무역상무연구
제68권
2015. 12, pp. 171~195.

논문접수일 2015. 11. 30.
심사완료일 2015. 12. 18.
게재확정일 2015. 12. 19.

Regional Trade Agreements : Exceptions to the MFN Principle in the GATT/WTO System*

In-Sop PAK**

Keywords : GATT, WTO, Multilateral Trading System, MFN, RTA

I. Introduction

The Most Favored Nation (MFN) principle, stipulated in Article Ⅰ of GATT 1994,[1] ensures that concessions and other privileges provided between World Trade

* This research was supported by Kyungpook National University Research Fund, 2012.

** Professor of International Trade, School of Economics and Trade, Kyungpook National University, E-Mail : ipak@knu.ac.kr

1) The General Agreement on Tariffs and Trade (GATT) 1994 includes the original agreement in the year of 1947, GATT 1947, the agreement that created the World Trade Organization (WTO), and many side agreements on specific trade issues as a result of Uruguay Round Multilateral Trade Negotiations that had begun in 1986. While the GATT 1947 only covered trade in goods, a General Agreement on Trade in Services (GATS) was added in 1994.

Organization (WTO) members are granted unconditionally on a non-discriminatory basis. The intent of this is to promote competition and minimize cost of production, based on the theory of competitive advantage. Since the inception of General Agreement on Tariffs and Trade (GATT) 1947 in the year of 1948, exceptions for the derogation to this rule have been allowed, notably in the form of Regional Trade Agreements (RTAs).

RTAs have become a key factor in the changing environment of the world trading system. According to the WTO data, 413 RTAs exist of which 240 are currently in force (See Table 1 and Figure 1),[2] and trade among RTA parties makes up more than 50 percent of global trade.[3]

<Table 1> Figures on all RTAs in force, sorted by Coverage

GATT Article XXIV (FTAs and CUs)	240
Enabling Clause	39
GATS Article V	134
Grand total	413

Source: WTO, 2015.

The issue of whether the recent wave of regionalism[4], represented by the large increase in RTAs since the late 1980's, undermines the multilateral trading system and whether regionalism and multilateralism can coexist effectively has been a topic of vigorous debate.[5] Putting this aside, RTA's aid in both reducing and eliminating tariffs and non tariff trade barriers between constituent parties and this has been considered an

2) World Trade Organization, *Regional Trade Agreements and Preferential Agreements*, available at http://www.wto.org/english/tratop_e/region_e/rta_pta_e.htm
(last visited Nov. 28, 2015). WTO statistics on RTAs are based on notification requirements rather than on physical number of RTAs.

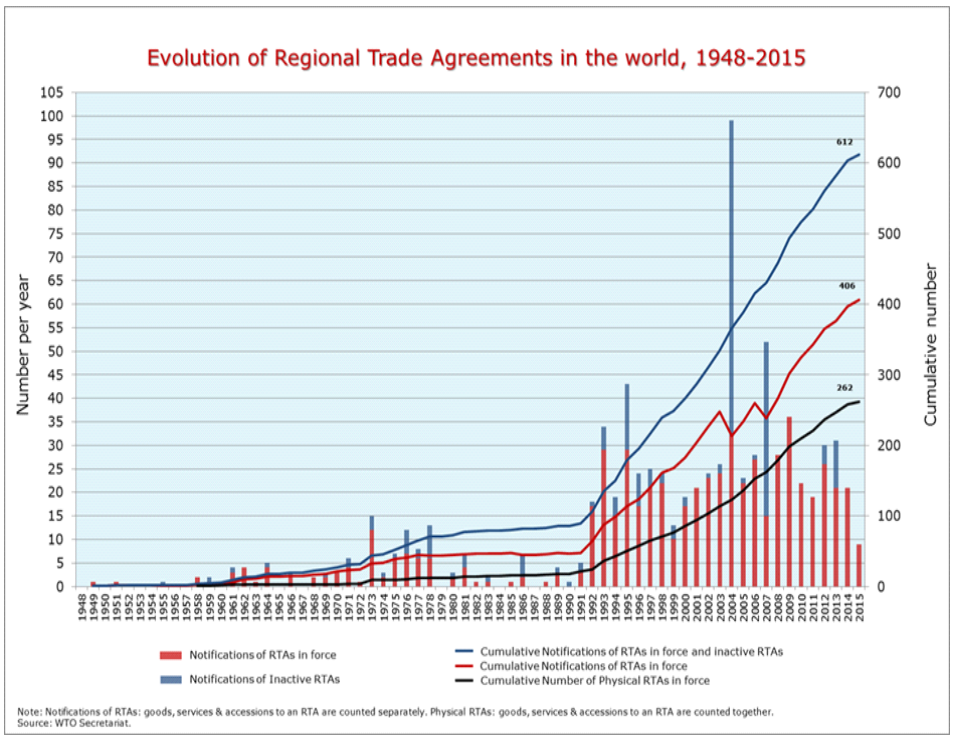
3) WTO, "Synopsis of 'Systemic Issues' Related to Regional Trade Agreements", WTO Secretariat, WT/REG/W/37, March 2, 2000, p. 4.
The most ambitious RTA deal, since the negotiations beginning in 2008, was finally sealed on October 5, 2015. That is, Trans-Pacific Partnership (TPP) as a mega Free Trade Agreement (FTA), which comprises twelve countries on the Pacific Rim, including the U.S. and Japan, will apply to 40% of the world economy.

4) The recent wave of regionalism is often referred to as 'new' regionalism vis-a-vis 'old' regionalism; that which began in Western Europe following World War Two. 'New' regionalism is generally viewed as a more 'open' and outward-looking form of its predecessor.

5) D. K. Das, *Regionalism in Global Trade*, Edward Elgar Publishing Limited, 2004, p. 5.

important step in the liberalization of international trade. The GATT/WTO framework has been essential in paving the way for these RTAs while ensuring a more multilateral and liberal trading system.

<Figure 1> Evolution of RTAs in the World (1948-2015)



Source: WTO, 2015.

The key articles in GATT which grant exceptions for the derogation to the MFN rule by allowing for RTAs include; (1) Article XXIV of GATT, pertaining to custom unions and free trade areas; (2) GATS Article V of General Agreement on Trade in Services (GATS) pertaining to RTAs in services, and finally (3) the Enabling clause, pertaining to developing countries.

