certain tariffs for government revenue and industry support.

121. Given that the assessment of the SAT requirement for an RTA member depends critically on the methodology chosen, in terms of the level of aggregation, the subject matter of measurement, the sectoral coverage requirement and the treatment of non-zero preferential duties, SDT in respect of the SAT requirement could include the following elements. First, a choice needs to be made with regard to the level of aggregation: whether SAT is measured at the level of regional trade as a whole, or country level imports. The SAT determination based on aggregate intra-RTA trade volume would leave greater flexibility for parties to mixed-RTAs. Second, if the country level approach is deemed appropriate, it may be suited for the purpose of SDT to apply asymmetrically different approaches with different requirements for developed and developing countries in terms of subject matter (quantitative versus qualitative approaches), sectoral requirements, and the treatment of non-zero preferential duties. For instance, a provision could be conceivable whereby the SAT requirement for a developed country member is determined by a combination of quantitative and qualitative approaches with regard to sectoral coverage, while for developing countries just one of the two, possibly the

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<sup>104</sup> See Davenport, *op. cit.*

<sup>105</sup> The average number of export commodities for ACP regions at the SITC 3-digit level (total 239) is 13 for Caribbean States (1997), 22 for Africa (1997) and 4 for the Pacific (1993). See UNCTAD (2002).

<sup>106</sup> Another form of special treatment often applied to agricultural products in an RTA is the tariff rate quota (TRQ). In terms of the GATT compatibility of the maintenance of TRQ *vis-à-vis* intra-RTA imports, TRQ may most likely be considered as a form of 'other restrictive regulations of commerce' (ORRCs) in the sense of Article XXIV:8, and thus would affect the extent to which a member of an RTA has met the SAT requirement. For example, if country A applies a TRQ on a commodity (e.g. bananas) imported from country B, a large share of whose intra-RTA exports to country A is accounted for by that commodity subject to the TRQ (e.g. 50% of total imports of country A from country B is accounted for by banana subject to a TRQ), then there is a risk that that country A may not meet the SAT requirement. Thus, whether or not the application of TRQ works for the purpose of WTO conformity of an RTA would depend on (1) whether TRQ constitutes an ORRC in the sense of GATT Article XXIV:8, and if not, (2) the importance (share) of that commodity in the total intra-RTA imports of a given country.

quantitative approach, could be applied for the measurement of imports on an across-the-board basis, thus without, or with lesser, regard to sectoral coverage, taking account non-zero preferential duties.

(v) *Fixed statistical criteria*

122. The setting of objective, fixed statistical criteria for evaluating the SAT requirement is an independent issue that is relevant to all four areas of measurement (i.e. the level of aggregation, subject of measurement, sectoral coverage and non-zero preferential duties). The threshold level of 80–95% has been cited as such a criterion. Whatever criterion is chosen, however, its impact depends critically on the measurement issues discussed above in assessing trade/product coverage. In this regard, there have been to date no agreed criteria in WTO practice. Fixed criteria, if agreed, would be conducive to instituting SDT in objectively measurable terms, as they would enable Members to set lower criteria for developing countries than for developed countries. For instance, if the coverage of 90–95% of both actual trade and HS 6-digit tariff lines with each HS 2-digit chapter is deemed required for developed countries, the coverage for developing countries may be set at 70% of actual trade across the board only, also taking account of trade subject to non-zero preferential duties. The modulated threshold criteria could be applied to both the quantitative and qualitative approaches, as well as in measuring sectoral coverage.

#### **IV.1(b) Other restrictive regulations of commerce (ORRCs)**

123. Another aspect of the SAT requirement pertains to non-tariff barriers (NTBs) to trade. Article XXIV:8 of GATT 1994 stipulates that ‘other restrictive regulations of commerce’ (ORRCs), together with customs duties, should be eliminated with respect to substantially all the trade of parties to an RTA. Explicit exemptions are made with regard to those permitted under GATT Articles XI (quantitative restrictions), XII (balance of payments), XIII (non-discriminatory administration of quantitative restrictions), XIV (exceptions to the rule of non-discrimination), XV (exchange arrangements) and XX (general exceptions). The non-reference in the article to such contingency measures as anti-dumping and countervailing duties (Article VI) or safeguards (Article XIX) has given rise to the debate as to whether and how members of an RTA are allowed/forbidden/obliged under Article XXIV of GATT 1994 to apply those measures among themselves and with regard to third parties.<sup>107</sup> Recently, concern has also been raised over regional regulation of sanitary, phytosanitary and technical standards and regulations, as it is equally unclear whether those SPS/TBT standards are included in the scope of ORRCs.

124. The GATT-conformity of preferential (non-)application of these non-tariff measures within RTAs appears to depend critically on whether or not those measures are ‘necessary’ for the formation of RTAs in the sense of Article XXIV: 5 and 8 of GATT 1994. To the extent of their necessity (and proportionality) for the formation of an RTA, otherwise GATT-inconsistent measures can find justification under Article XXIV:8 of GATT. Such a ‘necessity test’ was developed by the Appellate Body in the *Turkey-Textile* case. It asserts that in order for an RTA to be eligible for defence under Article XXIV of GATT against the claim of MFN violation, it is incumbent on the party to the RTA to demonstrate that the measures in question are ‘necessary’ for the formation of RTA, in the absence of which the formation of the RTA would have been impossible, and that the measures at issue were introduced upon the formation of RTA in the sense of Article XXIV:5 and 8 of GATT.<sup>108</sup>

125. The degree of ‘necessity’ depends, in turn, on the definition of ORRCs. Three interpretations have been put forward in this regard. First, if the list of exceptions under Article XXIV:8 of GATT is interpreted as exhaustive, the preferential application of those measures not covered in the list, including trade remedies and SPS/TBT standards, should be deemed ‘forbidden’ among RTA partners. Second, if the list of exceptions is only illustrative, then RTA members are ‘obliged’ to

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<sup>107</sup> For a discussion of the scope of ORRCs in relation to SPS and TBT, see Trachtman (2002).

<sup>108</sup> *Turkey-Textile Appellate Body Report, op. cit.*, paragraph 46.

apply those measures not listed to the RTA partners so that MFN obligation under GATT Article I:1, as incorporated in relevant provisions of WTO agreements, is given precedence over Article XXIV of GATT. The third ‘flexible’ interpretation, supported by the EU in the context of global safeguards, is that the application of those measures to RTA partners is ‘permitted but not obliged’ to the extent that their application does not prejudice the rights of third parties.<sup>109</sup>

126. Examination of the three interpretations in the context of the ‘necessity test’ points to a possible need to relax the criteria for meeting the test, as only the strict interpretation of ORRC (the first interpretation) could pass it. In order not to impede unnecessarily the formation of RTAs, while not inhibiting unnecessarily the right of RTA members to apply non-tariff measures to intra-RTA trade, the necessity test might need to be balanced with the kind of test that weighs up the economic effects of the measures in question in promoting the purposes of requirements under Article XXIV:5 and 8 of GATT, namely, the maximisation of the benefits from internal trade liberalisation and minimising adverse effects on third parties. Such an ‘economic test’ could usefully supplement the ‘necessity test’ in determining the degree of necessity so as to enable analysis based not only on the statutory provisions but also on the economic effects of the measures.

127. So the key issue in respect of possible reforms in WTO rules relating to safeguards, trade remedies and SPS/TBT standards is for clarification of the interpretation of ORRC in such a way as to permit, but not oblige, WTO Members to apply preferentially those non-tariff measures to intra-RTA trade. This requires an interpretation of the scope of ORRC as not including those trade contingency measures or including only part of SPS/TBT standards. Thus, the list of exceptions in Article XXIV:8 of GATT is to be understood as illustrative, not exhaustive. In addition, elements of SDT would need to be incorporated in the definition of ORRC so as to allow for elements of asymmetry in the rights and obligations under RTAs in favour of developing countries. The definition of ORRC with SDT would enable developing countries to apply intra-RTA safeguard, anti-dumping and countervailing measures, while developed countries would not to be obliged to apply global safeguards and other trade remedies to its intra-RTA trade with developing country partners. Although such a ‘flexible’ interpretation has already been put forward with regarding ORRC (e.g. the EU’s interpretation of safeguards),<sup>110</sup> the notion of SDT will more effectively cover elements of greater flexibility for developing countries.

128. In addition, ensuring the GATT-compatibility of preferential applications of non-tariff measures within an RTA in terms of the MFN obligations (e.g. the exclusion of RTA partners from the application of global safeguards and other trade remedies; raising *de minimis* levels only for RTA partners in the application of trade remedies; regional mutual recognition agreements, or MRAs, that are closed to third parties) would necessitate clarification not limited on Article XXIV of GATT but throughout GATT 1994. The relationship between rights and obligations under Article XXIV of GATT on the one hand, and Article I:1 of GATT 1994 as incorporated in various WTO agreements (GATT Articles VI and XIX, ASG, Agreement on the Implementation of Article VI of GATT 1994 (AAD), ASCM and SPS/TBT) on the other, would need clarification and adjustment. Ensuring the legality of such preferential non-tariff measures under WTO rules might amount to an interpretation with regard to the legal standing of Article XXIV of GATT as providing a comprehensive exemption from the MFN obligation with regard to non-tariff measures, as well as tariff treatment, even though Article XXIV:8 of GATT does not require their elimination. This requires the relaxation of the ‘necessity test’ and the introduction of a complementary economic balancing test to strengthen the applicability of Article XXIV:8 of GATT to non-tariff measures that are not necessarily required to be eliminated under the Article (thus outside of ORRC). This increases the possibility that preferential application of non-tariff measures, including regional Mutual Recognition Agreements (MRAs),

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<sup>109</sup> WT/REG/W/37, *op. cit.* The EU is reported to hold the view that the intra-RTA safeguard measures are only allowed during the transitional period of an agreement, after which other legislation such as competition policy should supersede the trade remedy laws.

<sup>110</sup> WT/REG/W/37, *op. cit.*

would be justified under Article XXIV:8 of GATT. The systemic implications of this issue requires in-depth examination.

