Bilateral and Regional Trade Agreements

Case Studies

Edited by
SIMON LESTER AND
BRYAN MERCURIO

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BILATERAL AND REGIONAL TRADE AGREEMENTS

As the Doha Development Round trade negotiations have stalled, bilateral and regional free trade agreements have become an important alternative. These agreements have proliferated in recent years, and now all of the major trading countries are engaging in serious bilateral trade negotiations with multiple trading partners.

This book provides a comprehensive study of recent bilateral and regional trade agreements. There are two main aspects. First, it situates bilateral and regional trade agreements in the context of economics, international law and international relations. Second, it surveys the most important recent agreements in relation to each substantive topic covered (e.g. intellectual property, investment, services and social policy) and provides an overview of the law being created in these areas.

SIMON LESTER is the co-founder and President of www.WorldTradeLaw.net.

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BILATERAL AND REGIONAL TRADE AGREEMENTS

COMMENTARY AND ANALYSIS

Edited by

SIMON LESTER

BRYAN MERCURIO

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Simon Lester thanks his family, in particular his wife and business partner Kara Leitner for her continued personal support and willingness to provide substantive comments on all of his writing endeavours.

FOREWORD

This two-volume book provides a critical addition to the literature on international trade law. In chapters that carefully describe and analyse a complex web of multilateral regional and bilateral trade agreements, this collection shows how, why, when and to what extent states have negotiated and signed regional and bilateral trade agreements in recent years.

It is well recognised by now that the landscape of international trade agreements has changed dramatically over the past decades – from bilateral agreements in the early nineteenth century to the growth of multilateralism and regionalism under the GATT and its successor, the WTO. Until fairly recently, the focus of international trade law was, for the most part, the GATT/WTO, the European Community, the NAFTA and MERCOSUR. However, following the 1999 Seattle Ministerial Conference of the WTO, we have now entered a period that has resurrected bilateralism and created a new form of 'loose' regionalism. As a result of the proliferation of such agreements, international trade law now consists of hundreds of new agreements, usually between just two countries, although sometimes more.

Illustrating the changing cycle of such agreements, this collection identifies the multi-faceted evolution of trade agreements and provides the first comprehensive look at the 'law and policy' of this recent wave of 'preferential' trade agreements (PTAs). The first volume explores different kinds of PTAs, situating each in its particular social, political, economic and cultural context, and offering an assessment of the substantive law of these agreements. The second volume consists of various case studies, which not only analyse the results of each particular trade agreement, but also show the practical side of how the agreements are negotiated. In both volumes, the authors have drawn on their own specialised knowledge of these topics, and the editors should be commended for assembling such an impressive team of contributors. Not only have the editors selected well-credentialed contributors, but they have also been careful to include contributors from academia, practising lawyers and government officials, so as to strike an appropriate balance and appeal to a wide-ranging audience.

The book is important, not simply because it identifies an assortment of trade agreements, but because it demonstrates the manner in which and extent to which they work differently and to different ends. Recognising that trade agreements vary from little more than 'treaties of friendship' to agreements supporting significant

economic integration, the contributors explore the extent to which such agreements are used to enhance domestic interests, promote foreign policy and build ever more inventive economic, political, social and cultural alliances. Demonstrating that trade agreements once were centrally preoccupied with the reduction of tariffs, the book shows how trade agreements often transcend tariffs, how they govern investment, intellectual property, labour, the environment, human rights and, ultimately, the domestic policies of states. As the scope of the agreements has expanded from formulaic tariff reductions, the legal and policy issues have become much more complicated. Whereas the previous debate involved mostly the question of how high tariffs should be, the law of today's PTAs asks diverse questions such as: how strongly should intellectual property be protected; how should intellectual property protection relate to access to medicines in poor countries; what impact does trade liberalisation have on labour rights, human rights, and environmental protection; and how should the rights of foreign investors be balanced with the ability of states to regulate. This two-volume set provides a high level of discussion of these issues in the context of the growing body of PTAs.

Nor do the essays in this book avoid controversy. Challenging the perception that free trade agreements are invariably 'free', several chapters reveal the extent to which trade agreements are used to both regulate and constrain trade. They also demonstrate why trade agreements are often appropriately referred to as 'preferential trade agreements'.

Finally and significantly, the editors will undertake in the future to supplement this two-volume collection in response to changes in the continually evolving trade environment. As the landscape grows, the editors will continue to survey it, tracing the path of the evolving field of international economic law. In this way, they will make a lasting contribution to the interdisciplinary landscape that will mark the Twenty First Century trade agreement.

Leon Trakman
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Antoine Goetz and others v. *Republic of Burundi*, ICSID Case No ARB/95/3, (Award of 10 February 1999)
Asian Agricultural Products Ltd. (AAPL) v. *Republic of Sri Lanka*, ICSID Case No ARB/87/3, (Award of 27 June 1990)
Azurix Corp. v. *Argentine Republic*, ICSID Case No ARB/01/12 (US/Argentina BIT), (Award of 14 July 2006)
CME Czech Republic BV (The Netherlands) v. *The Czech Republic*, UNCITRAL (Netherlands/Czech Republic BIT), (Partial Award of 13 September 2001)
CMS Gas Transmission Company v. *Argentine Republic*, ICSID Case No ARB/01/8 (US/Argentina BIT), (Award of 12 May 2005)
Emilio Agustin Maffezini v. *The Kingdom of Spain*, ICSID Case No ARB/97/7, Decisions of the Tribunal on Objections to Jurisdiction (25 January 2000)
Marvin Roy Feldman Karpa (CEMSA) v. *United Mexican States*, ICSID Case No ARB (AF)/99/1, (Award of 16 December 2002)
Metalclad Corporation v. *United Mexican States*, ICSID Case No ARB(AF)/97/1, (Award of 30 August 2000)
Methanex Corp v. *United States*, NAFTA Ch 11 Arbitral Tribunal Decision of the Tribunal on Petitions from Third Persons to Intervene as 'Amici Curiae' (15 January 2001); (Award of 9 August 2005)
Mondev International Ltd v. *United States of America*, ICSID Case No ARB (AF)/99/2, (Award of 11 October 2002)
MTD Equity Sdn Bhd & MTD Chile SA v. *Chile*, ICSID Case No ARB/01/7 (Malaysia/Chile BIT), Decision on Annulment (21 March 2007)
Occidental Exploration and Production Company v. *Republic of Ecuador*, LCIA Case No UN 3467, (Final Award of 1 July 2004)
Plama Consortium Limited v. *Republic of Bulgaria*, Decision on Jurisdiction, ICSID Case No ARB/03/24, Decision on Jurisdiction (8 February 2005)
Pope & Talbot Inc v. *Government of Canada*, NAFTA Ch 11 Arbitral Tribunal (Interim Award of 26 June 2000); (Award of 10 April 2001)
PSEG Global Inc., *The North America Coal Corporation and Konya Ilgin Elektrik Üretim ve Ticaret Limited Sirketi* v. *Republic of Turkey*, ICSID Case No ARB/02/05, (Award 19 January 2007)
Revere Copper & Brass, Inc v. *Overseas Private Investment Corp*, (Award of 24 August 1978), 56 ILR 258 (1978); 17 ILM 1321 (1978)
Robert Azinian and others v. *The United Mexican States*, ICSID Case No. ARB (AF)/97/2, (Award of 1 November 1999)
Ronald S. Lauder (USA) v. *The Czech Republic*, UNCITRAL (United States/Czech Republic BIT), (Final Award of 3 September 2001)
Salini Contruttori SpA and Italstrade SpA v. *The Hashemite Kingdom of Jordan*, ICSID Case No ARB/02/13 (Italy/Jordan BIT), Decision on Jurisdiction (9 November 2004)
Salini Costruttori SpA and Italstrade SpA v. *Kingdom of Morocco*, ICSID Case No ARB/00/4 (Italy/Morocco BIT), Decision on Jurisdiction (23 July 2001)