The purpose of this paper is to seek appropriate measures for strengthening the multilateral trading system in the GATT/WTO system. In this context, this study begins with an examination of the debate over RTAs versus the multilateral trade rules as well as key legal, economic, and policy raised by RTAs. Here, a controversial issue is

addressed on whether RTAs are building blocks for further multilateral liberalization or stumbling blocks. In that context, this research attempts to pin a in-depth historical and contemporary overview of the proliferation of RTAs, and a comprehensive review of the debate to existing academic literature, providing a deeper consideration of the broader legal and economic meaning of the recent wave of regionalism. That is, this paper engages with the many and varied theoretical strands that could help contextualize why RTAs do proliferate, and what the deeper meaning of the proliferation is in the GATT/WTO system. Further, this study intends to go beyond a summary of the immediate global trade regime implications of ongoing complex situation.

This paper turns to an analysis of the role of GATT Article XXIV in the multilateral trade system and the meaning and effectiveness of its key provisions in response to the proliferation of RTAs under the GATT/WTO system. In that context, this study seeks to answer the question to what problems exist throughout the interpretation and application of key provisions under GATT Article XXIV, and whether these provisions are achieving what they were set out to do. Further, this paper provides proper measures for the establishment of bases for the precise interpretation of GATT Article XXIV in accordance with the WTO quasi-judicial mechanism.

Then, this paper addresses a teething problem with the WTO's institutional framework for governing the RTAs. Special emphasis is placed on the evaluation of the WTO's role in the surveillance and oversight of RTAs.

Finally, this study concludes in addressing that any trade policy attempt should ensure that RTAs are non-discriminatory, and thereby strengthen the multilateral trading system.

Ⅱ. RTAs vs. Multilateral Trade Rules

Regardless of the factors of politics or the expansion of intra-regional economic ties that drive trade regionalism and economic integration, RTAs remarkably play key roles in the global trading system and world economy. As a result, two parallel, global and regional, are now in place. The conventional policy question concerning RTAs has been whether RTAs promote the multilateral trading system and the MFN treatment.

1. RTAs Stumbling Blocks

1) External Dynamics

This perspective is based on the claim that RTAs eventually bring about a reduction in aggregate global welfare as they compete both with non-member states and with other RTAs to shift the terms of trade in each bloc's favor by raising other blocks.[6] Arguably, global welfare is diminished since RTA member's made goods are protected regardless of whther they are of the same quality or their industries are as efficient as those of their non-member counterparts.

2) Internal Dynamics

According to this perspective, RTAs provide abundant opportunities for local interest groups of trade-sensitive goods producers to manipulate both the design and operation of RTAs, but they distort the efficient flow of interstate commerce.[7]. It is argued that to a certain degree a boost in intra-bloc trade driven by preferential rules of origin is offset by corresponding disadvantages. That is, such negative preferential rules discriminate against non-member trading partners, and thus generally block world trade flows.

3) The "Spaghetti Bowl" Thesis

This perspective argues that RTAs may weaken the global system by setting up competing regulatory frameworks, creating "a global patchwork of differing trade regulations".[8] This overlapping "spaghetti bowl" (See Figure 2)[9] type of RTAs results in complex and multiple layers of regulation, such as preferential rules of origin, overlapping tariff rates and other obligations, causing difficulties for traders and customs officials all over the world.

---

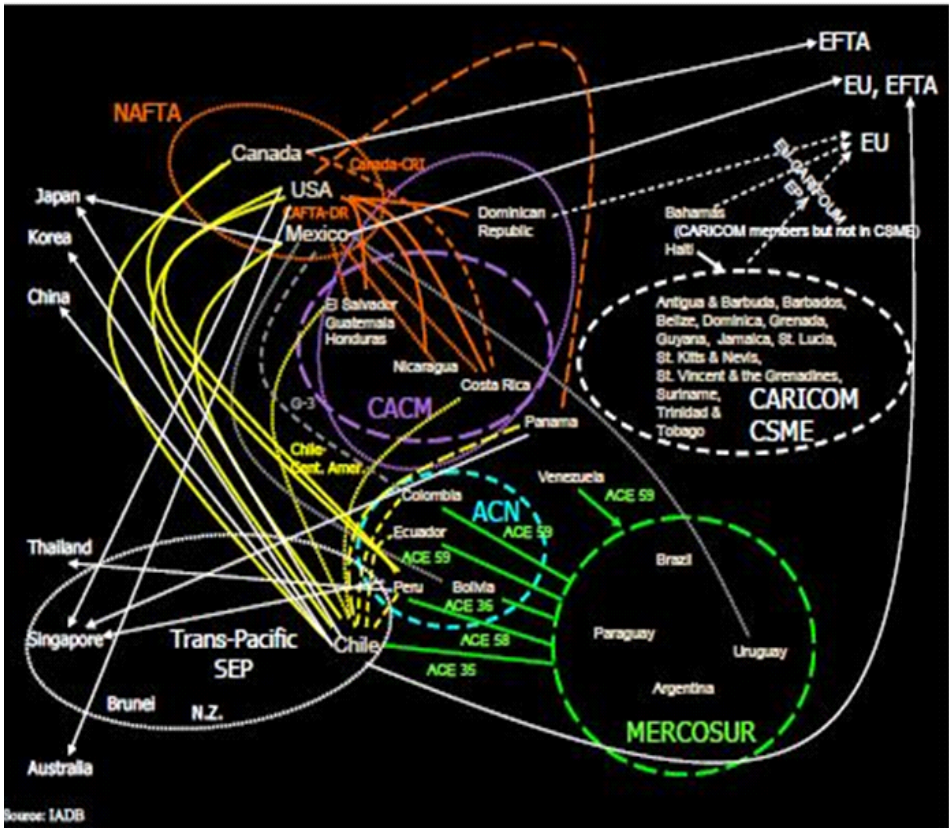
6) J. A. Frankel, *Regional Trading Blocs in the world Economic System*, Institute for International Economics, 1997, p. 1.

7) *Ibid.* p. 212.

8) WTO TPRB, *Overview of Developments in the International Trading Environment -Annual Report by the Director-General*, WT/TPR/OV/9, Feb. 20, 2004, Part 10.

9) J. Bhagwati and A. Panagariya, "Preferential Trading Areas and Multilateralism - Strangers, Friends, or Foes?"' in J. Bhagwati and A. Panagariya (eds), *The Economics of Preferential Trade Agreements*, AEI Press, 1996, pp. 7, 8~27.

<Figure 2> The Spaghetti Bowl



Source: INTRATRAD, 2012.