(1) *Safeguards*

129. The application of safeguard measures by members of an RTA has proved to be the most problematic of all trade remedies in relation to GATT Article XXIV.<sup>111</sup> This is because safeguard measures are origin-neutral, to be applied to imports ‘irrespective of its source’ (Article 2 of the Agreement on Safeguards, ASG), as opposed to the origin-specific anti-dumping or countervailing measures. Although the footnote to Article 2 of ASG stipulates that ‘Nothing in this Agreement prejudices the interpretation and the relationship between Article XIX and paragraph 8 of Article XXIV of GATT 1994’, all the requirements of Article XIX and ASG are deemed to apply also to the members of an RTA. Panel and Appellate Body rulings under dispute settlement cases have indeed confirmed that members of an RTA should also be subject to the same requirements as any other WTO Members, and are therefore obliged to apply ‘symmetry’ or ‘parallelism’ in the determination of serious injury or threat thereof to domestic industry and the (selective) application of global safeguard measures.<sup>112</sup>

130. Nonetheless, it is unclear from WTO jurisprudence whether a member of an RTA that applies safeguard measures in full conformity with all procedural obligations of Article XIX of GATT 1994 and ASG (thus applying ‘parallelism’ in the determination of domestic injury and the application of safeguards), is justified in excluding its RTA partners from the application of global safeguards on the basis of GATT Article XXIV:8. This seems to depend on the aforementioned ‘necessity test’. To the extent that the elimination of safeguards within RTAs is not required or necessary (as would be suggested by the second and third interpretations above), GATT Article XXIV is unable to provide justification to the otherwise GATT-inconsistent exclusion of RTA partners from global safeguards. The first interpretation of the ORRC would lead to the opposite conclusion that GATT Article XXIV:8 provides a defence for the MFN violations as they are required and necessary for the formation of the RTA in the sense of Article XXIV:8. But this interpretation would contradict the fact that the majority of RTAs apply safeguard measures to the intra-RTA trade.

131. In practice, safeguard provisions under RTAs distinguish between RTA-specific safeguards and global safeguards, and those applicable during and after the transitional period. During the transitional period, it appears to be the norm that RTAs provide for transitional RTA-specific safeguard measures in the form of the suspension of staged tariff reductions and/or raising of applied rates at that moment.<sup>113</sup> Intra-RTA safeguard action during the transitional period is less problematic as it could take the form of suspending the progressive elimination of duties for the product concerned by increasing applied rates up to the base rates, MFN applied rates or under a certain maximum percentage point (e.g. 20–25%), whichever is the lower. Some RTAs explicitly provide for asymmetric transitional safeguard measures during the transitional period whereby only one (developing country) party is entitled to safeguard measures.<sup>114</sup> Since the provisions of GATT Article

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<sup>111</sup> Application of global safeguard measures by a member of an FTA and the treatment of its FTA partners, have raised several dispute settlement cases, including: *United States - definitive safeguard measures on imports of wheat gluten*; *Argentina - safeguard measures on imports of footwear*; and *United States - safeguard measures on imports of fresh, chilled or frozen lamb from New Zealand and Australia*.

<sup>112</sup> In the *US - wheat gluten* case, the exclusion of NAFTA partners (Canada) from the application of definitive safeguard measures by the US on wheat gluten was found inconsistent with its obligations under the Agreement on Safeguards to apply ‘symmetry’ between investigation for serious injury and application of safeguard measures. The US investigating authority had included imports from Canada in its determination of serious injury but had excluded Canada from the application of safeguards, thereby failing to apply ‘symmetry’. Report of the Panel and the Appellate Body, *US - wheat gluten* (WT/DS166/R and WT/DS166/AB/R, respectively).

<sup>113</sup> For example, in the EC– Tunisia and EC–Morocco Euro-Mediterranean Agreements, EC– South Africa FTA, EC– Mexico FTA, Canada-Chile FTA, Canada-Cost Rica FTA, Chile-Mexico FTA, and EFTA-Morocco FTA.

<sup>114</sup> For example, the EC–South Africa FTA, EC–Morocco and EC–Tunisia Euro-Mediterranean Agreements. Article 25 of EC– South Africa FTA provides for transitional safeguard measures as ‘exceptional measures of limited duration’ ‘by South Africa in the form of an increase or reintroduction of customs duties’ not exceeding ‘the level of the basic duty or

XXIV:8 can not be considered as applicable to ‘RTAs’ during the transitional period (as they are under ‘transition’ to full RTAs, and are thus an ‘interim arrangement’ in the sense of Article XXIV:5), the question of ORRC does not arise.

132. Once the full RTA (FTA or customs union) has been established, however, the question of ORRC becomes relevant, and the legal consequences of applying safeguard measures to intra-RTA trade needs to be addressed. The majority of RTAs provide for RTA-specific safeguard measures on the assumption, or with explicit provision to that effect, that RTA partners are excluded from the application of global safeguards,<sup>115</sup> while some RTAs apply only global safeguards once the transitional period has expired.<sup>116</sup> Yet other RTAs simply oblige parties not to apply safeguard measures, RTA-specific or global, to each other’s trade.<sup>117</sup>

133. Developing countries would need intra-RTA safeguard measures during and after the transitional period in order to cater for unforeseen developments in their intra-group trade. At the same time, the application of those measures by developed countries could be subject to certain stringent conditions. In this light, elements of greater flexibility under a mixed North–South RTA for developing countries with regard to safeguard measures would include the following:

- (1) during the transitional period, asymmetric rights for developing countries to apply transitional intra-RTA safeguard measures (in line with those provided under the EC–South Africa and Euro-Mediterranean Agreements) below the base rate, MFN bound/applied rates or a certain maximum rate (e.g. 30%);<sup>118</sup>
- (2) after the transitional period, (asymmetric) rights for developing countries to apply intra-RTA safeguard measures, while developed countries are (prohibited from or) entitled to it subject to more stringent requirements in terms of, *inter alia*, ‘serious injury’ tests, as well as procedural requirements including consultation and compensation; and
- (3) asymmetric obligation (subject to the requirements of the ASG and GATT XIX) for developed countries to exclude developing country partners from the application of global safeguards, possibly under certain favourable conditions for developing countries, while developing countries are permitted to apply global safeguards to their intra-RTA trade;<sup>119</sup> and
- (4) as an alternative to (2) and (3), in case only global safeguards are to be applied to intra-RTA trade (thus no specific provision for RTA-specific safeguards), asymmetric obligation for

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the applied MFN rates of duty or 20% *ad valorem*, whichever is lower’, while maintaining ‘elements of preference’ for EC products; on products ‘not exceeding 10% of total imports of industrial products’ for a period ‘not exceeding 4 years’, with a prohibition of back-to-back application within 3 years (WT/REG114/1). Article 14 of the EC–Morocco and EC–Tunisia Euro-Mediterranean Agreements both provide for more favourable treatment for Morocco and Tunisia, as transitional safeguards measures are allowed up to 25% *ad valorem* duty with regard to the maximum value of imports of 15% of total imports for a maximum period of 5 years (WT/REG69/1). However, transitional safeguard measures apply to both industrial and agricultural goods in the case of EC–South Africa FTA, whereas they are limited to industrial products in the case of the Euro-Mediterranean Agreements.

<sup>115</sup> For example, EC–Tunisia and EC–Morocco Euro-Mediterranean Agreements, EC–Mexico FTA, EFTA–Mexico FTA, EFTA–Morocco FTA, Canada–Chile FTA, Chile–Mexico FTA and Mexico–Israel FTA. Canada–Chile FTA, Chile–Mexico FTA and Mexico–Israel FTA explicitly oblige parties to exclude each party from the application of global safeguard measures unless: (a) imports from the other party account for a ‘substantial share of total imports’; and (b) imports from the other party contribute ‘importantly’ to the serious injury, or threat thereof, caused by total imports (WT/REG125/1, WT/REG38/1, WT/REG124/1).

<sup>116</sup> For example, EC–South Africa FTA, Canada–Costa Rica FTA, and the Japan–Singapore New Age Economic Partnership (NAEP).

<sup>117</sup> Agreement between New Zealand and Singapore on a Closer Economic Partnership (CEP) (WT/REG127/1).

<sup>118</sup> On balance, the threshold levels greater than 20–25%, which are applied to South Africa and Morocco/Tunisia under their respective FTAs with the EC, could be justifiable for ACP States under EPAs given that the level of economic development of ACP States is generally lower than South Africa or Morocco/Tunisia.

<sup>119</sup> For example, the application of global safeguards to intra-RTA trade is allowed under Canada–Chile FTA, Chile–Mexico FTA and Mexico–Israel FTA only where the partner’s imports constitute a ‘substantive share of total imports’ and contribute ‘importantly’ to serious injury of domestic industry. Under the former FTA, ‘substantive share’ is understood to be among the top five suppliers measured by import share, with or without the additional requirement that the partner’s share be at least 15% of total market share. ‘Importantly’ is understood to be no ‘appreciably’ slower growth rate than total import growth rates during the period where domestic injury takes place (WT/REG125/1, WT/REG124/1).

developed country RTA members to raise *de minimis* threshold levels for the application of safeguards in terms of market share of imports, below which no safeguard measures should be applied for partners' imports above the levels stipulated under Article 9.1 of ASG (3%) to a certain higher level (e.g. 5%).<sup>120</sup>

(2) *Anti-dumping and countervailing measures*

134. The consideration of other trade remedies, namely anti-dumping and countervailing measures under RTAs, have been less problematic than safeguard measures in terms of their compatibility with the MFN obligations under GATT 1994 as they are origin-specific, and thus inherently 'discriminatory' in nature. Indeed, most RTAs do not provide any preferential treatment to RTA partners for those trade remedies by simply confirming the rights and obligations under the Agreement on Implementation of Article VI of GATT 1994 on anti-dumping (AAD) and the Agreement on Subsidies and Countervailing Measures (ASCM).<sup>121</sup> In addition, some North-South RTAs restate procedural SDT for developing countries in terms of providing 'possibilities for constructive remedies' prior to the imposition of anti-dumping measures pursuant to Article 15 of AAD.<sup>122</sup>

135. Nonetheless, a limited number of RTAs provide for according preferential treatment to parties to the RTA in the application of anti-dumping and/or countervailing measures. One such treatment, stipulated under the Canada-Chile FTA, is to exempt RTA partners reciprocally from the application of anti-dumping measures.<sup>123</sup> Another is to increase the *de minimis* threshold levels for exemption from the imposition of anti-dumping and countervailing duties in terms of the minimum market share of dumped imports from each source in the total imports and of the dumping/subsidy margin. The *de minimis* level is currently fixed at 3% for anti-dumping and 4% for subsidies and countervailing measures for minimum import share, and 2% for dumping/subsidy margins (AAD 5.8 and ASCM 27.10). The New Zealand-Singapore Closer Economic Partnership, for instance, increased with regard to intra-RTA trade the *de minimis* levels for RTA partners from 2% to 5% in respect of dumping margin, and from 3% to 5% in respect of import volume.<sup>124</sup>

136. The possible elements of greater flexibility for developing countries under North-South RTAs could include either (1) an obligation, possibly asymmetric as SDT, for developed countries to exclude developing country RTA partners from the application of anti-dumping and countervailing measures, or (2) the application of higher *de minimis* levels for intra-RTA trade in terms of import share and dumping/subsidy margin.