Saluka Investments BV (The Netherlands) v. *The Czech Republic*, UNCITRAL, (Partial Award of 17 March 2006)
SD Myers Inc v. *Government of Canada*, NAFTA Ch 11 Arbitral Tribunal; (Partial Award of 13 November 2000); (Award of 10 April 2001); (Final Award of 30 December 2002)
Siemens AG v. *The Argentine Republic*, Decision on Jurisdiction, ICSID Case No ARB/02/8 (Germany/Argentina BIT), Decision on Jurisdiction (3 August 2004)
Suez, Sociedad General de Aguas de Barcelona S.A. and InterAguas Servicios Integrales del Aguas SA v. *The Argentine Republic*, ICSID Case No ARB/03/17, Decision on Jurisdiction (16 May 2006)
Tecnicas Medioambientales Tecmed SA v. *United Mexican States*, ICSID Case No ARB (AF)/00/2 (Spain/Mexico BIT), (Award of 29 May 2003)
Telenor Mobile Communications v. *The Republic of Hungary*, ICSID Case No ARB/04/15 (Norway/Hungary BIT), (Award of 13 September 2006)
The Loewen Group, Inc. and Raymond L. Loewen v. *United States of America*, ICSID Case No ARB(AF)/98/3 (NAFTA), (Award of 26 June 2003)
United Parcel Service of America, Inc v. *Government of Canada*, NAFTA Ch 11 Arbitral Tribunal, Respondent's Counter-Memorial (22 June 2005)
Waste Management Inc v. *United Mexican States*, ICSID Case No ARB(AF)/98/2, (Award of 2 June 2000)

Iran–United States Claims Tribunal

Amoco International Finance Corp v. *Islamic Republic of Iran*, (Award No 310–56–3 of 14 July 1987) (Chamber 3), 15 Iran–US CTR 189
Sea-Land Services, Inc v. *The Government of the Islamic Republic of Iran, Ports and Shipping Organization*, (Award No 135–33–1 of 22 June 1984), 6 Iran–US CTR 149
Sedco Inc v. *National Iranian Oil Company*, (Award ITL 59–129–3 of 27 March 1986), 10 Iran–US CTR 189
Starrett Housing Corp v. *Islamic Republic of Iran*, (Award No ITL 32–24–1 of 19 December 1983), 4 Iran–US CRT 122
Tippets, Abbett, McCarthy, Stratton v. *TAMS-AFFA Consulting Engineers of Iran*, (Award No 141–7–2 of 22 June 1984), 6 Iran–US CRT 219

NAFTA Chapter 19 & 20 Disputes

NAFTA Ch 19 Panel Decision, *In the Matter of Certain Top-Mount Electric Refrigerators, Electric Household Dishwashers, and Gas or Electric Laundry Dryers*, CDA–USA–2000–1904–03 (15 April 2002)
NAFTA Ch 20 Panel Report, *In the Matter of Cross-Border Trucking Services*, USA–MEX–98–2008–01 (6 February 2001)
NAFTA Ch 20 Panel Report, *Tariffs Applied by Canada to Certain US-Origin Agricultural Products*, CDA–95–2008–01 (2 December 1996)

Permanent Court of Arbitration

North Atlantic Coast Fisheries Arbitration (United States v. *Great Britain)* (1910)
11 RIAA 167

United States Domestic Litigation

Crosby v. *National Foreign Trade Council* 120 SCt 2288 (2000)
Eldred v. *Ashcroft*, 537 US 186 (2003)

United States–Mexico General Claims Commission

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TABLE OF TREATIES AND INTERNATIONAL AGREEMENTS

(1) *International Conventions and Treaties*

Short Title	Long Title	Status
Basel Convention	Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal	Signed at Basel on 22 March 1989; in force 5 May 1992
Berne Convention	Berne Convention for the Protection of Literary and Artistic Works	Adopted in Berne on 9 September 1886; completed at Paris on 4 May 1896; revised 13 November 1908 (Berlin); completed 20 March 1914 (Berne); revised 2 June 1928 (Rome); revised 26 June 1948 (Brussels); revised 14 July 1967 (Stockholm); revised 24 July 1971 (Paris); amended 28 September 1979
Brussels Sugar Convention	Brussels Sugar Convention of 1902	Signed at Brussels on 5 March 1902; in force 1 September 1903
Cartagena Protocol	Cartagena Protocol on Biosafety to the Convention on Biological Diversity	Adopted in Montreal on 29 January 2000; in force 11 September 2003
CITES	Convention on International Trade in Endangered Species of Wild Fauna and Flora	Signed at Washington, DC, on 3 March 1973; in force 1 July 1975
CCAMLP	Convention for the Conservation of Antarctic Marine Living Resources	Signed at Canberra on 20 May 1980; in force 7 April 1982
Cultural Expressions Convention	Convention on the Protection and Promotion of the Diversity of Cultural Expressions	Adopted in Paris by the United Nations Educational, Scientific and Cultural Organization

(1) (*cont.*)

Short Title	Long Title	Status
		(UNESCO) on 20 October 2005; in force 18 March 2007
Havana Charter	Havana Charter for an International Trade Organization	Signed at Havana on 24 March 1948; never ratified
IATTC	Convention for the Strengthening of the Inter-American Tropical Tuna Commission	Signed at Washington, DC on 31 May 1949; in force 3 March 1950; Protocol of Amendment adopted on 11 June 1999, not yet in force; Convention for the Strengthening of IATTC adopted on 23 July 2003, not yet in force
ICJ Statute	Statute of the International Court of Justice	Established by the UN Charter, signed 26 June 1945; in force 24 October 1945
ILO Declaration	International Labour Organization on Fundamental Principles and Rights at Work	Adopted in Geneva by the General Conference of the International Labour Organization (ILO) during its 86th Session on 18 June 1998
London Convention	Convention on the Prevention of Marine Pollution by Dumping of Wastes and Other Matter	Signed at London on 13 November 1972; in force 30 August 1975
Montreal Protocol	Montreal Protocol on Substances that Deplete the Ozone Layer	Signed at Montreal on 16 September 1987; in force 1 January 1989
Paris Convention	Paris Convention for the Protection of Industrial Property	Signed at Paris on 20 March 1883; revised at Brussels on 14 December 1900, at Washington on 2 June 1911, at The Hague on 6 November 1925, at London on 2 June 1934, at Lisbon on 31 October 1958, and at Stockholm on 14 July 1967 and as amended on 28 September 1979 Substantive provisions (Articles 1–12) in force generally on 26 April 1970 (for countries recognising the accession of the