2. RTAs as Building Blocks

1) Laboratory Effect

This argument for RTAs derives from experimental or laboratory effect vis-a-vis multilateral trade liberalization. It is argued that once RTAs are successfully reached, the experience and lesson gained through trial and error will serve as a knowledge base,[10] and thereafter provide a valuable foundations on which subsequent multilateral trade rules can be built. Arguably, RTAs tend to provide global trade talks, and serve as test laboratories for the new trade rules in the multilateral trading system.

10) F. Bergsten, "Open Regionalism", *World Economy, vol. 20,* 1997, p. 548.

2) Regional Convergence Thesis

This view stresses RTAs lead to convergence, that is, not harmonization of trade rules across RTAs but unification of multiple overlapping trade rules with a new single list of them in a single cumulation zone.[11] Some scholars observe that multilateral rules of origin prevent trading opportunities for third parties, limit trading opportunities within RTAs by inhibiting access to competitive inputs, and increase transaction cost.[12] According to this perspective, the outcome of convergence creates "lasagna plates" (See Figure 3) from spaghetti bowl" and regional cumulation bowls, the largest would be centered on major industrial states, such as the US and the EU.[13] the evidence concerning the success of regional experiments, that is, convergence, for global trade liberalization may lessen the negative impacts associated with trade rules, in particular, rules of origin.[14]

---

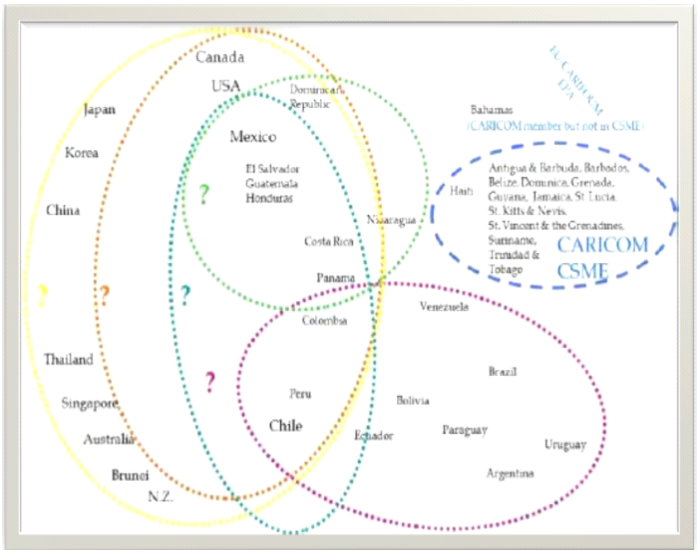
11) A. Estevadeordal, J. Harris and K. Suominen, "Harmonizing preferential rules of origin regimes and around the world', R. Baldwin and P. Low (eds.), *Multilateralizing Regionalism: Challenges for the Global Trading System*, Cambridge University Press, 2008. pp. 316~317.

12) *Ibid.* pp. 284~311. In this context, restrictiveness, and divergence in the rules of origin matter.

13) Key players in the process of convergence are each family member hub and its spokes. In this context, the "hub-and-spoke" type of RTA may cause negative impacts if the hub state prevail in its own market over other spoke states. Consequently, convergence process should be based on open regionalism rather than closed regionalism and not adopt stringent trade rules.

14) Estevadeordal, *et al., op. cit.*, pp. 316~325. The most prominent process was the establishment of the Paneuro System in the EU in 1999. This system essentially replaced all the bilateral FTA commitments between EU and Eastern European states for a single agreement.

<Figure 3> The Lasagna Plates



Source: IDB, 2012.

3) Lock-In Effect

Some observers argue that RTAs often "lock-in" preceding liberalization records or reforms in a manner that prevents subsequent backsliding.[15] This lock-in effect may attract governments of developing countries where economic reform attempts are prevented by deep solidarity of local interest groups.

3. Characteristics of RTAs in the GATT/WTO

In theory, multilateral liberalization and the MFN principle are panaceas to the world trade system. According to the conventional notion, RTAs are second-best to global trade liberalization.

The key feature of RTAs is that RTA members (parties) offer each other more favorable treatment in trade matters than they offer other trading partners. To the extent that these other trading partners are WTO member, such discriminatory treatment is not consistent with the MFN treatment obligation, one of key principle of WTO law.

15) Frankel, *op. cit.*, 10, p. 216.

However, GATT 1994 and GATS allow, in certain circumstances, RTAs establishing customs unions or free trade areas as noted below. WTO law also recognizes the advantages of economic integration and trade liberalization at a regional level. In the meantime the proliferation apart from economic reasons, states may also pursue regional integration driven by political reasons.[16)]

In the mean time the proliferation of RTAs pose huge challenges to the multilateral trading system. In this context, a balance should be struck between the interests of states pursuing deeper economic integration among a select group of states and the interest of states excluded from the group.

Ⅲ. GATT Article XXIV

1. Background

As mentioned above, deviation from the MFN principle in the form of RTAs has been allowed since the inception of the GATT in 1947. Around the time of the drafting of the charter of the International Trade Organization (ITO) in 1946-1947 it was clear that several of the founding parties had preferential trading schemes which would be contradictory to the MFN principle. Two salient examples of preferential arrangements include those of the British Imperial Preferences[17)] and preferences granted by the Benelux customs union.[18)] It was clear that some sort of provision was necessary to allow for these, if the constituent parties of these agreements were expected to go along with the ill-fated ITO.[19)] Another key factor for granting RTAs was clearly political and

16) The establishment of MERCOSUR, a customs union originally between Argentina, Brazil, Paraguay and Uruguay was motivated by the wish to support democracy in these states.

17) British Imperial Preferences were agreements were preferential treatment was granted between dominions and colonies within the British Empire.

18) The Benelux customs union was a union between Belgium, the Netherlands and Luxemburg established in 1944.

19) B. Onguglo, "Issues Regarding Notification to the WTO of a Regional Trade Agreement, Multilateralism and Regionalism: The New Interface", UNCTAD/DITC/TNCD/2004/7, 2004, p. 34. In 1944, at the Bretton Woods Conference, three pillars were envisaged in order to maintain international economic cooperation by industrialized countries: the International Monetary Fund

related to the Cold war. There was the view that RTAs helped to strengthen the bonds between noncommunist countries, ensure the commitment towards capitalism and create a “united front” against the Soviet Union.[20] In summary both the existing preferential trading schemes and the political situation at the time could be seen as key factors behind the creation of GATT Art. XXIV.

2. Key Provisions of Article XXIV

Key provisions of the GATT 1994 are stipulated in Article XXIV:4, Article XXIV:5(a), and (b), Article XXIV:6, and Article XXIV:8(a) (i), (ii) and (b). Article XXIV:4 provides that a Customs Union (CU) or a Free Trade Area (FTA) should facilitate trade between constituent territories, and refrain from raising trade barriers of other contacting parties with such territories.