137. As with safeguard measures, however, the WTO conformity with the MFN obligation of such preferential treatment of RTA partners in the application of contingency measures is questionable. The AAD and ASCM are unclear with regard to the measures that preferentially exclude RTA partners from the application of trade remedies, or that preferentially raise *de minimis* levels for RTA partners. They are most likely to constitute an infringement of the MFN obligation.<sup>125</sup> The ways in

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<sup>120</sup> Possibly, this raises an issue of compatibility with MFN principle if the *de minimis* level is raised only for RTA partners. See the discussion below on anti-dumping and countervailing measures.

<sup>121</sup> Among such RTAs are the EC-Morocco and EC-Tunisia Euro-Mediterranean Agreements, EC-Mexico FTA, EFTA-Mexico FTA, Mexico-Israel FTA, and Canada-Costa Rica FTA.

<sup>122</sup> EC-South Africa FTA.

<sup>123</sup> [www.dfait-maeci.gc.ca/tna-nac/cda-chile/menu.asp](http://www.dfait-maeci.gc.ca/tna-nac/cda-chile/menu.asp).

<sup>124</sup> WT/REG127/1.

<sup>125</sup> A complaint may be raised by a third party in the case of an RTA where the *de minimis* level is set at 5% for minimum import share on a preferential basis, if the third country is subject to anti-dumping duties while its import share of the 'dumped' product in the import country is between 2% and 5% – i.e. above WTO-sanctioned *de minimis* level but below RTA-specific *de minimis* level – and if an RTA partner country, whose import share of dumped product is similarly between 2% and 5%, is excluded from the application of anti-dumping duty under RTA-specific *de minimis* provision. This may be considered a violation of the MFN principle. For this to be legal under WTO rules, GATT

which the *de minimis* obligation is articulated in the relevant WTO provisions suggests that WTO Members are free to adopt higher threshold levels than those defined in the respective WTO agreements to the extent that the resulting higher *de minimis* level is applied on an MFN basis. The MFN general obligation applies broadly not only to tariff treatment but also ‘with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation’ (GATT Article I:1). Therefore, unless it is established that GATT Article XXIV provides a comprehensive exception to the MFN principle with respect to non-tariff measures, as well as tariff treatment, it is likely that such preferential measures as may be introduced in an RTA could not be justified under GATT 1994. For this to be the case, it will be necessary to relax the ‘necessity test’ requirement by complementing it with economic balancing tests. This would allow for non-tariff measures not necessarily required to be eliminated under GATT Article XXIV:8 (and thus not included in ORRC) to qualify for justification to the extent that they are trade promoting internally and less trade disturbing externally.

### (3) Standards

138. Other possible components of ORRC that have become increasingly prominent in recent years, are technical, sanitary and phytosanitary standards and regulations that may act as regulatory barriers to trade. The relative incidence of those measures on trade is increasingly important as tariffs are lowered and eliminated at the regional and multilateral levels. Harmonisation, or mutual recognition, which amounts to the elimination of residual non-tariff barriers (NTBs), of these standards would be significantly trade promoting. In practice, several recent ‘third-generation’ RTAs provide for the principle of mutual recognition of conformity assessment and/or equivalence of standards among RTA partners, while others stipulate work programmes aimed at increased regional cooperation for mutual recognition of conformity assessment/equivalence.<sup>126</sup> WTO disciplines are unclear with respect to mutual recognition of standards, particularly those based on RTAs. In order for regional (or any other) initiative for MRAs not to be found illegal under WTO, the clarification of multilateral disciplines may be necessary.

139. The question of the definition of ORRC in the case of SPS/TBT standards is slightly different from that of trade remedies. National SPS/TBT standards may well be considered as constituting part of ORRC, as the fact that GATT XXIV:8 refers to Article XX (general exception) as an exception to the to-be-eliminated ORRC indicates the relevance of at least a certain sub-category of SPS/TBT measures (as Article XX(b) can be presumed to comprise certain elements of SPS measures that are ‘necessary to protect human, animal or plant life or health’), which are authorised to persist under an RTA.<sup>127</sup> On the other hand, since the supposition that all other SPS/TBT measures fall within the scope of ORRC would lead to an absurd situation in which all those measures should be eliminated upon the formation of an RTA, SPS/TBT measures could not be presumed to constitute ORRC. A suggested solution to this dilemma has been to interpret the scope of ORRC to include only ‘unnecessary and discriminatory’ SPS/TBT measures such as NTBs to be eliminated from intra-RTA trade, so as not to inhibit inappropriately the formation of RTAs.<sup>128</sup> Such an interpretation would authorise national SPS/TBT measures to persist under RTAs, thus elimination, or the harmonisation and mutual recognition at the regional level of those measures are not required nor necessary under GATT Article XXIV:8.

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Article XXIV needs to be interpreted to constitute an exception to the MFN obligation in relation to the disciplines under AAD.

<sup>126</sup> Principles of mutual recognition are provided under, for example, Japan-Singapore NAEP, New Zealand-Singapore CEP and Chile-Mexico FTA. Increased cooperation to this effect is provided under Euro-Mediterranean Agreements (Morocco, Tunisia), EC–South Africa FTA and EC–Mexico FTA.

<sup>127</sup> Regional standards or MRAs are also relevant to ORCs under GATT Article XXIV:5 that should not be made ‘on the whole’ ‘more restrictive’ upon the formation of an RTA.

<sup>128</sup> However, the prohibition of ‘discriminatory and unnecessary’ measures (‘negative integration’) is already assured multilaterally under general MFN and national treatment obligations under GATT 1994 I.1 and III, and the SPS and TBT Agreements. Thus, this interpretation of prohibition required under Article XXIV:8 of such measures (comprising ORRC) can be seen at least in part redundant with multilateral disciplines. See Trachtman (2002).

140. The mutual recognition of standards gives rise to the issue of consistency with the MFN obligation under GATT 1994. Since mutual recognition agreements (MRAs) are inherently discriminatory against outsiders, they appear to be MFN-compatible only to the extent that they are open to third-country participation based on objective criteria (equivalence of standards/conformity assessment) – ‘open-MRAs’. While the SPS/TBT Agreements are both implicit, the protection against the MFN obligation of ‘open’ MRAs can be drawn from the preference given to them under Article 4.2 of the SPS Agreement and Article 6.3 of the TBT Agreement,<sup>129</sup> as well as similar but more explicit treatment on the ‘recognition’ of qualifications for licensing and certification of service suppliers in GATS Article VII.<sup>130</sup> In this light, the harmonisation of standards, or mutual recognition mandated under an RTA, which is closed to third parties, is likely to constitute a violation of the MFN obligation and would not be defensible under Article 4.2 of the SPS Agreement or Article 6.3 of the TBT Agreement. Therefore, GATT Article XXIV must provide a defence as exceptions to the MFN obligation. In this regard, the interpretation of ORRC discussed above has led to the observation that the elimination, or harmonisation including mutual recognition, of the majority of SPS/TBT standards is not required or necessary under GATT Article XXIV: 8. The *Turkey-Textile* necessity test suggests that the party to the RTA would be required to demonstrate that the measures in question are ‘necessary’ for the formation of the RTA. It follows that GATT Article XXIV:8 does not provide protection from MFN violation of RTA-mandated (closed) MRAs.

## IV.2 TRANSITIONAL PERIOD: GATT ARTICLE XXIV:5(C)

The transitional period is a pertinent issue for North–South RTAs as a longer transitional period has been an element of implicit flexibility under GATT Article XXIV. The ‘Reasonable period of time’ stipulated in Article XXIV:5(c) of GATT, was clarified in the 1994 Understanding (paragraph 3) as exceeding ‘10 years only in exceptional cases’. It has been further clarified that if the period of 10 years is insufficient, the requesting RTA parties shall give ‘a full explanation’ to the Council for Trade in Goods. Given that developing countries need a longer transitional period on the ground of infant industry protection, enhanced competitiveness of domestic industry and curtailing government revenue loss, elements of SDT relating to the transitional period should focus on two issues. First, the legal nature of the ‘RTAs’ during the transitional period; and, second, the length of the transitional period, including (a) the absolute duration of the transitional period, and (b) the asymmetry in the duration of the period applied by parties to the RTA.

141. The key issue is to secure common understanding among WTO members that the substantive disciplines of GATT Article XXIV on FTAs and customs unions applies to ‘RTAs’ only upon the completion of the transitional period; during the transitional period such RTAs are deemed to be ‘interim arrangements’. The WTO compatibility of certain transitory arrangements that may be introduced in North–South RTAs in favour of developing country parties (e.g. a lower SAT requirement or provision of asymmetrical intra-RTA safeguards) depends critically on whether the relevant GATT XXIV disciplines are waived during transitional period. If such an interpretation is agreed among WTO members, RTAs are theoretically free to adopt any measure deemed appropriate among members during the transitional period, including staged tariff elimination (thus not meeting SAT requirement at a given point in time during transitional period) or intra-RTA safeguard measures.

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<sup>129</sup> SPS: 4.2 stipulates that ‘Members shall, upon request, enter into consultation with the aim of achieving bilateral and multilateral agreements on recognition of equivalence’. TBT:6.3 stipulates that ‘Members are encouraged ... to be willing to enter into negotiations for the conclusion of agreements for the mutual recognition of results of each other’s conformity assessment procedures’.

<sup>130</sup> GATS VII:2 requires Members to ‘afford adequate opportunity for other interested Members to negotiate their accession to such an agreement or arrangement or to negotiate comparable ones with it’.

142. The legal character of ‘RTAs’ during the transitional period and applicable rules (or the timing of the applicability of disciplines of GATT Article XXIV) is indeed one of the systemic issues that have been debated in CRTA. The current practice seems to confirm such an understanding, although there are still different in views among WTO Members. Thus, a clarification would be usefully brought to the issue by agreeing multilaterally upon a common understanding to that effect.