(1) (*cont.*)

Short Title	Long Title	Status
		German Democratic Republic); 19 May 1970 (for countries not recognising the accession of the German Democratic Republic) Administrative provisions (Articles 13–30) in force generally on 26 April 1970
Ramsar Convention on Wetlands	Convention on Wetlands of International Importance, especially as Waterfowl Habitat	Signed at Ramsar on 2 February 1971; in force 21 December 1975
UN Charter	Charter of the United Nations	Signed at San Francisco on 26 June 1945; in force 24 October 1945
UNCLOS	United Nations Convention on the Law of the Sea	Signed at Montego Bay, Jamaica, on 10 December 1982; in force 16 November 1994
Vienna Convention	Vienna Convention on the Law of Treaties	Signed at Vienna on 23 May 1969; in force 27 January 1980
1986 Vienna Convention	Vienna Convention on the Law of Treaties Between States and International Organizations or Between International Organizations	Signed at Vienna on 21 March 1986; not yet in force
WCT	WIPO Copyright Treaty	Adopted in Geneva by the Diplomatic Conference on 20 December 1996; in force 6 March 2002
WPPT	WIPO Performances and Phonograms Treaty (1996)	Adopted in Geneva by the Diplomatic Conference on 20 December 1996; in force 20 May 2002
Whaling Convention	International Convention for the Regulation of Whaling	Signed at Washington, DC, on 2 December 1946; in force 10 November 1948; Protocol revising the Convention signed 19 November 1956

(2) *GATT/WTO Agreements*

Short Title	Full Title	Status/Source
Agriculture Agreement	Agreement on Agriculture	Annex 1A of the WTO Agreement
Anti-dumping Agreement	Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994	Annex 1A of the WTO Agreement
Customs Valuation Agreement	Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994	Annex 1A of the WTO Agreement
DSU	Understanding on Rules and Procedures Governing the Settlement of Disputes	Annex 2 of the WTO Agreement
GATT 1947	General Agreement on Tariffs and Trade 1947	Signed 1 January 1948; in force 29 July 1948
GATT 1994	General Agreement on Tariffs and Trade 1994	Annex 1A of the WTO Agreement
GATS	General Agreement on Trade in Services	Annex 1B of the WTO Agreement
GPA 1994	Agreement on Government Procurement 1994	Annex 4(b) of the WTO Agreement
Safeguards Agreement	Agreement on Safeguards	Annex 1A of the WTO Agreement
SCM Agreement	Agreement on Subsidies and Countervailing Measures	Annex 1A of the WTO Agreement
SPS Agreement	Agreement on the Application of Sanitary and Phytosanitary Measures	Annex 1A of the WTO Agreement
TBT Agreement	Agreement on Technical Barriers to Trade	Annex 1A of the WTO Agreement
TRIMs Agreement	Agreement on Trade-Related Investment Measures	Annex 1A of the WTO Agreement
TRIPS Agreement	Agreement on Trade-Related Aspects of Intellectual Property Rights	Annex 1C of the WTO Agreement
WTO Agreement	Marrakesh Agreement Establishing the World Trade Organization	Signed 15 April 1994; in force 1 January 1995

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
ALADI/LAIA	Latin American Integration Association (Asociación Latinoamericana de Integración)	Argentina, Bolivia, Brazil, Chile, Columbia, Cuba, Ecuador, Mexico, Paraguay, Peru, Uruguay, Venezuela	Signed 12 August 1980; in force 18 March 1981
Albania–Bosnia and Herzegovina FTA	Albania–Bosnia and Herzegovina Free Trade Agreement	Albania, Bosnia and Herzegovina	Signed 28 April 2003; in force 1 December 2004
AFTA	ASEAN Free Trade Area	Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam	Signed 28 January 1992; in force 28 January 1992
ANZCERTA (*also referred to as* CER)	Australia–New Zealand Closer Economic Relations Trade Agreement	Australia, New Zealand	Signed 28 March 1980; in force 1 January 1983
AP (*currently known as* CAN)	Andean Pact *known since 1996 as the* Andean Community of Nations (Comunidad Andina de Naciones)	Bolivia, Columbia, Ecuador, Peru, Venezuela	Signed 26 May 1969; in force 16 October 1969 Official codified text of the CAN signed 25 June 2003
Armenia–Kazakhstan FTA	Armenia–Kazakhstan Free Trade Agreement	Armenia, Kazakhstan	Signed 2 September 1999; in force 25 December 2001
ASEAN–China Framework Agreement	Framework Agreement on Comprehensive Economic Cooperation Between the Association of South East Asian Nations and the People's Republic of China	ASEAN states, China	Signed 4 November 2002; in force 1 July 2003 Agreement on Trade in Goods (ASEAN–China Goods Agreement) signed 29 November 2004; in force 1 January 2005

			Agreement on Dispute Settlement Mechanism (ASEAN–China DSM) signed 29 November 2004; in force 1 January 2005
ASEAN–India Framework Agreement	Framework Agreement on Comprehensive Economic Cooperation Between the Republic of India and the Association of Southeast Asian Nations	ASEAN states, India	Signed 8 October 2003; in force 1 July 2004
ASEAN–Korea Framework Agreement	Framework Agreement on Comprehensive Economic Cooperation Among the Governments of the Member Countries of the Association of Southeast Asian Nations and the Republic of Korea	ASEAN states, South Korea	Signed 13 December 2005; in force 1 July 2006 Agreement on Dispute Settlement Mechanism (ASEAN–Korea DSM) signed 13 December 2005; in force 1 July 2006
AUSFTA	Australia–United States Free Trade Agreement	Australia, United States	Signed 18 May 2004; in force 1 January 2005
Benelux	Benelux Customs Union *later known as the* Benelux Economic Union	Belgium, Luxembourg, Netherlands	Signed 5 September 1944; in force 1 January 1948; Treaty of the Benelux Economic Union signed 3 February 1958; in force 1 November 1960
BFTA	Baltic Free Trade Area	Estonia, Latvia, Lithuania	Signed 13 September 1993; in force 1 April 1994
BLEU	Belgium–Luxemburg Economic Union	Belgium, Luxemburg	Signed 25 July 1921; in force 22 December 1922
Bulgaria–Bosnia and Herzegovina FTA	Bulgaria–Bosnia and Herzegovina Free Trade Agreement	Bulgaria, Bosnia and Herzegovina	Signed 16 October 2003