Ultimately Article XXIV would permit parties to form RTAs if they were willing to commit to liberalization of trade policy in the form of custom unions or free trade area s.[21] The draftsmen of Article XXIV were aware of the possible problems that could arise due to these agreements and thus were cautious in protecting the interests of third parties.[22] In order to ensure that the WTO trading system keeps on track towards the liberalization of trade, provisions were put in place for which RTA members are required to comply with. One discusses several key provisions relating that RTAs; namely those covering facilitation of trade, reciprocity in trade negotiations, coverage of trade, and systemic dynamics.[23]

(IMF), the International Bank for Reconstruction and Development, and the International World Trade Organization (ITO). The ITO could never come into existence despite the Havana Charter resulting from this promising multilateral commitment mainly due to the lack of support in the U.S. congress for yet international organization. Simultaneously with the negotiations on the Havana Charter, negotiations on a multilateral tariff-reduction treaty entered into full swing at the Geneva Conference in 1947. The result of the latter set of negotiations was the GATT 1947. See J. Jackson, *World Trade and the Law of the GATT*, Bobbs-Merrill, 1969, pp. 576~580.

20) K. Chase, "Multilateralism compromised: the mysterious origins of GATT Article XXIV", *World Trade Review* 5 (1), 2006, p. 21.

21) M. R. Islam and S. Alam, "Preferential Trade Agreements and the Scope of GATT Article XXIV, GATS Article V and the Enabling Clause: An Appraisal of GATT/WTO Jurisprudence", *Netherlands International Law Review* 26 (1), 2009, p. 6.

22) Das, *op. cit.*, 5, p. 100.

23) *Ibid.* pp. 98-99.

Several contentious and ambiguous issues relating to these provisions have been raised and accordingly Article XXIV of GATT has faced considerable criticism. Some observers brought to light the failure of Article XXIV to "function well in practice" and listed several opinions about the ambiguities, complexities and contradictions that lie within Article XXIV.[24] Consequently the inherent ambiguities would weaken Article XXIV and make it essentially unenforceable. Pomfret made the point that "no custom union or free trade agreement presented for review has complied with Article XXIV and yet every such agreement has been approved by a tacit or explicit waiver."[25] This ultimately left a large loophole for countries to circumvent the MFN principle and made it clear that the provisions laid down were ineffective.

Lastly, a key issue since the introduction of Article XXIV has been its scope. Divergent opinions exist where some argue that Article XXIV allows members to derogate from only Article Ⅰ of GATT and others insist that it allows derogation from all provisions of GATT. It has been argued however that Article XXIV should not be used as legal basis to explain trade policies and measures which are inconsistent with GATT and that it "should be understood in the light of RTA's building block function."[26]

1) Article XXIV:4

Article XXIV provides the following:

> 4. The contracting parties recognize the desirability of increasing freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries parties to such agreements. They also recognize that the purpose of a customs union or a free trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories.

The key provision, stipulated in Article XXIV paragraph 4 states that members must recognize the purpose of RTAs in facilitating trade between constituent members while not raising barriers to other contracting parties. While RTA members are prohibited to raise trade barriers above the level they were before the formation of the RTA, the issue of trade diversion should be also be examined. Viner's developments of trade creation and trade diversion theories have had a significant contribution in this field of research

---

24) Islam and Alam, *op. cit.*, 21, p. 4.
25) R. Pomfret, *The Economics of Regional Trading Agreements*, Oxford University Press, 1997, p. 76.
26) WTO, *op. cit.*, 3, p. 12.

and provide a way of examining the effects of RTA's on both constituent and outside parties.[27]

Trade diversion is the term used to describe the phenomenon when trade is diverted from the more efficient country (in this case the third party) to a less efficient country (a RTA member). The general idea is that an RTA where trade creation is greater than trade diversion should be implemented. However, this analytical approach has faced economists' fierce criticism in that the scope of its inquiry is too narrow. One observes that the original theory of customs unions drew heavily on classical exposition of the gains from trade.[28] Further, this critique stresses that before the establishment of a truly multilateral trade regime, regional trade blocs should offer substantial welfare benefits to member states of regional trade blocs.[29] Viner's theory ignored the potential gain through increased economic growth and foreign competition within a customs union. More importantly, the possible welfare benefits of foreign competition might be quite substantial in a world with imperfect competition. Therefore, it can be concluded that not only static aspects of economic welfare, but also certain other socio-political concerns associated with RTAs should be considered in supporting or opposing the establishment of RTAs.

The Appellate Body in *Turkey-Textiles* held that the provisions of Article XXIV should be interpreted in the context stipulated in Article XXIV: 4 through a process of "constant reference to the purpose".[30]

2) External Liberalization Requirement under Article XXIV:5

Another key provision is related to the systemic dynamics of RTAs. The three forms of agreements Article XXIV provide for include custom unions, free trade areas and

---

27) J. Viner, The Customs Union Issue, The Carnegie Endowment for International Peace, 1950, pp. 18-20.

28) D. Kennedy, "Regional Trading Blocs, Multilateralism and the New GATT Agreement: An Introduction", in T. Geiger and D. Kennedy (eds.), *Regional Trade Blocs, Multilateralism, and the GATT: Complimentary Paths to Free Trade*, Printer, 1996, p. 1.

29) Kennedy argues that Viner's theory ignored the potential gain through increased economic growth and foreign competition within a customs union.

30) *Turkey-Restrictions on Imports of Textiles and Clothing Products*, WTO Doc. WT/DS34/AB/R, Report of the Appellate Body, para. 58. India argued Turkey's quantitative restrictions on textiles and clothing applied by the EC were inconsistent with the Agreement on Textile and Clothing (ATC). Turkey appealed the Panel's Report in favor of India.

interim agreements. According to paragraph 5 of Article XXIV an interim agreement should (a) lead to the formation of a customs union or free trade agreement (FTA), (b) contain a plan and schedule to achieve this formation, and (c) accomplish this within a reasonable period of time.