143. Once the legal security of the transitional period is confirmed, the second issue concerns the length of the transitional period. The majority of RTAs provide transitional periods, while some North–South RTAs provide a period longer than 10 years for developing countries, ranging 12 to 17 years in an asymmetric manner (i.e. a shorter transitional period or none at all for developed countries).<sup>131</sup>

144. In terms of WTO-compatibility it appears that only the absolute duration of the transitional period for interim agreements is subject to WTO disciplines under Article XXIV:5(c) of GATT and paragraph 3 of the 1994 Understanding. These rules remain indifferent as to the asymmetric application of the transitional period among parties to an RTA. Thus it may well be the case that to the extent that the absolute transitional period does not exceed 10 years, the asymmetric application of the transitional period among members of RTAs is allowed under existing rules. The application of asymmetry in the transitional period could, if deemed necessary, be explicitly be recognised under new rules through the notion of SDT. The more acute issue, however, is whether and to what extent developing countries are allowed a transitional period longer than 10 years. While the 1994 Understanding stipulates that only in ‘exceptional cases’ could parties to an RTA adopt a transitional period of longer than 10 years, it is yet to be clarified what circumstances would constitute an ‘exceptional case’. Nor is it clear how long the transitional period can be, or what would be regarded as ‘a full explanation’.

145. In this light, a possible reform of WTO disciplines over the transitional period for interim agreements could be geared toward clarifying the notion of ‘exceptional circumstances’, if not revising altogether the fixed criterion of 10 years. The first element to that effect would be to introduce the notion of SDT to enable more favourable treatment for developing countries in meeting the ‘exceptional circumstances’ criterion. The second element in the clarification exercise would be to set explicitly 15–20 years as the maximum permissible duration of the transitional period under ‘exceptional circumstances’. A formal understanding to this effect could serve to balance the relaxation of the ‘exceptional circumstance’ criterion with a ceiling of the maximum period permissible, while providing a sufficiently long transitional period once the ‘exceptional circumstances’ test is cleared.

146. For the purpose of incorporating the notion of SDT, two possible approaches are conceivable. The first would be to create a presumption of ‘exceptional circumstances’ when developing countries are concerned so that the ‘full explanation’ requirement would not apply. This approach reflects and complements the current practice of some RTA members whereby justification is given in the CRTA to the longer-than-10-year transitional period on the ground of the special needs of developing country members.<sup>132</sup> At the same time, such a presumption would not be applicable to developed countries, thus ‘a full explanation’ requirement would apply to them. In this situation, a clarification of the concrete elements of ‘a full explanation’ would be useful in order to render it more difficult for developed countries to apply a longer-than-10-year transitional period (‘reverse flexibility’).

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<sup>131</sup> The Euro-Mediterranean Agreements (Morocco, Tunisia), the EC–South Africa FTA, and the EFTA–Morocco FTAs provide a transitional period of 12 years; the Canada–Chile FTA provides 17 years; and NAFTA, exceptionally, provides a 15-year transitional period for some products for the United States.

<sup>132</sup> As noted previously, the 12-year transitional period under the EC–Tunisia Euro-Mediterranean Agreement was justified on the basis of ‘the sharp difference between the respective level of development’ of parties to the RTA and the need to allow developing country members ‘to deal progressively with the economic and social consequences linked to the process of economic liberalisation and market opening under the FTA’ (WT/REG69/4, *op.cit.*).

147. The second approach would be to define objective fixed statistical criteria in terms of the percentage share of tariff lines or trade volume that could be subject to a transitional period longer than 10 years for the purpose of ‘exceptional cases’. In addition, the fixed criteria would be defined only for developing countries, or in terms of asymmetric criteria for developing and developed countries. This could clarify the extent to which internal liberalisation in an RTA can be subjected to a longer transitional period for developing (and developed) countries in an objective manner, while limiting the scope of exceptions quantitatively. If developed countries are deemed eligible for the ‘exceptional circumstances’, very strict criteria would be necessary.

### **IV.3 LEVEL OF BARRIERS TO THIRD PARTIES: GATT ARTICLE XXIV:5(A) AND (B)**

148. The third issue arising from the formation of North–South RTAs concerns the level of barriers to third countries. Article XXIV:5(a) and (b) of GATT 1994 stipulates that customs duties and ‘other regulations of commerce (ORC)’ should not be made higher or more restrictive against third countries upon the formation of the RTA. The 1994 Understanding clarified that the evaluation of general incidence of the duties and ORC before and after the formation of a customs union under paragraph 5(a) would be based on weighted average tariff rates using applied rates. As future EPAs would be FTAs rather than customs unions, the issue of external duties should not arise; the salient issues thus relate to non-tariff barriers, particularly preferential rules of origin and standards.

#### **IV.3(a) Rules of origin**

149. Preferential rules of origin are key features of FTAs. Similar to the SAT requirement under GATT Article XXIV:8, definitional issues regarding the scope of ORC is at the centre of debate relating to preferential rules of origin in the context of GATT Article XXIV:5. The Panel in the *Turkey-Textile* case only clarified that ORC, as an ‘evolving concept’, could include ‘any regulation having an impact on trade’.<sup>133</sup> Multilateral disciplines are weak if not irrelevant in this area and the relationship between preferential rules of origin and Article XXIV of GATT is left unanswered. The Agreement on Rules of Origin resulting from the Uruguay Round only concerns non-preferential rules of origin for commercial policy on an MFN basis, while the Common Declaration with Regard to Preferential Rules of Origin attached to that Agreement only ensures the transparent application of those rules.

150. There has been no agreement among WTO Members as to whether preferential rules of origin should be seen as falling within the scope of ORC. On the one hand, it has been argued that the preferential rules of origin instituted upon the formation of an FTA could be considered as new trade barriers to third countries that export intermediate products utilised in the production of final products processed within the FTA. This interpretation implies that preferential rules of origin constitute ORC. Another case for the inclusion of preferential rules of origin in ORC relates to the asymmetry in the degree of disciplines of Article XXIV of GATT between customs unions and FTAs with regard to the external requirement not to raise barriers to third countries. It has been observed that, on balance, the disciplines are more ‘stringent’ for customs unions than for FTAs. While customs unions are to abide by the requirement not to raise barriers to third countries upon their formation, there is no comparable discipline on preferential rules of origin, a feature of free trade areas, although preferential rules of origin, by promoting the use of intermediate goods produced within an RTA, may well constitute additional barriers to third countries.<sup>134</sup> On the other hand, arguments have been advanced for the exclusion of preferential rules of origin from the scope of ORC. It has been argued that while Article

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<sup>133</sup> *Turkey-Textile* Panel report, *op. cit.*, paragraph. 9.120.

<sup>134</sup> With a view to preventing trade diversion from taking place upon the formation of an FTA, it has been suggested that the GATT/WTO rules be modified in such a way as to require that there be no rules of origin on a product in a member country with the lowest tariff in the RTA on that product. See Panagaria (1999).

XXIV:5 of GATT requires the general incidence of ORC not to be made more ‘restrictive’ than before upon the formation of an FTA, the *ex ante* and *ex post facto* comparison of ‘restrictiveness’ is irrelevant in the case of preferential rules of origin, as parties to an RTA would not have utilised preferential rules of origin for the purpose of the FTA in question before its formation.<sup>135</sup>

151. From the perspective of developing countries party to an FTA, an important issue relating to greater flexibility in terms of the rules of origin regime is to ensure reasonably liberal preferential rules (and relevant to their production capacities) through, *inter alia*, less stringent rules on the change in tariff lines, local content or substantial transformation requirements. As to the local content requirement, the higher the local content requirement, the more difficult it is for an RTA member to benefit from preferential market access under the RTA. While origin regimes differ significantly among preferential schemes, existing RTAs have adopted on average a threshold of domestic content of between 40–60%.<sup>136</sup> Relatively liberal regimes include the one provided under Canada–Chile FTA and COMESA where local content requirements are 23–35% and 35%, respectively. Where product-specific rules are to be negotiated, products of export interest to developing countries would need to be provided with less stringent requirements. The use of cumulation provisions could also be provided for developing countries under preferential rules of origin.

152. The possible elements of reform for SDT in WTO rules could involve provisions that those preferential rules of origin negotiated and agreed upon by developing countries cannot be subjected later to challenges by third countries on the grounds of increased (more restrictive) ORC. This may possibly be achieved through an agreement that preferential rules of origin do not fall within the definition of ORC. Conversely, in order to promote more liberal origin regimes, preferential rules of origin could be included in the scope of ORC and thus subjected to review under the CRTA to ensure that such rules are reasonably liberal without protectionist effects on third parties. This issue requires further investigation.

#### **IV.3(b) Standards**

153. Mutual recognition arrangements under RTAs for SPS/TBT standards in the context of the SAT requirement could also be seen as forming part of ORC. The way in which mutual recognition under an RTA of SPS/TBT-related standards affects exports of third parties resembles that of preferential rules of origin. As the third country importing ‘like products’ is excluded from the RTA-based mutual recognition regime, the resulting effect for outsiders is a relative increase in barriers to their exports. Such characteristics of RTA-based MRAs regime gives rise to conflicts between the purposes of GATT Article XXIV:5 and 8. Harmonised TBT/SPS standards may facilitate intra-RTA trade but have the effect of raising barriers against third parties. Whether or not such discriminatory effects of regional MRAs violate GATT 1994 will depend, first, on the definition of ORC under Article XXIV:5(b) of GATT and, second, on the availability of Article XXIV of GATT as an exception to GATT 1994 disciplines including SPS/TBT, which in turn depends on the definition of ORC under Article XXIV:8 of GATT. The ORC is important as it determines the degree of ‘necessity’ of the measures at issue. This should be supplemented by the ‘economic test’ which should define the scope of ‘necessity’ on the basis of economic benefits internally and detrimental effects externally, thereby balancing the dual purposes of Article XXIV:5 and 8 of GATT. It may be necessary that Article XXIV:5 of GATT is available as an exception to GATT 1994 disciplines so that regional MRAs are not unduly subject to legal challenge.

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<sup>135</sup> Hudec and Southwickes (1999).

<sup>136</sup> WTO (2002b).