(3) (*cont.*)

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
CACM	Central American Common Market	Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua	Signed 13 December 1960; in force 3 June 1961 (Guatemala, El Salvador, Nicaragua), 27 April 1962 (Honduras), 23 September 1963 (Costa Rica)
CAFTA–DR–US	Central America–Dominican Republic–United States Free Trade Agreement	Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, United States	Signed 5 August 2004; in force 1 March 2006 (El Salvador, United States), 1 April 2006 (Honduras, Nicaragua), 1 July 2006 (Guatemala), 1 March 2007 (Dominican Republic)
Canada–Chile FTA	Canada–Chile Free Trade Agreement	Canada, Chile	Signed 5 December 1996; in force 5 July 1997
Canada–Costa Rica FTA	Canada–Costa Rica Free Trade Agreement	Canada, Costa Rica	Signed 23 April 2001; in force 1 November 2002 Canada–Costa Rica Agreement on Environmental Cooperation (CCRAEC) signed 23 April 2001; in force 1 November 2002 Canada–Costa Rica Agreement on Labour Cooperation (CCRALC) signed 23 April 2001; in force 1 November 2002
Canada–Israel FTA	Canada–Israel Free Trade Agreement	Canada, Israel	Signed 31 July 1996; in force 1 January 1997

CARICOM	Caribbean Community and Common Market	Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, St. Lucia, St. Kitts/Nevis/Anguilla, St. Vincent, Trinidad and Tobago	Signed 4 July 1973; in force 1 August 1973
CARIFTA	Caribbean Free Trade Area	Antigua, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, St. Kitts/Nevis/Anguilla, St. Vincent, Trinidad and Tobago	Signed 15 December 1965; in force 1 May 1968
CARICOM–Costa Rica FTA	CARICOM–Costa Rica Free Trade Agreement	CARICOM states, Costa Rica	Signed 9 March 2004; in force 15 November 2005 (Costa Rica, Trinidad and Tobago), 30 April 2006 (Costa Rica, Guyana), 1 August 2006 (Costa Rica, Barbados)
CARICOM–DR FTA	CARICOM–Dominican Republic Free Trade Agreement	CARICOM states, Dominican Republic	Signed 22 August 1998; in force 1 December 2001 (Trinidad and Tobago, Jamaica, Barbados), 5 February 2002 (Dominican Republic), 6 October 2004 (Guyana), August 2005 (Suriname)
CEAO/WAEC	West African Economic Community (Communauté Économique de l'Afrique de l'Ouest)	Benin (*then* Dahomey), Burkino Faso (*then* Upper Volta), Cote d'Ivoire, Mali, Mauritania, Niger, Senegal	Signed 3 June 1972; in force 1 January 1974
CEEAC/ECCAS	Economic Community of Central African States (Communauté	Angola, Burundi, Cameroon, Central African Republic, Chad,	Signed 18 October 1983; in force 18 December 1984

(3) (*cont.*)

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
	Économique des États d'Afrique Centrale)	Democratic Republic of Congo, Republic of Congo, Equatorial Guinea, Gabon, Rwanda, São Tomé and Príncipe	
CEFTA	Central European Free Trade Agreement	*Parties to the original agreement*: Bulgaria, Croatia, Czech Republic, Hungary, Poland, Republic of Macedonia, Romania, Slovak Republic, Slovenia *Parties to the new enlarged agreement*: Albania, Bosnia and Herzegovina, Croatia, Republic of Macedonia, Moldova, Montenegro, Serbia, UNMIK (on behalf of Kosovo)	Original agreement signed 21 December 1992; in force 1 March 1993; New enlarged agreement signed 19 December 2006; in force 26 July 2007 (Albania, Kosovo, Macedonia, Moldova, Montenegro), 22 August 2007 (Croatia)
CEMAC	Central African Economic and Monetary Community/Economic and Monetary Community of Central Africa (Communauté Économique et Monétaire de l'Afrique Centrale)	Cameroon, Central African Republic, Chad, Republic of Congo, Equatorial Guinea, Gabon	Signed 16 March 1994; in force June 1999
Central America–Chile FTA	Central America–Chile Free Trade Agreement	Chile, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua	Signed 18 November 1999 (Chile–Costa Rica; El Salvador–Chile), 20 November 2000 (Costa Rica–El

			Salvador); in force 14 November 2002 (Chile–Costa Rica), 3 June 2002 (El Salvador–Chile; Costa Rica–El Salvador)
Central America–Panama FTA	Central America–Panama Free Trade Agreement	Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, Panama	Signed 6 March 2002 (El Salvador and Panama), 15 June 2007 (Honduras and Panama); in force 11 April 2003 (El Salvador and Panama)
CEPGL	Economic Community of the Great Lakes Countries (Communauté Économique des Pays des Grands Lacs)	Burundi, Democratic Republic of the Congo, Rwanda	Established 20 September 1976
Chile–China FTA	Chile–China Free Trade Agreement	Chile, China	Signed 18 November 2005; in force 1 October 2006
China–Hong Kong CEPA	China–Hong Kong Closer Economic Partnership Agreement	China, Hong Kong SAR	Signed 29 June 2003; in force 1 January 2004
China–Macao CEPA	China–Macao Closer Economic Partnership Agreement	China, Macao SAR	Signed 17 October 2003; in force 1 January 2004
China–Pakistan FTA	China–Pakistan Free Trade Agreement	China, Pakistan	Signed 24 November 2006; in force 1 July 2007
Cobden–Chevalier Treaty	Cobden–Chevalier Treaty	France, United Kingdom	Signed 23 January 1860
COMESA	Common Market for Eastern and Southern Africa	Angola, Burundi, Comoros, Democratic Republic of Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia, Zimbabwe	Signed 5 November 1993; in force 8? Free Trade Area established on 31 October 2000

(3) (*cont.*)

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
Cotonou Agreement	ACP–EU Cotonou Partnership Agreement	ACP countries, European Union	Signed 23 June 2000; in force 1 April 2003; revised agreement signed 25 June 2005
Croatia–Albania FTA	Croatia–Albania Free Trade Agreement	Albania, Croatia	Signed 27 September 2002; in force 1 June 2003
CUSFTA	Canada–United States Free Trade Agreement	Canada, United States	Signed 2 January 1988; in force 1 January 1989
Deutscher Zollverein	Deutscher Zollverein (German Customs Union)	Majority of German Confederation states	Signed 22 March 1833; in force 1 January 1834
EAC	East African Community	Kenya, Tanzania, Uganda *Parties to the re-established treaty*: Burundi, Kenya, Rwanda, Tanzania, Uganda	Originally established 6 June 1967; Abolished 1 July 1977 Re-established 30 November 1999; in force 7 July 2000
EAC Customs Union	East African Community Customs Union	Burundi, Kenya, Rwanda, Tanzania, Uganda	Signed 2 March 2004; in force 1 January 2005
ECCM	East Caribbean Common Market	Antigua and Barbuda, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia, St. Vincent	Established 11 June 1968
ECOWAS	Economic Community of West African States	Benin, Burkina Faso, Cape Verde, Cote d'Ivoire, Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, Togolese	Signed 28 May 1975; in force 20 June 1975