This external requirement for RTAs, in particular, that other regulations (ORC) shall not be more restrictive than those of pre-RTAs, includes an economic concern that an RTA should not cause trade diversion effects.[31] It deserves noting that whereas Article XXIV:4 also addresses the same aspect of economic concern by stipulating that the purpose of RTAs "should be to facilitate trade" between parties and "not to raise barriers to the trade of other contracting parties", Article XXIV: 5 provides a more direct and independent legal obligation.[32]

On the other hand, it is noteworthy that mere trade diversion effects on balance may not make pertinent RTAs inconsistent with Article XXIV:5.[33] In this regard, notable that Article XXIV:5 prescribes the different legal requirements for duties and other regulations of commerce (ORC): "not higher" for the former and "not more restrictive" for the latter. In reality, the legality of other regulations of commerce (ORC) in respect of Article XXIV: 5 may not be easily determined despite both *ex ante* assessment of structures of regulations and *ex post* evaluation of trade effects.[34]

In relation to the inquiry, paragraph 2 of the Understanding on the Interpretation of Article XXIV (the Understanding on Article XXIV) of the GATT 1994 stipulates on Article XXIV:5 through case-by-case assessment for other regulations of commerce (ORC) as follows:

> ...It is recognized that for the purpose of the overall assessment of the incidence of other regulations of commerce for which quantification and aggregation are difficult, the examination of individual measures, regulations, products covered and trade flows affected may be required.

---

31) D. Ahn, "Foe or Friend of GATT Article XXIV: Diversity in Trade Remedy Rules", *Journal of International Economics*, 11 (1), 2008, p. 122.

32) *See* K. W. Dam, "Regional Economic Arrangements and the GATT: The Legacy of a Misconception", University of Chicago Law Review 30, 1963, p. 633.

33) J. H. Matis, *Regional Trade Agreements in the GATT/WTO Article XXIV and Internal Trade Requirement*, Springer, 2002, p. 112.

34) Ahn, *op. cit.*, 31.

As noted in the last sentence of the paragraph, the Understanding on Article XXIV doe not, however, provide the specific criteria to evaluate each case.

The Appellate Body in *Turkey-Textiles* interpreted Article XXIV:5 to imply that any measure imposed by WTO members inconsistent with GATT 1994 do not fall within the Article XXIV:5 exception unless they are "introduced upon the formation of the a customs union" and "only to the formation of the CU would be prevented if the introduction of the measures were not allowed.[35)]

Article XXIV:5 exceptions apply only to inconsistencies with GATT 1994, and thus any RTA measures inconsistent with certain other WTO agreements may not be justified. However, in *Turkey-Textiles* the Appellate Body referred to legal scholars' view that Article XXIV provides an exception for inconsistencies with the provisions of GATT,[36)] that is, paragraph 5 of the chapeau refers only to the provisions of GATT 1994 and makes no reference to the Agreement on Textile and Clothing (ATC).[37)] Nevertheless, the Appellate Body held that Article XXIV:5 could provide an exception for an inconsistency with Article 2.4 of the ATC, because the latter allows restrictions under "relevant GATT 1994 provisions".

Many elements of Article XXIV are not clear and thus lead to divergent interpretations of its disciplines.[38)] That is, there are two different perspectives on the relationship between Article XXIV and other GATT/WTO Articles and provisions: (1) that Article XXIV should be considered as a derogation only from GATT Article I, which means that RTA members should follow all other GATT/WTO provisions; and (2) that Article XXIV should be considered as a derogation from all the GATT/WTO provisions,[39)] and not just from the MFN principle. In this context, both legal and

---

35) Report of the Appellate Body, op. cit., 30, para. 46. In this case the Appellate body held on a CU and not an FTA.

36) *Ibid.*,, fn. 13.

37) Agreement on Textiles and Clothing, 1868 UNTS p. 14; Annex 1A of the Mararakesh Agreement Establishing the World Trade Organization, 1867 UNTS p. 3, Art. IX:2.

38) For an overview of systemic issues related to GATT Article XXIV, see ibid.

39) Arguably, international law on multilateral treaties generally provides that parties to a multilateral treaty may execute subsequent agreements, varying their rights and obligations between themselves, subject to the limitation that they do not modify their rights of third parties to the wider agreement. See Committee on Regional Trade Agreements, *Synopsis of "Systemic Issues related to Regional Trade Agreements*: not by the Secretariat, WTO Doc. WT/REG/W/37 (Mar. 2, 2000), para. 27(b). In this regard, the Appellate Body in *Turkey-Textiles* noted that "Article XXIV may justify a measure which is inconsistent with certain other GATT provisions". *See op. cit.*, 30.

economic work is required to resolve the fundamental ambiguity of Article XXIV in the GATT/WTO.

3) Article XXIV:6

The reciprocity of trade concessions, is a vital foundation of the multilateral trading system and thus it is not surprising that reciprocity is also a condition in the formation of RTAs. Article XXIV:6 emphasizes a 'balance of concessions', however in reality RTA rarely live up to this. Due to differences in size and development levels of the economies of constituent parties the resulting benefits for market access will clearly be different. Rationally, one could expect greater reciprocity between more analogous economies and less so as they deviate. A great example of lack of reciprocity was the banana import regime of the European Economic Community (EEC). The EEC brought up Article XXIV as a defense for its discriminatory import regime based on the Lomé Conventions.[40] The various Lomé Conventions provided duty free imports for agricultural and mineral products from African, Caribbean and Pacific countries (ACP countries)[41]. Ultimately the panel for this case rejected the EEC claim stating that the Lomé convention failed to qualify as a FTA as it did not require any corresponding concession or elimination of trade barriers from the 69 ACP countries.[42]

4) Article XXIV:8

Article XXIV:8 stiplulates the requirement for a CU and a FTA as follows:

> 8. For the purpose of this agreement:
>
> a. A customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that
>
> i. duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and

40) EEC-Import Regime for Bananas, GATT Doc. DS38/R (1994), Report of the Panel (unadopted).

41) The ACP countries were once colonies of the UK, Spain, and France, located in Africa, Caribbean, and the Pacific.

42) Islam and Alam, *op. cit.*, 21, p. 8.

> ii. subject to the provisions of paragraph 9, substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union;
>
> b. A free-trade area should 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.

Overly narrow scope of non-exhaustive illustratively listed provisions in the exception parenthesis causes ambiguity as to the meaning of the phrase "other restrictions of commerce" (ORRCs). In Turkey-Textiles the Panel interpreted "other regulations of commerce" (ORC) broadly to include "any regulation having an impact on trade (such as customs valuation, environmental standards, Sanitary and Phytosanitary standards).[43] Despite this interpretation, it is ambiguous whether ORRCs as trade remedies including antidumping duties, countervailing duties and safeguard measures may be applied to RTA partners, or they should be exempted from such measures.[44]

With respect to trade coverage. Article XXIV:8 requires that the reduction and removal of trade barriers cover "substantially all trade". Some observers can point out the paradoxical nature of this requirement as it is expected that as the ambit of a RTA increases so does the level of discrimination; thus making such an agreement economically unsound.[45] This can also be explained by considering both dynamic aspects of substantial welfare benefits and socio-polical concerns associated with RTAs. Merits to the "substantially all trade" requirement also exist. It a can be seen as important in preventing the temptation and political pressure to minimize tariff concessions, especially in import-competing sectors and is also useful for counteracting the use of narrow sectoral arrangements like that of the Lomé Convention discussed above.[46]

The key issue and most salient ambiguity lie in methodology of the evaluation of the term "substantially all trad". The WTO noted there have been two approaches to the evaluation of this term, one being a quantitative approach and the other being qualitative.