#### IV.4 PROCEDURAL REQUIREMENTS: GATT ARTICLE XXIV:6 AND 7; AND THE 1994 UNDERSTANDING, PARAGRAPH 12

154. Article XXIV of GATT 1994 and the 1994 Understanding stipulate a series of procedural requirements for RTAs that have been gradually clarified and improved by the CRTA. These include the notification and examination requirements (Article XXIV:7) and the requirement for compensation to third parties in the case of withdrawal of concessions upon the formation of a customs union (Article XXIV:6). The 1994 Understanding paragraph 12 has also clarified that the dispute settlement procedure as stipulated in the Understanding on Rules and Procedures Governing the Settlement of Disputes is applicable to ‘any matters arising from the application of those provisions of Article XXIV’. The notification and examination benchmarks pertain directly to multilateral surveillance of RTAs, which has proved to be deficient in effectively disciplining newly created RTAs and in monitoring the operations of existing RTAs. Thus, improving the notification and examination procedures would also be at the centre of the WTO negotiations on rules on RTAs, as well as other substantive requirements. The elements of SDT enabling greater flexibility for developing countries could be instituted with regard to each of those procedural requirements. Given the importance given to the supervisory function of WTO over RTAs, the procedural SDT needs in-depth analysis. Some possible elements for consideration and further examination are highlighted in the following paragraphs.

155. With regard to the notification and examination requirements of RTAs under the CRTA, procedural SDT may be instituted with, *inter alia*, provisions mandating favourable consideration in the examination and assessment of the WTO-compatibility of notified North–South RTAs, in line with ‘special regard’ of the type comparable to Article 15 of AAD.<sup>137</sup> A facility providing consideration for the special needs of developing countries would complement SDT incorporated into the substantive requirements of GATT Article XXIV. In addition, at the operational administrative level, streamlined, less onerous notification and reporting conditions could provide additional flexibilities for developing countries.

156. Compensation requirements under Article XXIV:6 of GATT relate to customs unions, and thus are less relevant to North–South FTAs, as in future EPAs. The 1994 Understanding clarified that negotiations for the purpose of compensation to third parties upon the formation of a customs union under paragraph 6 was understood to start before tariff concessions are modified and withdrawn. The problems arising from the operation of the provisions pertained to the timing of compensatory negotiations (when to start), and the right of affected third parties to request compensation. SDT in this respect might include allowing developing countries for *ex post facto* negotiations. Also, developing countries might be entitled to raise requests for compensation in the event that they are negatively affected by measures taken by developed countries in the formation of a customs union.

157. The provision on dispute settlement was explicitly included for the first time in the 1994 Understanding. The applicability of the DSU has had significant consequences for the legal standing of RTAs before WTO law and the functions of the CRTA in the examination of RTAs. As noted previously, the *Turkey-Textile* case created the presumption of inconsistency by shifting the burden of proof to the party invoking Article XXIV of GATT as its defence. SDT in this regard, therefore, may include the possibility of reconstituting the presumption for WTO compatibility of RTAs involving developing countries under certain conditions. The issue of presumption for WTO-conformity related institutionally to the distribution of jurisdiction between the Dispute Settlement Body (DSB) and the CRTA.<sup>138</sup> Whether or not the dispute settlement panel has jurisdiction over issues pertaining to

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<sup>137</sup> Article 15 of AAD stipulates SDT for developing countries in the application of anti-dumping measures by stating ‘it is recognised that special regard must be given by developed country members to the special situation of developing country members when considering the application of anti-dumping measures’.

<sup>138</sup> As noted above, the issue relating to the distribution of jurisdiction between the WTO committee and the DSB was raised in the context of balance of payments measures under Article XVII. In the context of implementation issues,

Article XXIV of GATT even while the examination of the RTA in question by the CRTA is ongoing was the question behind the explicit recognition of the applicability of DSU in 1994 Understanding. In this respect, possible elements of SDT might institute a ‘moratorium’ from the application of dispute settlement procedures as long as the examination is ongoing within the CRTA on the RTA in question (similar to Article 64.2 of TRIPS<sup>139</sup>). Other possible elements might include ‘special regard’ to developing countries in the case of a dispute (Article 15 of AAD), or a ‘standard of review’ of the type provided under Article 17.6 of AAD,<sup>140</sup> whereby developing countries could claim for more favourable permissible interpretation on issues arising from Article XXIV of GATT disciplines. These issues need further examination.

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India and others have proposed to clarify Article XVIII of GATT 1994 ‘to the effect that only the Committee on Balance of Payments shall have the authority to examine the overall justification of BOP measures’ (WT/GC/W/354).

<sup>139</sup> Article 64.2 of the TRIPS Agreement stipulates a moratorium on ‘non-violation’ and ‘situation’ complaints under GATT XXIII:1(b) and (c) for a period of 5 years, which was subsequently further extended by Doha Ministerial Conference until the Fifth WTO Ministerial.

<sup>140</sup> ‘Standard of review’ mandates the panel to find the national authority’s measures in the application of anti-dumping measures in conformity with the Agreement ‘if it rests upon one of those permissible interpretations ... where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation’ (AAD:17.6(ii)).

## Chapter V SUMMARY AND CONCLUSIONS

158. The ACP–EU Partnership Agreement signed between the ACP States and EU in Cotonou in June 2000 is one of the most important instruments of development cooperation contracted between the two parties and between any developed and developing countries. It retains and builds upon the *acquis* of the Lomé Conventions. It provides a new framework for economic and trade cooperation whose specific modalities are to be introduced gradually during a preparatory period between March 2000 and December 2007 and which shall, *inter alia*, ensure full conformity with WTO provisions including special and differential treatment for ACP States. The new trade and economic framework consists essentially of four pillars, namely: (i) the temporary non-reciprocal preferential treatment for ACP States basically continuing the trade preferences under the Fourth Lomé Convention; (ii) economic partnership agreements (EPAs) between willing ACP States and the EU; (iii) alternative arrangements for ACP States that choose not to enter into EPAs; and (iv) special treatment for ACP least-developed countries in the form of duty-free and quota-free treatment for their exports.

159. In designing, negotiating and adopting the modalities under the four pillars, the WTO compatibility of the resultant arrangements is a fundamental condition albeit juxtaposed against the SDT requirements for ACP States. The modalities for the LDC pillar have been addressed by the EU's 'Everything but Arms (EBA) market access initiative, as an extension of its GSP scheme. The EBA entered into force in March 2001 for an indefinite (permanent) period for all LDCs. Such special GSP treatment for LDCs is compatible under the WTO with the Enabling Clause paragraphs 2(a) and (d). The modalities for possible alternatives to EPAs, and the attendant WTO compatibility, have yet to be identified, as this pillar is scheduled for consideration in 2004 (although some preliminary analyses suggest a 'super-GSP' scheme). The modalities for the EPA pillar would be defined through consultations and negotiations, which were launched on 27 September 2002. The WTO compatibility aspect of future EPAs, especially with regard to SDT for ACP States needs to be addressed. The pillar pertaining to the temporary continuation of the Lomé type non-reciprocal trade preferences required a WTO waiver under WTO Agreement Article IX, which was requested by the EU in March 2000. Following a long delay, two waivers on Article I and Article XIII of GATT 1994 were granted in November 2001 by the Fourth WTO Ministerial Conference. This act removed the ambiguity over the consistency of the entire new ACP–EU pact with WTO obligations and allows both parties to focus on implementing the Partnership Agreement and negotiating the new trading arrangements. It is particularly important during the preparatory period that the ACP States and their regional groupings make effective use of the non-reciprocal preferences prior to their expiry.

160. The Doha work programme on RTAs and the emphasis on SDT provides a unique opportunity for the ACP Group of States to engage actively in the negotiations to introduce reforms that address their specific, common trade and developmental interests in forming EPAs with the EU. At the same time, the ACP Group's negotiating strategy has to incorporate the wider universal, systemic case for clarity and improvements in the WTO rules on RTAs as supported by other WTO members. The rationale for this is twofold; first, as a negotiating strategy and, second, as part of the effort to develop effective and equitable rules to ensure that RTAs contribute to strengthening the multilateral trading system and that they do not have trade diversion effects.

161. In recognition of such opportunities and challenges, the ACP Trade Ministers mandated an examination of the options for reforming the WTO rules on RTAs to provide adequate flexibility to enable ACP States to advance their interests in forming WTO-compatible arrangements with the EU. Hence, the ACP States and the EU need to work within the Doha agenda on RTAs to introduce SDT and flexibility needed by ACP States and incorporated within EPAs. Such an approach would also be justified by the recognition given to 'developmental aspects of regional trade agreements' in the Doha Ministerial Declaration. Given the sensitivity of the matter, the ACP States and the EU have agreed to 'closely cooperate and collaborate in the WTO with a view to defending the arrangements reached, in particular with regard to the degree of flexibility available'.

162. Against this background, this report aims to contribute to the preparations by ACP States for the negotiations with the EU of new WTO-compatible EPA(s), with flexibility and special and differential treatment for ACP States, taking advantage of the Doha work programme on WTO rules applying to regional trade agreements. It is argued that for future EPAs to be legally valid under the WTO, it is imperative that special and differential treatment be made available to developing countries that enter into reciprocal trade agreements with developed countries in respect of the relevant WTO rules, namely GATT 1994 Article XXIV.

163. In North–South RTAs such as EPAs, developing countries would most certainly need greater policy flexibility to adjust their economies in order to benefit from the intense competition arising from freer regional trade. This is particularly the case where the level of development of the participating countries is significantly lower and more vulnerable in relative and absolute terms, as is the case with ACP States in EPAs *vis-à-vis* the EU. Due to their long-standing reliance on non-reciprocal preferences for their exports and their dependence on tariff revenues as a major source of government revenue, the case for SDT and flexibility under EPAs is thus compelling. Indeed, the extent of asymmetry in the level of development between ACP States and the EU, as well as the absolute level of development of ACP States, make EPAs distinct from any other existing North–South RTAs. This fact raises legitimate concerns as to the economic viability of future EPAs under existing WTO rules that require reciprocity in exchange for concessions among parties to an RTA. The issue of WTO conformity is particularly acute for EPAs to be formed between an ACP regional grouping and the EU (namely regional economic partnership agreements), as the ACP regional grouping being notified under the Enabling Clause conditions is likely to be ‘GATT XXIV-minus’ by definition, which would render the ACP regional grouping contestable when it forms an EPA with the EU under the terms of Article XXIV of GATT 1994. Therefore, there exists both an economic and a legal rationale for ACP States to seek to reform the WTO rules so that EPAs with SDT and flexibility for ACP States could be deemed to be WTO compatible.

164. In this respect, the major deficiency of WTO rules as applied to North–South RTAs is the absence of SDT for developing countries. Although the concept of SDT is a recognised principle of the WTO Agreements, and even forms a key theme of the Doha work programme, the currently prevailing WTO rules on RTAs against which the compatibility of future EPAs would be judged lack explicit SDT provisions. This constitutes a legal lacuna and inconsistency in existing WTO disciplines.