EEA	European Economic Area	EFTA states (except Switzerland), European Union	Signed 2 May 1992; in force 1 January 1994
EFTA	European Free Trade Association	Iceland, Liechtenstein, Norway, Switzerland	Stockholm Convention: signed 4 January 1960, in force 3 May 1960; Vaduz Convention (amending the Stockholm Convention): signed 21 June 2001; in force 1 June 2002
EFTA–Chile FTA	EFTA–Chile Free Trade Agreement	Chile, EFTA states	Signed 26 June 2003; in force 1 December 2004
EFTA–Croatia FTA	EFTA–Croatia Free Trade Agreement	Croatia, EFTA states	Signed 21 June 2001; in force 1 April 2002
EFTA–Israel FTA	EFTA–Israel Free Trade Agreement	EFTA states, Israel	Signed 17 September 1992; in force 1 January 1993
EFTA–Jordan FTA	EFTA–Jordan Free Trade Agreement	EFTA states, Jordan	Signed 21 June 2001; in force 1 September 2002
EFTA–Korea FTA	EFTA–Korea Free Trade Agreement	EFTA States, Korea	Signed 15 December 2005; in force 1 September 2006
EFTA–Lebanon FTA	EFTA–Lebanon Free Trade Agreement	EFTA states, Lebanon	Signed 24 June 2004; in force 1 January 2007
EFTA–Macedonia FTA	EFTA–Macedonia Free Trade Agreement	EFTA states, Macedonia	Signed 19 June 2000; in force 1 May 2002
EFTA–Mexico FTA	EFTA–Mexico Free Trade Agreement	EFTA states, Mexico	Signed 27 November 2000; in force 1 July 2001
EFTA–Morocco FTA	EFTA–Morocco Free Trade Agreement	EFTA states, Morocco	Signed 19 June 1997; in force 1 December 1999
EFTA–Palestinian Authority FTA	EFTA–Palestinian Authority Free Trade Agreement	EFTA states, Palestinian Authority	Signed 30 November 1998; in force 1 July 1999
EFTA–SACU FTA	EFTA–SACU Free Trade Agreement	EFTA states, SACU states	Signed 26 June 2006; not yet in force
EFTA–Singapore FTA	EFTA–Singapore Free Trade Agreement	EFTA states, Singapore	Signed 26 June 2002; in force 1 January 2003

(3) (*cont.*)

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
EFTA–Tunisia FTA	EFTA–Tunisia Free Trade Agreement	EFTA states, Tunisia	Signed 17 December 2004; in force 1 June 2005
EFTA–Turkey FTA	EFTA–Turkey Free Trade Agreement	EFTA states, Turkey	Signed 10 December 1991; in force 1 April 1992
EU/EC/EEC/ European Treaty	Treaty of the European Union/Treaty Establishing the European Communities	Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom	EEC (Treaty of Rome): signed 25 March 1957; in force 25 March 1957 EU (Maastricht Treaty): signed 7 February 1992; in force 1 November 1993 EU Enlargement (25): accession 1 May 2004 EU Enlargement (27): accession 1 January 2007
EU–Algeria AA	European Union–Algeria Association Agreement	European Union, Algeria	Signed 22 April 2002; in force 1 September 2005
EU–Chile AA	European Union–Chile Association Agreement	Chile, European Union	Signed 18 November 2002; in force 1 March 2005
EU–Croatia SAA	European Union–Croatia Stabilisation and Association Agreement	European Union, Croatia	Signed 29 October 2001; in force 1 February 2005
EU–Egypt AA	European Union–Egypt Association Agreement	Egypt, European Union	Signed 25 June 2001; in force 1 June 2004
EU–FYROM SAA	European Union–Former Yugoslavia Republic of Macedonia Stabilisation and Association Agreement	European Union, FYROM	Signed 9 April 2001; in force 1 April 2004

EU–Israel AA	European Union–Israel Association Agreement	European Union, Israel	Signed 20 November 1995; in force 1 June 2000
EU–Jordan AA	European Union–Jordan Association Agreement	European Union, Jordan	Signed 24 November 1997; in force 1 May 2002
EU–Lebanon AA	European Union–Lebanon Association Agreement	European Union, Lebanon	Signed 17 June 2002; in force 1 April 2006
EU–MERCOSUR Framework Agreement	European Union–MERCOSUR Interregional Framework Cooperation Agreement	European Union, MERCOSUR countries	Signed 15 December 1995; in force 1 July 1999
EU–Mexico FTA	European Union–Mexico Economic Partnership, Political Co-ordination and Co-operation Agreement	European Union, Mexico	Signed 8 December 1997; in force 1 October 2000
EU–Morocco AA	European Union–Morocco Association Agreement	European Union, Morocco	Signed 26 February 1996; in force 1 March 2000
EU–Palestinian Authority Interim AA	European Union–Palestinian Authority Interim Association Agreement	European Union, Palestinian Authority	Signed 24 February 1997; in force 1 July 1997
EU–SA TDCA	European Union–South Africa Trade, Development and Co-operation Agreement	European Union, South Africa	Signed 11 October 1999; in force 1 May 2004
EU–Syria AA	EU–Syria Association Agreement	European Union, Syria	Initialled 19 October 2004; yet to be signed
EU–Tunisia AA	European Union–Tunisia Association Agreement	European Union, Tunisia	Signed 17 July 1995; in force 1 March 1998
Faroe Islands–Norway FTA	Faroe Islands–Norway Free Trade Agreement	Faroe Islands, Norway	In force 1 July 1993
FTAA	Free Trade Area of the Americas	Antigua and Barbuda, Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Dominica,	Ministerial Declaration of Miami, 8th Ministerial Meeting, adopted 20 November 2003

(3) (*cont.*)

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
		Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Trinidad and Tobago, United States, Uruguay, Venezuela	
G–3 FTA	Group of Three (G–3) Free Trade Agreement *now known as the* Mexico–Colombia Free Trade Agreement *after Venezuela's withdrawal 22 May 2006*	Columbia, Mexico, Venezuela	Signed 13 June 1994; in force 1 January 1995
GAFTA	Greater Arab Free Trade Area	Jordan, Bahrain, United Arab Emirates, Tunisia, Saudi Arabia, Syria, Iraq, Oman, Qatar, Kuwait, Lebanon, Libya, Egypt, Morocco, Sudan, Yemen, Palestine	Signed 19 February 1997; in force 1 January 1998
Georgia–Armenia FTA	Georgia–Armenia Free Trade Agreement	Armenia, Georgia	Signed 14 August 1995; in force 11 November 1998
India–Nepal FTA	India–Nepal Trade Treaty	India, Nepal	Signed 1951; last renewal 6 March 2002