---

43) *Turkey-Restrictions on Imports of Textiles and Clothing Products*, WTO Doc. WT/DS34/AB/R, Report of the Panel, para. 9, 120. The panel noted that this is an evolving concept.

44) Islam and Alam, *op. cit.*, 21, p. 14.

45) *Ibid.*,. p. 14.

46) Das, *op. cit.*, 5, p. 99.

The quantitative approach is generally seen as placing a statistical benchmark such as a certain percentage of trade between the constituent parties. For the qualitative approach, on the other hand, "substantially all trade" is viewed as a comprehensive term in that no sector should be left out of the RTAs liberalization.[47] The lack of one standard criteria across the board such as a fixed level for the statistical benchmark can lead to disagreements in the assessment of RTAs.

Ⅳ. Strengthening the Multilateral Trading System

1. Enhancement of WTO Surveillance and Supervision of RTAS

What could and should the WTO to enhance WTO surveillance over RTAs for the 21st century? Since the GATT/WTO rules on RTAs are not broken, it is worth asking what should be done about them. Here the focus is placed on WTO's institutional content, and on more feasible approach for the reform of the rules. A vehicle to take forward reform measures to enhance WTO's role in the surveillance of RTAs is the Committee on Regional Trade Agreements (CRTA).

Up until the inauguration of the WTO, working parties were established on a case by case basis where they would review any potential RTAs. That is, the increase in RTAs during the late 1980s and early 1990s led to create administrative vehicle.[48] In the circumstances, the Committee on Regional Trade Agreements (CRTA), established in February 1996, would replace the existing working parties in examining individual

---

47) WTO, *op. cit.*, 3, p. 21. Even though the Understanding on the Interpretation of Article XXIV of GATT notes the exclusion of any major sector of trade as the diminution to the expansion of world trade, this issue has remained contentious. On the other hand, the panel and Appellate Body in *Turkey-Textiles* found that the phrase "substantially all" encompassed both quantitative and qualitative components. *See op. cit.*, 30, para.49. In this case, the Appellate Body noted that substalntially all trade is not the same as all trade, but considerably more than some of the trade. *See op. cit.*, 30, para.48.

48) *See* the Understanding on the Interpretation of Article XXIV of GATT 1994.
During the Uruguay Round, in order to clarify GATT Article XXIV, members agreed to the Understanding on GATT Article XXIV, which clarifies and by the interpretation of any issues of procedural nature other than issues of substantive nature.

regional agreements and also analyze the systemic implications of RTAs on the multilateral trading system. The examination process is seen to provide the members with an opportunity to evaluate the consistency of any RTA with WTO rules and ensure transparency. The CRTA dealings with systemic issues (Questions of cross-cutting concern) under a three pro-longed approach mainly encompass legal analyses of relevant WTO provisions, horizontal comparisons of RTAs and a debate on the context and economic aspects of RTAs.

In this regard, GATT Article XXIV:7 provides the obligation of RTA members to notify other members for RTAs.[49] Nevertheless, up until the launch of Doha Ministerial Conference in November 2001,[50] the CRTA had resulted in little progress on the mandate of consistency assessment due to the lack of consensus. First, this problem arises from possible links between CRTA-consistency judgement and the dispute settlement process. Additionally, it is due to long-standing controversies about the interpretation of key provisions under GATT Article XXIV against the assessment of RTAs. Third, it derives from institutional problems either from the absence of WTO rules, such as preferential rules of origin, or from discrepancies between WTO rules stipulated in RTAs.

A further effort to create more effective WTO surveillance over RTAs in July 2006, established on a provisional basis a new WTO Transparency Mechanism for RTAs (TM).[51] Its two principal objectives are to examine individual RTAs, and to consider the systemic implications of RTAs for the multilateral trading system and their inter-relationship.[52] The TM, in accordance with paragraph 47 of Doha Ministerial declaration, requires early announcement of new RTA negotiations by the identification of affected WTO provisions accompanied by the full text.[53]

---

49) *See also* para. 7 of the Understanding on the Interpretation of Article XXIV of GATT 1994.

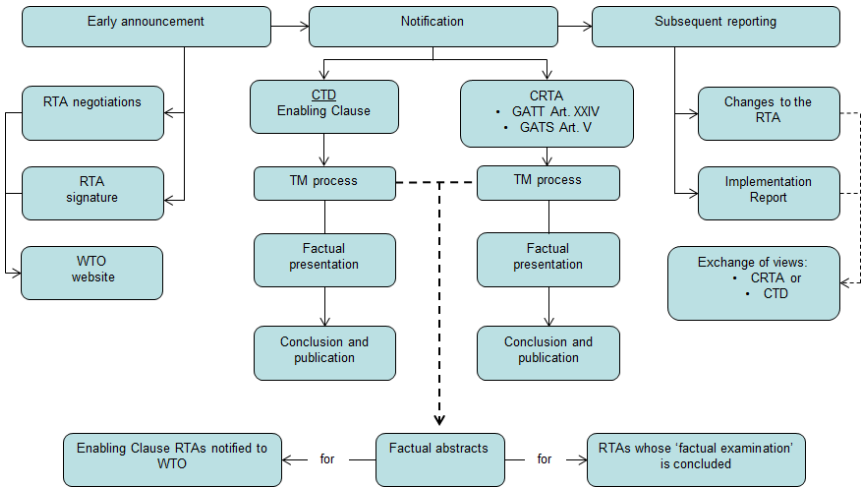
50) WTO, *Ministerial Declaration*, WTO Doc. WT/Min(01)/DEC/1 (20 November 2001) (Doha Ministerial Declaration); WTO, *Transparency Mechanism for Regional Trade Agreements* , WTO Doc. WT/Min(01)/DEC/1 (20 November 2001) (Doha Ministerial Declaration).

51) WTO, *Transparency Mechanism for Regional Trade Agreements*, WTO Doc. WT/L/671 (18 December 2006) (Decision on Transparency Mechanism).