165. Future EPAs, being mixed North–South RTAs, would have to be notified under Article XXIV of GATT 1994, which has provided the benchmarks for examining and approving RTAs involving developed countries since 1947. However, this Article has no provisions that can be labelled as explicit SDT. While Part IV of GATT 1994 has provided a set of SDT provisions for developing countries since 1964, a dispute settlement case has established that Part IV of GATT 1994 is not applicable in conjunction with Article XXIV of GATT 1994. This undermines a possible claim that in a North–South RTA, the reciprocity requirement of Article XXIV of GATT 1994 can be waived for developing countries on the basis of the non-reciprocity exhortation of Part IV of GATT. The Enabling Clause has provided since 1979 a flexible framework of rules for developing countries in forming regional integration agreements among themselves. However, its current provisions do not cover those RTAs formed between developed and developing countries, as would be the case of future EPAs. Therefore, the result is that no SDT is applicable to developing countries forming North–South RTAs in conforming to requirements as provided under GATT Article XXIV.

166. The lack of SDT within GATT 1994 Article XXIV is most evident if a comparison is made with its counterpart article in trade in services, namely GATS Article V. GATS Article V:3(a) clearly provides and locks in flexibility for developing countries in meeting conditions set in GATS Article V:1 regarding substantial sectoral coverage, absence or elimination of discriminatory measures in accordance with their level of development. Furthermore, GATS Article V:3(b) recognises a distinction between North–South RTAs and RTAs involving only developing countries i.e. South–

South RTAs. In this light, a similar distinction should be relevant in the case of trade in goods. This inconsistency in the availability of SDT between goods and services highlights the need for SDT in the context of North–South RTAs.

167. Although some flexibility is inherent in current provisions of GATT Article XXIV resulting from the current permissive practice in WTO in the application of this article, such ‘*de facto*’ existing flexibility is inadequate in providing sound legal basis and security for the flexibilities that would be deemed necessary for ACP States under EPAs. First, such inherent *de facto* flexibility might still proved to be insufficient to provide sufficient legal cover for ACP flexibility under EPAs. Since such *de facto* flexibility does not differentiate between the flexibility available to developed countries and to developing countries, there persists a risk that the needs of developing countries for enlarging the scope of flexibility is curtailed by the systemic need for more stringent and effective disciplines (thus less flexibility) for all WTO Members. Second, such implicit flexibility is not appropriate in effectively providing legal security for, and to pre-empt future legal challenge against, EPAs.

168. Without explicit SDT provisions applicable to developing countries, and the existing *de facto* flexibility deemed insufficient in scope and inadequate in nature, it has become increasingly evident that GATT Article XXIV has in some sense become irrelevant in effectively addressing the development concerns of evolving North–South RTAs; hence the case for reforming the relevant WTO rules to incorporate SDT applicable to North–South RTAs, most notably GATT Article XXIV. Since SDT is the modality to provide greater flexibility only to developing countries, it also responds to the systemic need for improved and clarified disciplines on RTAs.

169. In order to introduce SDT into WTO rules to cover mixed RTAs with SDT for developing countries, three options are conceivable, namely, through (i) reforming Article XXIV of GATT 1994, (ii) reforming Part IV of GATT 1994 and (iii) reforming the Enabling Clause. These are the WTO provisions relevant to RTAs and the SDT principle. In considering the three options, there is a strong case for reforming specifically Article XXIV of GATT 1994. The option of reforming Article XXIV of GATT is a sound, more legally viable and politically sustainable approach to cater for EPAs with flexibility for ACP States. The elements of flexibility through SDT pertain to those key benchmark requirements under Article XXIV of GATT 1994, namely, the ‘substantially all the trade’ requirement, the transitional period, and the ‘not-on-the-whole-higher-or-more-restrictive’ requirement. The option of reforming Article XXIV of GATT has an added advantage.

170. Three options are conceivable in introducing flexibility as a form of SDT within Article XXIV of GATT 1994. These are (i) generic provisions on SDT within Article XXIV of GATT in favour of developing countries; (ii) review of specific provisions in Article XXIV of GATT; and (iii) revision of GATT Article XXIV:10 on derogation from the substantive requirements therein. Option (i) could consist in inserting a generic paragraph into Article XXIV of GATT 1994 or the 1994 Understanding stating that the flexibility is to be provided for developing countries in terms of the key requirements stipulated in Articles XXIV:5 and 8 (drawing some guidance from Article V:3(a) of GATS). The flexibility would in particular be applied to seek product and trade coverage and longer and more secure transitional periods. Option (ii) is in principle an alternative, but eventually complementary to option (i), depending on negotiations; it consists in revising and modifying specific provisions on the key requirements of Article XXIV of GATT, particularly Articles XXIV:5(c) and 8(a)(i) and (b), so as to allow differentiation for developing countries. The distinction between the two approaches would depend on the actual negotiations. The aim of these changes is to allow flexible interpretation of the key requirements of Article XXIV of GATT 1994 for developing countries in the form of SDT, on the basis of which operationally ‘greater flexibility’ is defined specifically to developing countries. Option (iii) is a supplement to the two options and consists in rendering it easier for developing countries to seek derogation from the substantive requirements of GATT Articles 5–8.

171. Amending Part IV of GATT 1994 to be applicable to North–South RTAs is another option to render SDT applicable to GATT Article XXIV. The reform would be geared towards rendering the non-reciprocity principle in multilateral trade negotiations (as provided in GATT Article XXXVI:8)

applicable to negotiations in the regional context, such as the EPAs by ACP–EU. A key difficulty with this option lies in the fundamental irrelevance – as found in a GATT dispute panel ruling – of the non-reciprocity principle in multilateral trade negotiations to conditions set out in GATT Article XXIV. First, SDT in GATT Article XXXVI:8 by definition applies only to multilateral trade negotiations, and is thus irrelevant to regional trade negotiations. Second, GATT Article XXIV concerns conditions that individual RTAs have to meet, and not regional trade negotiations. This option thus cannot be considered as a realistic and workable basis for negotiations on the reform of WTO rules.

172. The option of reforming the Enabling Clause would involve extending the scope of the clause beyond South–South RTAs to encompass North–South RTAs like EPAs. This would ensure that the maximum flexibility enjoyed by developing countries under this clause in the formation of RTAs among themselves would also apply to RTAs they formed with developed countries. It would in effect exclude the future EPAs from the purview of Article XXIV of GATT 1994 and its tougher terms (compared with the Enabling Clause). A serious shortfall with this option, however, is that the legal validity of the Enabling Clause and its coverage of agreements formed among developing countries is increasingly being challenged by some WTO Members. In the light of these attacks, there is the danger that opening negotiations on the reform of the Enabling Clause may lead to a weakening of the clause and an erosion of its flexibility. On the other hand, the Enabling Clause, without having any formal link to GATT Article XXIV conditions, could not guarantee reciprocity in exchange of concessions among the parties to an RTA, and thus may cover a non-generalised non-reciprocal preferential scheme as an ‘RTA’, thereby circumventing the waiver requirements for such preferential schemes. This has systemic risk to the validity of unilateral preferences such as GSP as well, since the Enabling Clause condition that unilateral preference is only allowed under GSP scheme could also be circumvented. This is not in the general interest of developing countries as they need to retain the current legal validity of the Enabling Clause for covering unilateral preferences under the GSP and for maintaining the SDT provided to RTAs formed among developing countries.

173. Given the superiority of direct reform of GATT Article XXIV for the purpose of rendering SDT applicable to developing countries in the context of North–South RTAs, there would be a further need, depending partly on negotiations, for operationalising the concept of ‘flexibility’ to be made available to developing countries in respect of substantive and procedural requirements of GATT Article XXVI. This amounts to the option (ii) as regards direct reform of GATT Article XXIV. Since the degree of flexibility to be made available specifically to developing countries through SDT would depend critically on the definition of generally applicable existing flexibility as well as concrete terms of ‘flexibility’ for developing countries, both elements of flexibilities may require operational definition and interpretation. The most relevant requirements for developing countries include the ‘substantially all the trade’ requirement for internal trade liberalisation and the transitional period. In respect of the ‘substantially all the trade requirement’, possible modalities include the application of different methodologies between developed and developing countries (including the level of aggregation, subject of measurement, sectoral composition and treatment of non-zero preferential duties) and statistical threshold levels. This would ensure lesser degree of market opening for developing countries in meeting the ‘substantially all the trade’ criterion.

174. ‘Other restrictive regulations of commerce’ would need to be interpreted so that the preferential application of trade remedy measures by developing countries on intra-RTA trade would not be unduly impeded. The issue of the transitional period pertains both to its legal standing and its duration, including asymmetry. As RTAs are deemed to be interim arrangements during the transitional period, securing legal protection from the requirements of GATT Article XXIV would leave significant flexibility for developing countries during that period. A transitional period of longer than 10 years could be secured by loosening the conditions for developing countries to meet the ‘exceptional cases’ test, and possibly by defining a maximum duration of transitional periods longer than 10 years.

175. This report points to some priority negotiating issues for ACP States in the multilateral negotiations on the WTO rules on RTAs under the Doha work programme:

1. The starting point for any negotiations would be to retain the legal validity of the Enabling Clause for those RTAs formed among ACP States and developing countries generally. The coverage of South–South RTAs under the Enabling Clause is to be considered *acqui* and not be subjected to negotiation.
2. Securing agreement among WTO Members on the incorporation of the principle/elements of SDT into GATT Article XXIV, possibly in the form of a generic paragraph, may well constitute a negotiating issue independent of other specific systemic issues. This would ensure special treatment for developing countries in meeting the requirements of GATT Article XXIV relative to generally applicable disciplines. For this purpose, a paragraph similar to GATS Article V:3(a) may prove to be useful.
3. The systemic debate on key substantive and procedural requirements on which the actual negotiations would be centred, would need to be geared towards ensuring the most favourable interpretation of and operational understanding on the generally applicable flexibility. Thus, in case there is a need to define concrete terms of additional degrees of flexibility for developing countries, a sufficient degree could be made available to them in terms of key requirements. Such an exercise may be necessary, since the generally applicable flexibility would form the basis on which to build, as SDT, additional degrees of flexibility for developing countries. This is a way to maximise the degree of flexibility available for ACP States and developing countries in the application of GATT Article XXIV disciplines.