India–Singapore CECA	India–Singapore Comprehensive Economic Co-operation Agreement	India, Singapore	Signed 29 June 2005; in force 1 August 2005
India–Sri Lanka FTA	India–Sri Lanka Free Trade Agreement	India, Sri Lanka	Signed 28 December 1998; in force 1 March 2000
Japan–Malaysia EPA	Japan–Malaysia Economic Partnership Agreement	Japan, Malaysia	Signed 13 December 2005; in force 13 July 2006
Japan–Mexico EPA	Japan–Mexico Economic Partnership Agreement	Japan, Mexico	Signed 17 September 2004; in force 1 April 2005
Japan–Philippines EPA	Japan–Philippines Economic Partnership Agreement	Japan, Philippines	Signed 8 September 2006; not yet in force
Japan–Singapore EPA	Japan–Singapore New-Age Economic Partnership Agreement	Japan, Singapore	Signed 13 January 2002; in force 30 November 2002
Japan–Thailand EPA	Japan–Thailand Economic Partnership Agreement	Japan, Thailand	Signed 3 April 2007; in force 1 November 2007
Korea–Chile FTA	Korea–Chile Free Trade Agreement	Chile, South Korea	Signed 15 February 2003; in force 1 April 2004
Korea–Singapore FTA	Korea–Singapore Free Trade Agreement	Singapore, South Korea	Signed 4 August 2005; in force 2 March 2006
KORUS FTA	Korea–United States Free Trade Agreement	South Korea, United States	Signed 30 June 2007; not yet in force
Kyrgyzstan–Moldova FTA	Kyrgyzstan–Moldova Free Trade Agreement	Kyrgyzstan, Moldova	Signed 26 May 1995; in force 21 November 1996
LAFTA	Latin American Free Trade Association	Argentina, Bolivia, Brazil, Chile, Columbia, Ecuador, Mexico, Paraguay, Peru, Uruguay, Venezuela	Signed 18 February 1960; in force 2 June 1961
Lomé Convention	Lomé Convention	ACP countries, European Union	First Lomé Convention: signed 28 February 1975; in force 1 April 1976

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
			Second Lomé Convention: signed 31 October 1979; in force 1 January 1981 Third Lomé Convention: signed 8 December 1984; in force 1 May 1986 Fourth Lomé Convention: signed 15 December 1989; in force 1 March 1990
MERCOSUR	Common Market of the Southern Cone (Mercado Común del Sur)	Argentina, Brazil, Paraguay, Uruguay	Signed 26 March 1991; in force 29 November 1991
Mexico–Bolivia FTA	Mexico–Bolivia Free Trade Agreement	Bolivia, Mexico	Signed 10 September 1994; in force 1 January 1995
Mexico–Chile FTA	Mexico–Chile Free Trade Agreement	Chile, Mexico	Signed 1 October 1998; in force 1 August 1999
Mexico–Costa Rica FTA	Mexico–Costa Rica Free Trade Agreement	Costa Rica, Mexico	Signed 5 April 1994; in force 1 January 1995
Mexico–Israel FTA	Mexico–Israel Free Trade Agreement	Mexico, Israel	Signed 10 April 2000; in force 10 July 2000
Mexico–Nicaragua FTA	Mexico–Nicaragua Free Trade Agreement	Mexico, Nicaragua	Signed 18 December 1997; in force 1 July 1998
Mexico–Northern Triangle FTA	Mexico–Northern Triangle (El Salvador–Guatemala–Honduras) Free Trade Agreement	El Salvador, Guatemala, Honduras, Mexico	Signed 29 June 2000; in force 14 March 2001 (Mexico), 15 March 2001 (El Salvador, Guatemala), 1 June 2001 (Honduras)

Mexico–Uruguay FTA	Mexico–Uruguay Free Trade Agreement	Mexico, Uruguay	Signed 15 November 2003; in force 15 July 2004
Mexico–Venezuela FTA	Mexico–Venezuela Free Trade Agreement	Mexico, Venezuela	Signed 22 May 2006; in force 19 November 2006
MRU	Mano River Union	Guinea, Liberia, Sierra Leone	Established 3 October 1973
NAFTA	North American Free Trade Agreement	Canada, Mexico, United States	Signed 17 December 1992; in force 1 January 1994 North American Agreement on Environmental Co-operation (NAAEC) signed 14 September 1993; in force 1 January 1994 North American Agreement on Labor Cooperation (NAALC) signed 14 September 1993; in force 1 January 1994
NZ–Australia FTA	New Zealand–Australia Free Trade Agreement	Australia, New Zealand	Signed 31 August 1965; in force 1 January 1966
NZ–Singapore CEPA	New Zealand–Singapore Closer Economic Partnership Agreement	New Zealand, Singapore	Signed 14 November 2000; in force 1 January 2001
NZ–Thailand CEPA	New Zealand–Thailand Closer Economic Partnership Agreement	New Zealand, Thailand	Signed 19 April 2005; in force 1 July 2005
Panama–Taiwan FTA	Panama–Taiwan Free Trade Agreement	Panama, Taiwan	Signed 21 August 2003; in force 1 January 2004
PTA	Preferential Trade Area for Eastern and Southern African States	Angola, Burundi, Comoros, Djibouti, Eritrea, Ethiopia, Kenya, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Rwanda, Seychelles, Somalia, Sudan, Swaziland, Tanzania, Uganda, Zambia, Zimbabwe	Signed 21 December 1981; in force 30 September 1982

(3) (*cont.*)

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
SACU	Southern African Customs Union	Botswana, Lesotho, Namibia, South Africa, Swaziland	Signed 11 December 1969; in force 1 March 1970
SADC	Southern African Development Community	Angola, Botswana, Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia, Zimbabwe	Signed 17 August 1992; in force 30 September 1993
SADCC	Southern African Development Co-ordination Conference	Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia, Zimbabwe	Signed 1 April 1980; in force 20 July 1981
Singapore–Australia FTA	Singapore–Australia Free Trade Agreement	Australia, Singapore	Signed 17 February 2003; in force 28 July 2003
Singapore–Jordan FTA	Singapore–Jordan Free Trade Agreement	Jordan, Singapore	Signed 16 May 2004; in force 22 August 2005
Thailand–Australia FTA	Thailand–Australia Free Trade Agreement	Australia, Thailand	Signed 5 July 2004; in force 1 January 2005
Trans-Pacific SEP (*also referred to as* P4 Agreement)	Trans-Pacific Strategic Economic Partnership	Brunei, Chile, New Zealand, Singapore	Signed 18 July 2005 (Chile, New Zealand, Singapore), 2 August 2005 (Brunei); in force 28 May 2006 (New Zealand, Singapore), 12 July 2006 (Brunei), 8 November 2006 (Chile)
Treaty of Balta Liman	Treaty of Balta Liman	Ottoman Empire, United Kingdom of Great Britain and Ireland	Signed 16 August 1838