52) This approach follows the precedent of Trade Policy Review Mechanism (TPRM) which was authorized and applied provisionally after the Montreal mid-term review in 1988 until the conclusion of the Uruguay Round accords. A new TPRM was created under the Understanding on the Article XXIV of the GATT 1994 to monitor the trade policies of members See G. Hufbauer and J. Schott, "Fitting Asia-Pacific agreements into the WTO system", R. Baldwin and P. Low (eds.), *Multilateralizing Regionalism: Challenges for the Global Trading System*, Cambridge University Press, 2009. p. 615.

53) *Ibid.*, para. 3.

<Figure 4> WTO process for RTAs according to the Decision on RTA Transparency



As in Figure 4, upon the notification of all parts of the agreement to the WTO, the examination process should start in accordance with a precise timetable and generally be ended within one year after the date of notification.[54] The necessary data, such as electronic versions, should be submitted by the parties within ten weeks of notification (for twenty weeks for developing countries).[55] The Secretariat is charged with the preparation of a factual presentation of all notified RTAs which cover trade in goods and/or services.[56] However, the mechanism prohibits the Secretariat report from making any value judgement and preclude the use of report in any dispute settlement.[57]

As noted, the WTO has made efforts to strengthen its oversight over RTAs through the creation of the TM under the CRTA. Nevertheless, a few problems remain. The capacity to provide the necessary data in time, and the quality of submitted data vary from member to member.[58] In addition, the time periods for the examination process have been deemed too short by members.[59] There is another issue of the periodicity

54) *Ibid.*, para. 6.
55) *Ibid.*, paras. 7 and 8.
56) *Ibid.*, para. 7(b).
57) *Ibid.*,. paras. 9 and 10. Likewise, the TPRM was not intended to serve as a basis for the enforcement of specific obligations under the GATT 1994 or for dispute settlement procedures, or to impose new policy commitments on members in accordance with Annex 3 of the Marrakesh Agreement.
58) R. V. Fiorentino, J. Crawford and C. Toqueboeuf, "The Landscape of regional trade agreements and WTO surveillance", R. Baldwin and P. Low (eds.), *Multilateralizing Regionalism: Challenges for the Global Trading System*, Cambridge University Press, 2009. p. 63.

of data to be used in the factual presentation. That is, even if the parties should provide import statistics for the most recent three years before the notification of the RTA, some members would not sanction the use of post-entry-into-force data in the factual presentation due to their concern over a misinterpretation of data.[60] In addition, some observers criticize the notification requirements under the mechanism in that the data required relate mainly to tariffs, quotas, and safe guard measures other than trade remedies or other regulatory policies conferring preferences on RTA members' firms.[61] More important ongoing issue remains that further efforts in the long term should be made to accommodate into GATT/WTO framework on a more permanent basis.[62]

2. Establishment of Bases for the Precise Interpretation of GATT Article XXIV

Now a more feasible approach than unconditional open access is to define and enforce current rules more precisely. However, the ambiguity of key provisions of GATT Article XXIV causes very wide interpretation of them. As noted, "substantially all trade" has at least four interpretations, such as a percentage of trade between the RTAs parties, most commonly noted 90, 85, and 80 percent by a quantitative approach. Moreover, a qualitative approach providing that any sector, or any more sector at least should not be kept from liberalization, with wide variance of sector definitions.

Similarly, there is no clear agreement on the precise meaning of "other restrictive regulations of commerce" (ORRCs). RTAs carry several trade rules, such as tariff rate quotas, safeguards, anti-dumping regulations, non-tariff measures, and rules of origin. A more constraining view of ORRCs is arguably necessary to ensure that trade rules stipulated under RTAs are non-discriminatory and strengthen the multilateral trading system. These teething problems may be resolved by contextualizing DSB's decisions that constitute the definitive interpretation of GATT Article XXIV. Also, the problems

---

59) *Ibid.* Under the TM, time periods are set for comments from the parties to the first draft of the factual presentation and for members' questions and replies.

60) *Ibid.*, pp. 63~64.

61) Hufbauer and Schott, *op. cit.*, 52, p. 616.

62) Fiorentino, et al., *op. cit.*, 58, p. 64. In reality, there is a long way to go. As argued by some scholars, WTO members as always favor their "don't ask too much, don't tell too much" policy toward RTAs, because they are concerned that their own RTAs may come under scrutiny. See Hufbauer and Schott, op. cit., 52, p. 617.

may be resolved by making future subsequent panels give quasi-judicial deference to them with binding precedential value. In doing so, bases for the precise interpretation of the GATT Article XXIV may be established in accordance with the DSB's decisions.

3. Other Considerations

In reality, there is a need to embrace increasing opportunities of RTAs motivated by key political economy and foreign policy incentives. In this regard, there have been several policy proposals to ensure that RTAs are non-discriminatory, and strengthen the multilateral trading system in the GATT/WTO.[63] These policy attempts deserve noting in helping the WTO avoid a situation where negative aspects of RTAs, and arguably promote multilateralization.

Most importantly, it is inevitable to reform WTO's decision-making process of achieving consensus for strengthening the multilateral trading system in the 21st century. In other words, global efforts should be made to restructure the WTO for the renewed multilateral trade liberalization in the GATT/WTO.[64] Last but not the least, the GATT/WTO framework has been essential in paving the way for RTAs while ensuring a more multilateral and liberal trading system.

V. Conclusion

The large increase in RTAs since the late 1980's has challenged the foundations of the WTO multilateral trading system. While RTAs can be seen to be contradictory to the overall aim of the WTO they were allowed for in Article XXIV of GATT conditional to certain provisions. As argued above, failure of compliance and subsequently enforcement of these provisions could be seen as a serious flaw of Article

63) These policy proposals include rule convergence, that is the convergence of RTA provisions, such as complicated rules of origin, and the multilateralization of RTA regulations, etc. For the detail, see generally, R. Baldwin and P. Low (eds.), Multilateralizing Regionalism: *Challenges for the Global Trading System*, Cambridge University Press, 2009.

64) *See* K. Jones, *Reconstructing the World Trade Organization for the 21st Century: An Institutional Approach*, Oxford University Press, 2015, pp. 239~243.

XXIV since the inception of GATT system.

Many elements of GATT Article XXIV are not clear and thus lead to divergent interpretations of its disciplines. This considerable divergence in opinions arises from both ambiguities throughout the provisions such as a precise definition of "substantially all trade" and "other restrictive regulations of commerce" (ORRCs) respectively, and lack of fixed methodology for the measurement of each term. In this regard, both economic and legal work is required to keep up with constantly changing nature of the world trading system.