176. Given the sequence of negotiations at the WTO and ACP–EU levels, it is important that ACP States and the EU elaborate their negotiating objectives on the new trading arrangements back-to-back with their participation in multilateral trade negotiations so that the objectives of WTO-compatible arrangements with flexibility for ACP States can be promoted in a coherent and mutually supportive manner. The preparation of a negotiating mandate for the ACP States in respect of EPAs will require intensive and extensive negotiations within and among the different ACP regions prior to the official start of negotiations in September 2002, and during the five years of actual negotiations. With regard to the new multilateral trade negotiations, newly adjusted multilateral rules on RTAs will have to be concluded no later than 1 January 2005, as provided in the Doha Ministerial Declaration. The ACP States (and the EU) will then be in a position to gauge the WTO compatibility of the specific terms of EPAs with the WTO rules prevailing at that time.

177. Preparations by ACP States for those negotiations will require the identification of national, subregional/regional and ultimately ACP-wide priorities and strategies, taking into account their different levels of development and safeguarding and strengthening their subregional and regional integration processes. In the context of parallel negotiations at the multilateral level (WTO), subregional and regional levels (within ACP regions) and interregional levels (ACP–EU, and others), ACP States will also need to elaborate their negotiating objectives and strategies taking into account all trade negotiations in a mutually supportive manner in order to enhance the contribution of trade liberalisation to their development process. Hence, there is a need for ACP States to analyse and consider various options at the national, subregional/regional and ACP–wide levels in preparation for the EPA negotiations with the EU, as well as with the WTO membership.

178. In conclusion, this report has provided a preliminary analysis of the options for reforming the existing WTO rules on RTAs to include explicit SDT and flexibility for developing countries in order to provide the necessary legal coverage for future EPAs with greater flexibility for ACP States. It is argued that there is substantial economic justification and legal basis for incorporating SDT and greater flexibility for developing countries in the WTO rules relating to RTAs formed between developed and developing countries. There is a legitimate and imperative case for reforming the WTO rules on RTAs to redress imbalances in the multilateral system of rights and obligations as regards the provision of SDT for developing countries under mixed RTAs. Finally, the report is intended as a contribution to the ongoing discussions among ACP States on SDT and flexibility for their economies

to undertake the necessary adjustment for moving from non-reciprocal to reciprocal trade relations with the EU.

## ANNEX 1: SUMMARY OF POSITIONS AND PROPOSALS ON REGIONAL TRADE AGREEMENTS

Sponsor Doc. No./Date <sup>1</sup>	Proposal/General issue	Systemic Issues	Procedural issues (examination of RTAs)
<b>Japan (1)</b> WT/GC/W/145 (08/02/1999)	Examine regionalism strictly to ensure the supremacy of the MTS.	Clarify the interpretation of the WTO rules including GATT XXIV; Strengthen the current rules to cope with situations unforeseen at the time of the formulation of Article XXIV of the GATT.	Review the procedures for examining RTAs to secure their consistency with WTO rules.
<b>Korea</b> WT/GC/W/171 (16/04/1999)	Review the WTO rules on RTAs to clarify and strengthen them as necessary	Develop yardsticks for, and define the scope of: 'SAT' (GATT XXIV) and 'substantial sectoral coverage' (GATS V); 'ORC' and 'ORRC' (GATT XXIV); 'level of duties and other regulations of commerce' (GATT XXIV) and 'level of barriers' (GATS V). Develop disciplines on preferential ROO; Relationship between GATT XXIV and GATS V. Relationship between WTO provisions on RTAs and other WTO Agreements.	Clarify the notification requirements. Consider strengthening examination of RTAs' operation.
<b>Hong Kong, China</b> WT/GC/W/174 (30/04/1999)	Clarify and reinforce existing WTO rules and decisions on RTAs .		

<sup>1</sup> Proposals include: (i) submissions to the WTO General Council during the preparatory process (1998-1999) for the Third Ministerial Conference (Seattle) (WT/GC/W series), and (ii) submissions to the Negotiating Group on Rules established under Trade Negotiating Committee according to the Doha work programme (TN/RL/W series).

<p><b>Australia (1)</b> WT/GC/W/183 (19/05/1999)</p>	<p>Agree on new understanding of regionalism and its relationship to the MTS, involving greater precision of rules governing RTAs;</p> <p>Ensure that outcomes of build-in agenda negotiations are not undermined by even greater derogation from MFN obligations as RTAs continue to be established</p>	<p>Decide whether the various WTO rules on RTAs should be integrated into a single framework, including whether 'substantially all the trade' (GATT XXIV) should be measured in terms of goods and services together;</p> <p>Clarify thresholds for meeting basic requirement that RTAs cover SAT (GATT XXIV) or have 'substantial sectoral coverage' (GATS V), including the GATS requirement that 'agreements should not provide for a priori exclusion of any mode of supply';</p> <p>Clarify the scope of 'ORC' and 'ORRC' (GATT XXIV): whether the listing of regulations permitted in RTAs (GATT Article XXIV:8 and GATS Article V:1) is exhaustive or illustrative, and also identify what constitutes 'ORRC' and 'discriminatory measures' (GATS) which should be eliminated.</p> <p>Clarify the extent to which WTO rights and obligations for regulations of commerce can be derogated in RTAs. For example, decide whether: regulations of commerce can be applied differently during the transitional period to full implementation; AD, CVM and safeguards provisions are allowed in RTAs once they have been fully implemented; AD, CVM and safeguards provisions be applied differently for those products which are covered and those excluded by the RTA; whether the above regulations can be applied to RTA members in a more favourable way.</p> <p>Develop disciplines on preferential ROO.</p> <p>Develop ways to measure 'level of duties and other regulations of commerce' (GATT XXIV) and 'level of barriers' (GATS V);</p> <p>Decide whether agreements covered by the Enabling Clause should be subject to the disciplines of GATT Article XXIV;</p> <p>Clarify whether other thresholds for RTAs need to be introduced, e.g. linking the extension of preferences under a proposed RTA to a reduction in trade barriers on an MFN basis.</p>	<p>Clarify the notification requirements, particularly in terms of time-frames.</p> <p>Agree on ways to improve the examination of RTAs, including as rules are clarified: e.g. through the strengthening of notification requirements for trade statistics to be provided to the WTO to justify 'substantially all the trade' (GATT XXIV) or 'substantial sectoral coverage' (GATS V).</p>
<p><b>Hungary</b> WT/GC/W/213 (18/06/1999)</p>	<p>Existing WTO rules concerning RTAs should be further clarified both from substantial and procedural points of view.</p>	<p>The result of the exercise should become part of the rights and obligations of the Members in respect of and applicable to all RTAs concluded after the adoption of these modifications.</p>	<p>RTAs presently under review or notified to the WTO should be considered against the GATT/WTO conformity conditions that prevailed at the time of notification of such agreements. These agreements should be deemed to be virtually consistent with Article XXIV of GATT and Article V of GATS.</p>
<p><b>Japan (2)</b> WT/GC/W/214 (22/06/1999)</p>	<p>Include the work on RTAs in future round negotiations.</p>	<p>Clarify the meaning of the provisions of GATT XXIV and GATSV: 'ORC' (GATT XXIV:5); 'ORRC' (GATT XXIV:8); 'SAT' (GATT XXIV:8); 'Substantial sectoral coverage' (GATS V:1); 'Absence or elimination of substantially all discrimination' (GATS V:1).</p>	<p>Strengthening the examination procedures through:</p> <ul style="list-style-type: none"> <li>- Establishing a review process;</li> <li>- Ensuring the enforcement of the results of the examination;</li> <li>- Establishing the obligation for the notification of EIAs in services.</li> </ul>
<p><b>Turkey (1)</b> WT/GC/W/219 (29/06/1999)</p>		<p>In case of a consensus on systemic issues, such rules should be applied exclusively to those RTAs which are signed after the new rules are adopted</p>	<p>The examination of the RTAs should not be delayed pending on systemic issues and the CRTA examination process should proceed under the existing WTO rules.</p>

<b>Romania</b> WT/GC/W/317 (15/09/1999)	No link should be created between the review and systemic issues.	In case of a consensus achieved on systemic issues, the new rules should be applied exclusively to those RTAs concluded after the entry into force of the agreed new rules.	The RTAs presently under review or notified to the WTO should be considered and processed against WTO rules that prevailed at the time of conclusion of such agreements.
<b>Jamaica</b> WT/GC/W/369 (13/10/1999)	There is a doubt about whether the current GATT XXIV provides sufficient scope for a successful transition.	Examine the relevant provisions of GATT XXIV and GATS V with a view to providing DCs with adequate scope for absorbing the adjustment costs of trade liberalisation and ensuring that these agreements make a sustained contribution to their economic development.	
<b>Australia (2)</b> TN/RL/W/2 (24/04/2002)	Start work on WTO rules on RTAs by (1) procedural issues and (2) systemic issues	Thresholds for meeting the SAT (GATT XXIV) and ‘substantially all sectoral coverage’ (GATS V); Scope of ORRCs (GATT XXIV) and ‘substantially all discrimination’ (GATS V); Ways to measure ‘level of duties and ORC’ (GATT XXIV) and ‘level of barriers’ in GATS V; Extent to which rights and obligations for regulations of commerce can be derogated in RTAs; Other thresholds for RTAs (link preferences to a MFN reduction of barriers); Relationship between WTO rules on RTAs (GATT, GATS and Enabling Clause); Extent to which RTAs under Enabling Clause should be subject to GATT XXIV; Relationship between WTO rules on RTAs and WTO accessions; Extent to which the enlargement of existing RTAs should be regulated; Extent to which provision of overlapping RTAs can coexist; Extent to which compensation should be provided upon the enlargement/formation of RTAs; Extent to which provisions of preferential ROO should be developed.	Notification requirements Legal status of CRTA examination reports; Requirements of periodic reporting;
<b>EC</b> TN/RL/W/14 (09/07/2002)	The scope of the work should encompass all WTO provisions relating to RTAs; WTO framework should serve to encourage ‘deep integration’ and liberalisation.	Clarify the flexibilities already provided for within the existing framework through examination of: - Relationship between GATT XXIV and Enabling Clause; - Extent to which WTO rules already take into account discrepancy in development levels between RTA parties; - Flexibilities available during the transitional period (length, level of final trade coverage, degree of asymmetry) Inputs could be received from CTD and WPSE on development aspects. Definition of key concepts (SAT, ORC, ORRC, ‘applicable duties’ ‘major sector’); Clarification of provisions on staged implementation (‘exceptional circumstances’); Alignment of disciplines between FTA and CU; Treatment of non-tariff measures (ROO); Relationship between Enabling Clause and GATT XXIV; Clarification of key concepts in GATS V; Definition of ‘reasonable time frame’ in GATS V; Appropriate combination of ‘elimination’ (rollback) and prohibition of new discriminatory measures (standstill) in GATS V:1; Methodology to ensure non-raising of barriers to third parties in EIAs;	Timing of notifications, nature and form of information, timing of examination;  Procedures for examination of RTAs notified under Enabling Clause;