Turkey–Morocco FTA	Turkey–Morocco Free Trade Agreement	Morocco, Turkey	Signed 7 April 2004; in force 1 January 2006
UDAO/WACU	West African Customs Union (Union Douaniere des États de l'Afrique Occidentale)	Benin (*then* Dahomey), Burkina Faso (*then* Upper Volta), Cote d'Ivoire, Mali, Mauritania, Niger, Senegal	Established 9 June 1959
UDE/ECU	Equatorial Customs Union (Union Douanière Equatoriale)	Cameroon, Central African Republic, Chad, Republic of the Congo, Gabon	Established 23 June 1959
UDEAC/CACEU	Central African Customs and Economic Union/Customs and Economic Union of Central Africa (Union Douanière et Économique de l'Afrique Centrale)	Cameroon, Central African Republic, Chad, Republic of Congo, Equatorial Guinea, Gabon	Signed 8 December 1964; in force 1 January 1966
UDEAO/CUWAS	Customs Union of West African States/West African Customs and Economic Union (Union Douanière et Économique de l'Afrique de l'Ouest)	Benin (*then* Dahomey), Burkino Faso, Cote d'Ivoire, Mali, Mauritania, Niger, Senegal	Established 3 June 1966
UEMOA/WAEMU	West African Economic and Monetary Union/Economic and Monetary Union of West Africa (Union Économique et Monétaire Ouest-Africaine)	Benin, Burkina Faso, Cote d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal, Togo	Established 10 January 1994
US–Andean TPA	United States–Andean Countries Trade Promotion Agreement	Bolivia, Colombia, Ecuador, Peru, United States	Signed 12 April 2006 (Peru, United States), 22 November 2006 (Colombia, United States); not yet in force
US–Bahrain FTA	United States–Bahrain Free Trade Agreement	Bahrain, United States	Signed 14 September 2004; in force 1 January 2006

(3) (*cont.*)

Short Title	Long Title	Current Parties (or membership immediately prior to extinction) (unless otherwise indicated)	Status
US–Chile FTA	United States–Chile Free Trade Agreement	Chile, United States	Signed 6 June 2003; in force 1 January 2004
US–Columbia TPA	United States–Colombia Trade Promotion Agreement	Colombia, United States	Signed 22 November 2006; not yet in force
US–Israel FTA	United States–Israel Free Trade Agreement	Israel, United States	Signed 22 April 1985; in force 1 September 1985
US–Jordan FTA	United States–Jordan Free Trade Agreement	Jordan, United States	Signed 24 October 2000; in force 17 December 2001
US–Morocco FTA	United States–Morocco Free Trade Agreement	Morocco, United States	Signed 15 June 2004; in force 1 January 2006
US–Oman FTA	United States–Oman Free Trade Agreement	Oman, United States	Signed 19 January 2006; not yet in force
US–Panama TPA	United States–Panama Trade Promotion Agreement	Panama, United States	Signed 28 June 2007; not yet in force
US–Peru TPA	United States–Peru Trade Promotion Agreement	Peru, United States	Signed 4 December 2006; not yet in force
US–Singapore FTA	United States–Singapore Free Trade Agreement	Singapore, United States	Signed 6 May 2003; in force 1 January 2004
US–South Korea FTA	United States–South Korea Free Trade Agreement	South Korea, United States	Signed 30 June 2007; not yet in force

(4) *Bilateral Investment Treaties*

Short Title	Long Title	Parties	Status
AIA Framework Agreement	Framework Agreement on the ASEAN Investment Area (AIA)	Brunei, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam	Signed 7 October 1998
CCIA Investment Framework Agreement	Investment Framework Agreement for the COMESA Common Investment Area	Angola, Burundi, Comoros, Democratic Republic of Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia, Zimbabwe	Draft as of 2003
Germany–China BIT	Agreement between the People's Republic of China and the Federal Republic of Germany on the Encouragement and Reciprocal Protection of Investments	China, Germany	Signed 1 December 2003
Germany–Ethiopia BIT	Treaty between the Federal Republic of Germany and the Empire of Ethiopia	Ethiopia, Germany	Signed 21 April 1964
Italy–Jordan BIT	Agreement between the Government of the Hashemite Kingdom of Jordan and the	Italy, Jordan	Signed 21 July 1996

(4) (*cont.*)

Short Title	Long Title	Parties	Status
	Government of the Italian Republic on the Promotion and Protection of Investments		
Spain–Argentina BIT	Agreement on the Reciprocal Promotion and Protection of Investments signed by the Kingdom of Spain and the Argentine Republic	Argentina, Spain	Signed 3 October 1991
Spain–Mexico BIT	Agreement on the Reciprocal Promotion and Protection of Investments signed by the Kingdom of Spain and the United Mexican States	Mexico, Spain	In force 18 December 1996
Sweden–Laos BIT	Agreement between the Government of the Kingdom of Sweden and the Government of the Laos People's Democratic on the Promotion and Reciprocal Protection of Investments	Laos (Lao PDR), Sweden	Signed 29 August 1996

Sweden–Philippines BIT	Agreement between the Government of the Republic of the Philippines and the Government of the Kingdom of Sweden on the Promotion and Reciprocal Protection of Investments	Philippines, Sweden	Signed 18 August 1993
Switzerland–Iran BIT	Agreement between the Swiss Confederation and the Islamic Republic of Iran on the Promotion and Reciprocal Protection of Investments	Iran, Switzerland	Signed 8 March 1998
Switzerland–Jordan BIT	Agreement between the Hashemite Kingdom of Jordan and the Swiss Confederation on the Promotion and Reciprocal Protection of Investments	Jordan, Switzerland	Signed 11 November 1976
United States–Argentina BIT	Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment	Argentina, United States	Signed 14 November 1991; in force 20 October 1994

(5) *Wine and Spirits Agreements*

Short Title	Full Title	Parties	Status
EC–Australia Wine Agreement	Agreement between Australia and the European Community on Trade in Wine	Australia, European Union	Signed 26 January 1994 (at Brussels) and 31 January 1994 (at Canberra); in force 1 March 1994
EC–Canada Wine and Spirits Agreement	Agreement between the European Community and Canada on Trade in Wines and Spirit Drinks	Canada, European Union	Signed 16 September 2003; in force 1 June 2004
EC–Chile Spirits Agreement	Agreement establishing an association between the European Community and its Member States, of the one part, and the Republic of Chile, of the other part (Annex VI: Agreement on Trade in Spirit Drinks and Aromatised Drinks)	Chile, European Union	Signed 14 February 2006
EC–Chile Wine Agreement	Agreement establishing an association between the European Community and its Member States, of the one part, and the Republic of Chile, of the other part (Annex V: Agreement on Trade in Wines)	Chile, European Union	Signed 14 February 2006