Further, global efforts are required to resolve another teething issue of WTO's problematic institutional framework on GATT/WTO's oversight and surveillance of RTAs. In other words, enhancing GATT/WTO requirements for RTAS, which improves the CRTA's decision-making mechanism, and thereby strengthens the multilateral trading system.

The GATT/WTO framework has been essential in paving the way for these RTAs while ensuring a more multilateral and liberal trading system. To sum up, global efforts should be made to restructure the WTO for the renewed multilateral trade liberalization in the GATT/WTO.

Consequently, more in-depth work should be done to increase the sophistication of the argument for strengthening the multilateral trading system, because this study may raise more questions than it answers. If engaging with theoretical works on international economics and trade law at least succeeded in contextualizing this research within an academic strand, it could further identify more fundamental issues which will strengthen the GATT/WTO's multilateral trading system in action. Hopefully, it would be the achievement of this study.

References

Ahn, D., "Foe or Friend of GATT Article XXIV: Diversity in Trade Remedy Rules", *Journal of International Economics, vol.* 11, No. 1, 2008.

Bergsten, F., "Open Regionalism", *World Economy, vol.* 20, 1997.

Bhagwati, J. and Panagariya, A., "Preferential Trading Areas and Multilateralism - Strangers, Friends, or Foes?"' in Bhagwati, J. and Panagariya, A. (eds), The Economics of Preferential Trade Agreements, AEI Press, 1996.

Chae, H. B., "Legal issues of 'Zeroing' Practice Based on the Article 2.4.2 of the WTO Anti-Dumping Agreement", *The International Commerce and Law Review*, vol. 38, 2008. 5.

Chase, Kerry, "Multilateralism compromised: the mysterious origins of GATT Article XXIV", *World Trade Review*, vol. 5, No. 1, 2006.

Dam, K. W., "Regional Economic Arrangements and the GATT: The Legacy of a Misconception", University of Chicago Law Review, vol. 30, 1963.

Das, D. K., *Regionalism in Global Trade*, Edward Elgar Publishing Ltd. 2004.

Estevadeordal, A., et al., "Harmonizing preferential rules of origin regimes and around the world", Baldwin, R. and Low, P. (eds.), *Multilateralizing Regionalism: Challenges for the Global Trading System*, Cambridge University Press, 2009.

Fiorentino, R. V., et al., "The Landscape of regional trade agreements and WTO surveillance', Baldwin, R. and Low, P. (eds.), *Multilateralizing Regionalism: Challenges for the Global Trading System*, Cambridge University Press, 2009.

Hufbauer, G. and Schott, J., "Fitting Asia-Pacific agreements into the WTO system", Baldwin, R. and Low, P. (eds.), Multilateralizing Regionalism: Challenges for the Global Trading System, Cambridge University Press, 2009.

IDB, *Regional Trade Agreements: Development Challenges and Policy Options*, Paper for the ICTSD-IDB E-15 dialogue on RTAs, 2012.

Islam, M. R. and Alam, S., "Preferential Trade Agreements and the Scope of GATT Article XXIV", GATS Article V and the Enabling Clause: An Appraisal of GATT/WTO Jurisprudence", *Netherlands International Law Review*, vol. 26, No. 1, 2009.

Jackson, J., *World Trade and the Law of the GATT*, Bobbs-Merrill, 1969.

Jones, K., *Reconstructing the World Trade Organization for the 21st Century: An Institutional Approach*, Oxford University Press, 2015.

Kennedy, D., "Regional Trading Blocs, Multilateralism and the New GATT Agreement: An Introduction", in Geiger, T. and Kennedy, D. (eds.), *Regional Trade Blocs, Multilateralism, and the GATT: Complimentary Paths to Free Trade 1,* Printer, 1996.

Lee, K. B., "The International Arbitration System for the Settlement of Investor-State Disputes in the FTA", *The International Commerce and Law Review,* vol. 38, 2008. 5.

Lyou, B. W., "WTO GATs and Disputes on Trade in Service", *The International Commerce and Law Review*, vol. 53, 2012. 2.

Matis, J. H., *Regional Trade Agreements in the GATT/WTO: Article XXIV and Internal Trade Requirement*, Springer, 2002.

Onguglo, B., "Issues Regarding Notification to the WTO of a Regional Trade Agreement", in *Multilateralism and Regionalism: The New Interface*, UNCTAD/DITC/TNCD/2004/7, 2004.

Pomfret, R., *The Economics of Regional Trading Agreements*, Oxford University Press, 1997.

Viner, J., *The Customs Union Issue*, The Carnegie Endowment for International Peace, 1950.

WTO, *Regional Trade Agreements and Preferential Agreements*, available at http://www.wto.org/english/tratop_e/region_e/rta_pta_e.htm (last visited Nov. 28, 2015).

WTO, Ministerial Declaration, WTO Doc. WT/Min(01)/DEC/1, November 20, 2001.

WTO, Transparency Mechanism for Regional Trade Agreements, WTO Doc. WT/Min(01)/DEC/1, November 20, 2001.

WTO, "Synopsis of 'Systemic' Issues Related to Regional Trade Agreements", *not by the Secretariat*, WTO Doc. WT/REG/W/37, 2000.

ABSTRACT

Regional Trade Agreements: Exceptions to the MFN Principle in the GATT/WTO System

In-Sop PAK

The large increase in RTAs since the late 1980's has challenged the foundations of the multilateral trading system, and thereby has become an axis in the GATT/WTO system. While RTAs can be seen to be contradictory to the overall aim of the WTO, they were allowed for in Article XXIV of GATT conditional to certain provision. The failure of compliance and subsequently enforcement of these provisions could be seen as a serious flaw of Article XXIV since the inception of GATT system.

Many elements of GATT Article XXIV are not clear and thus lead to divergent interpretations of its disciplines. This considerable divergence in opinions arise from both ambiguities throughout the provisions under GATT Article XXIV. In this regard, both economic and legal work is required to keep up with constantly changing nature of the world trading system. Further, global efforts are required to resolve another teething issue of WTO's problematic institutional framework on GATT/WTO's oversight and surveillance of RTAs. and thereby strengthen the multilateral trading system.

Needless to say, the GATT/WTO framework has been essential in paving the way for RTAs while ensuring a more multilateral and liberal trading system. Consequently, global efforts should be made to restructure the WTO for the renewed multilateral trade liberalization in the GATT/WTO.

Keywords : GATT, WTO, Multilateral Trading System, MFN, RTA