<b>Australia (3)</b> TN/RL/W/15 (09/07/2002)	SAT definition	Define 'SAT' in terms of coverage by RTAs of a defined percentage of all the 6-digit tariff lines listed in the HS.	
<b>Chile</b> TN/RL/W/16 (10/07/2002)	Procedural matters		Notification could be made directly to CRTA; Studies of notified RTAs to be carried out by third parties (WTO secretariat or independent experts).
<b>Turkey (2)</b> TN/RL/W/32 (25/11/ 2002)	Priority should be given to procedural aspects	Measure SAT on the basis of 'quantitative approach'; Harmonise preferential ROO with a view in the longer term to a uniform ROO; Harmonise non-preferential ROO by first adopting a single set of ROO among the members of every RTA which would be converged among different RTAs. Focus on rules on regulatory harmonisation; Clarify 'flexibilities' provided within existing provisions in terms of a longer transitional period, level of final trade coverage, degree of asymmetry, as well as flexibility in examination and surveillance process.	Apply 'grandfathering' to existing RTAs based on the determined 'expiry date'. Examine a set of RTAs by (geographical) group; Focus only on trade flows; Redefine information to be provided under standard format; Notification should be made directly to CRTA; Less complex rule is required given increased number of disputes involving RTAs.

**ANNEX 2: POSSIBLE NEGOTIATING OBJECTIVES FOR ACP STATES AND OPTIONS FOR  
GATT 1994 ARTICLE XXIV REFORM THROUGH SDT**

	<b>Possible objective for ACP States in WTO rules negotiations on RTAs</b>	<b>Options for reform through SDT of GATT Article XXIV</b>
<b>SAT requirement (XXIV:8 (a)(i) and (b))</b>		
<b>Duties</b>	Ensure lesser degree of trade/product coverage for developing countries (to allow for exclusion of sensitive sectors on permanent bases) and higher and commercially meaningful product coverage for developed countries (to ensure the most liberal market access opportunities for developing country exports).	<p>Measure SAT requirement in terms of aggregate internal trade volume of an RTA, or;</p> <hr/> <p>Measure SAT requirement at country level based on any combination of (1)-(4):</p> <ol style="list-style-type: none"> <li>1) Apply asymmetric methodology for developing and developed countries (e.g. choice between across the board qualitative and quantitative criteria for developing countries and the combination of the both for developed countries);</li> <li>2) Apply asymmetric requirements for developed and developing countries in terms of sectoral coverage (e.g. no 'exclusion of major sector' for developed countries in terms of certain percentage coverage of tariff lines within each HS chapter level (e.g. 90% within HS-2 digit level) and no such regard, or lower threshold level, for developing countries);</li> <li>3) Apply asymmetric treatment between developing and developed countries of non-zero, less-than-MFN duty rate (e.g. to be taken into account for SAT requirement only for developing countries with certain conditions (e.g. some provision for reduction or harmonisation of tariff schedules under RTA);</li> <li>4) Apply asymmetric statistical threshold for developing and developed countries (e.g. 95% for developed countries and 70% for developing countries);</li> </ol> <hr/> <p>In case of RTAs involving pre-existing sub-regional groupings, measure SAT requirement based on aggregate trade between pre-existing RTAs only;</p>
<b>ORRC</b>	Ensure that the right of developing countries to use trade remedy measures on intra-RTA imports is not unduly restrained and that their intra-RTA exports are not unduly subject to such actions by developed country RTA partners.	Interpret GATT XXIV:8 as providing exception from MFN obligation under GATT I:1 in relation to GATT VI and XIX, AAD, ASG, ASCM and SPS/TBT by loosening the threshold for the 'necessity' test (so that some measures not necessarily required under Article XXIV:8 may more easily be covered by that article depending on, possibly, whether they are trade promoting among members (and that they are unnecessarily trade discouraging against third parties (ORC) ('Economic and balancing tests'))
<i>Safeguards</i>	<u>During the transitional period:</u> Ensure that asymmetric right is granted only to developing countries to apply intra-RTA (thus origin specific) transitional safeguard measures; that developed countries are prohibited to apply such measures.	Already permitted under XXIV? If not: Legal status of transitional period may additionally be strengthened to the effect that no XXIV requirements apply to an RTA during the transitional period (see also 'transitional period' below)

	<p><u>After the transitional period</u>, either of (1) or (2) below:</p> <p>1) In case that an RTA provides for the intra-RTA safeguards on intra-RTA trade and for the exclusion of RTA partners from the application of global safeguards, ensure that more favourable requirements for developing countries (and more stringent requirements for developed countries) in applying intra-RTA safeguards measures in terms of ‘serious injury’ test, combined possibly with asymmetric obligation for developed countries to exclude developing country partners from the application of global safeguards (thus right for developing countries to apply global safeguards to developed countries partners as well); or</p> <p>2) In case that an RTA provides the application of global safeguards only (i.e. no-intra-RTA safeguards is allowed), ensure that asymmetric obligation for developed countries to apply higher <i>de minimis</i> levels for developing country RTA partners;</p>	<p>Interpret ORRC to the effect that:</p> <p>1) SDT is applied to allow for certain asymmetry in rights and obligations between developing and developed countries;</p> <p>2) Trade remedies (SG, AD and CVD) are not included in the scope of ORRC, thus not required to be eliminated on the intra-RTA trade (so as to apply them as emergency measures);</p> <p>3) Flexibility is provided so that intra-RTA application of SG, AD and CVD is ‘permitted but not obliged’ (so as to allow developed countries to exclude developing country partners from the application of global/internal safeguards, AD, and CVD);</p> <p>4) Application of preferentially higher <i>de minimis</i> levels for global safeguards, AD and CVD as well as the exclusion of RTA partners from the application of global safeguards, AD, CVD (by developed countries) to be WTO compatible in relation to MFN obligation (GATT Article I:1) as incorporated in GATT VI, XIX, and ASG, AAD and ASCMs;</p>
<i>AD/CVD</i>	Ensure that developed country member of an RTA is subject to (possibly asymmetric) obligation not to apply AD/CVDs to intra-RTA trade or to apply preferentially higher <i>de minimis</i> threshold levels for RTA-partner developing countries; that developing countries are ensured the right to apply AD/CVDs to intra-RTA trade;	
<i>Standards</i>	Ensure that trade-facilitating regional mutual recognition agreement of SPS/TBT standards (or intensive work programme to that effect) is not unduly hampered by the requirement ORC and ORRC requirements;	Interpret ORRC to include only ‘discriminatory and unnecessary’ SPS/TBT to be included in the scope of ORRC?
<b>Transitional period (XXIV:5(c) and 1994 Understanding para. 3)</b>		
Interim arrangement	Ensure that special transitory measures in favour of developing countries are protected from challenge during the transitional period (in terms of product coverage, safeguard measures etc):	Already permitted under Article XXIV? If not: Agree upon an understanding that during the transitional period RTAs are deemed ‘interim arrangements’ and no requirements for FTAs or CUs need not be met.
	Ensure that transitional period longer than 10 years is entitled for developing countries.	Interpret as SDT broadly ‘exceptional cases’ for DCs either through (1) or (2): 1) By creating presumption for ‘exceptional circumstances’ when DCs are concerned; or; 2) By setting percentage share of number of tariff lines/trade volume that may be subject to the longer-than-10-year transitional period for DCs only (or for DDCs also with significantly lower rates to measure ‘exceptional circumstances’).
	Ensure sufficiently long transitional period for developing countries.	Define explicitly maximum duration of 15-20 years in the case of ‘exceptional circumstances’.
	Ensure that no reverse flexibility (longer-than-10-year transitional period) to be made admissible to developed countries (or under very strict conditions).	Interpret narrowly ‘exceptional circumstances’ and clarify ‘full explanation’ requirement for DDCs (possibly with fixed criteria in terms of the number of tariff lines or trade volume that could be subjected to the longer transitional period as noted above).
	Secure formal recognition of asymmetry in transitional period between parties to an RTA?	Already covered under XXIV: 5(c) and 1994 Understanding.

<b>'Not-on-the-whole-higher-or-more-restrictive' requirement (XXIV:5 (b))</b>		
<b>Rules of origin</b>	Ensure liberal preferential ROO in terms of, <i>inter alia</i> , local content requirements:	Interpret ORC to include preferential ROO and subject to review under CRTA to ensure liberal regime?
	Ensure that RTA is not subject to challenges from third countries on the ground of preferential ROO:	Interpret ORC not to include ROO?
<b>Standards</b>	Ensure that trade-promoting mutual recognition of SPS/TBT standards among RTA partners is not deemed to constitute increased external barrier.	Interpret ORC to include only 'protectionist' SBS/TBT? Interpret XXIV:5 to provide exception to SPS/TBT in accordance with 'necessity test'?
<b>Procedural requirements (XXIV:6 and 7, and 1994 Understanding para.12)</b>		
<b>Compensation requirements (XXIV: 6)</b>	Ensure that developing country RTA member is not subject to excessive compensation requirement?	Only <i>ex post</i> compensation negotiable (in case of customs union) required for DCs? DCs to be entitled for requesting compensation negotiations (XXIV: 6)?
<b>Notification and examination (XXIV:7)</b>	Ensure that notification and reporting requirements does not incur undue administrative burden to developing countries and that CRTA examination process duly take into development concern.	'Sympathetic consideration' to be given to developing countries; Streamlined notification and reporting requirements for North-South RTAs.
<b>Dispute settlement (1994 Understanding 12)</b>	Ensure that developing countries measures taken in pursuance to an RTA are not unduly subject to dispute settlement.	Presumption of GATT-conformity' for mixed-RTAs under certain conditions (as a form of 'special regard' for developing countries)? 'Moratorium' from DSU proceedings while examination in the CRTA is ongoing? A 'standard of review' to be applied so that DSB does not override decision of CRTA?

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