EC–Mexico Spirits Agreement	Agreement between the European Community and the United Mexican States on the Mutual Recognition and Protection of Designations for Spirit Drinks	European Union, Mexico	Signed 27 May 1997
EC–South Africa Spirits Agreement	Agreement between the European Community and the Republic of South Africa on Trade in Spirits	European Union, South Africa	Signed 28 January 2002
EC–South Africa Wine Agreement	Agreement between the European Community and the Republic of South Africa on Trade in Wines	European Union, South Africa	Signed 28 January 2002
EC–Switzerland Spirits Agreement	Agreement between the European Community and the Swiss Confederation on Trade in Agricultural Products (Annex 8)	European Union, Switzerland	Signed 21 June 1999
EC–Switzerland Wine Agreement	Agreement between the European Community and the Swiss Confederation on Trade in Agricultural Products (Annex 7)	European Union, Switzerland	Signed 21 June 1999
EC–US Wine Agreement	Agreement between the European Community and the United States of America on Trade in Wine	European Union, United States	Signed 10 March 2006

TABLE OF ABBREVIATIONS

ACP	African–Caribbean–Pacific
AMS	Aggregate Measurement of Support
ASEAN	Association of Southeast Asian Nations
APEC	Asia-Pacific Economic Co-operation
BIT	Bilateral Investment Treaty
BTA	Bilateral Trade Agreement
CAFTA	Central America Free Trade Agreement
CACM	Central American Common Market
CAP	Common Agriculture Policy
CARICOM	Caribbean Common Market
CCRAEC	Canada–Costa Rica Agreement on Environmental Co-operation
CCRALC	Canada–Costa Rica Agreement on Labour Co-operation
CEECs	Central and Eastern European Countries
CEFTA	Central European Free Trade Area
CEPT	Common Effective Preferential Tariff
CIS	Commonwealth of Independent States
CU	Customs Union
CRTA	Committee on Regional Trade Agreements
DDA	Doha Development Agenda
DSB	Dispute Settlement Body
DSM	Dispute Settlement Mechanism
DSU	Understanding on Rules and Procedures Governing the Settlement of Disputes
EBA	Everything But Arms
EC	European Communities
ECHR	European Court of Human Rights
ECJ	European Court of Justice
ECLA	Economic Commission for Latin America
ECOSOC	The Economic and Social Council of the United Nations
EEC	European Economic Community
EFTA	European Free Trade Association

EU	European Union
EC Treaty/EU Treaty	Treaty of the European Union/Treaty Establishing the European Communities
FNC	Friendship, Navigation and Commerce
FTA	Free Trade Agreement
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GCC	Gulf Cooperation Council
GDP	Gross domestic product
GI	Geographical indications
GSP	Generalised system of preferences
Havana Charter	Havana Charter for an International Trade Organisation
ICJ	International Court of Justice
ICJ Statute	Statute of the International Court of Justice
ICSID	International Centre for Settlement of Investment Disputes
ICTSD	International Centre for Trade and Sustainable Development
ILC	International Law Commission
ILO	International Labour Organization
IMF	International Monetary Fund
IP	Intellectual Property
ISDS	Investor–State Dispute Settlement
ITO	International Trade Organization
MERCOSUR	Common Market of the Southern Cone
MEA	Multilateral Environmental Agreement
MFN	Most favoured nation
NAAEC	North American agreement on Environmental Co-operation
NAALC	North American Agreement on Labor Co-operation
NAFTA	North American Free Trade Agreement
NGO	Non-Governmental Organisation
NT	National Treatment
OECD	Organisation of Economic Co-operation and Development
OECS	Organisation of East Caribbean States
OPEC	Organisation of Petroleum-Exporting Countries
PCIJ	Permanent Court of International Justice
PTA	Preferential Trade Agreement
ROO	Rules of origin
RTA	Regional Trade Agreement
SACU	Southern African Customs Union

SCM	Subsidies and Countervailing Measures
SPS	Sanitary and Phytosanitary Agreement
TBT	Technical Barriers to Trade
TIFA	Trade and Investment Framework Agreement
TPA	Trade Promotion Agreement
TRIMs	Agreement on Trade-Related Investment Measures
TRIPS	Agreement on Trade-Related Aspects of Intellectual Property Rights
TRQ	Tariff-rate quotas
UK	United Kingdom
UN	United Nations
UN Charter	Charter of the United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
UNESCO	United Nations Educational, Scientific and Cultural Organisation
US	United States of America
USSR	Union of Soviet Socialist Republics/Soviet Union
USTR	United States Trade Representative
Vienna Convention	Vienna Convention on the Law of Treaties of 1969
WIPO	World Intellectual Property Organisation
Working Procedures	Working Procedures for Appellate Review
World Bank	International Bank for Reconstruction and Development
WTO	World Trade Organisation
WTO Agreement	Marrakesh Agreement Establishing the World Trade Organisation

PART I

Introduction

1

Introduction

SIMON LESTER AND BRYAN MERCURIO

The modern history of the world trading system, and in particular international trade agreements, is evidenced by shifts among bilateralism, regionalism and multilateralism. In the late nineteenth century and early twentieth century, bilateralism was clearly dominant. Trade agreements were negotiated on a bilateral basis between individual countries. In the 1860s and 1870s, England initiated much of this activity, pushing its trading partners to sign trade agreements that reciprocally lowered tariff rates. In the 1930s, it was the United States (US) that made a big push in this area, through its Reciprocal Trade Agreements programme, although a number of other countries were also active in negotiating bilateral agreements to lower tariff rates.

However, immediately after World War II, multilateralism and regionalism replaced bilateralism as the dominant approach. From the late 1940s to the mid-1990s, multilateralism grew in strength as more and more nations joined the GATT or its successor, the WTO. The GATT, which began with 23 countries, unquestionably came to dominate the world trading scene. It did not, however, completely replace regional and bilateral trade agreements. Regionalism remained a competing model, as nations in Europe, North America, South America and elsewhere all formed trading blocs during this period. East Asia was the only region to eschew regionalism, while Western Europe was the clear leader in terms of both the timing and the scope of its economic integration, with other regions following behind. Bilateralism, on the other hand, diminished considerably during this period. Such agreements were extremely rare, and where they did exist could usually be explained mostly by political, rather than economic, factors.

In recent years, though, bilateralism has returned with a vengeance. The initial return to bilateralism can be traced to the breakup of the Soviet Union and collapse of Communism in the early 1990s. The newly formed nations, along with several Eastern European economies in transition from a centrally planned to a market-based economy, led a mini-revival of bilateralism in the mid- to late 1990s. Bilateralism, however, only significantly gained momentum following the failed WTO negotiations at the 1999 Seattle Ministerial Conference. Prior to 1999, it was rare for the major trading powers to negotiate and sign bilateral trade agreements. Following the failed Ministerial, all major trading nations (including the East Asian nations) almost immediately launched multiple negotiations. A large number of

such agreements have now been negotiated and signed, and many more are currently being negotiated. The rapid increase in the total number of agreements has created a competitive process among nations, with all of the major trading powers pushing hard to conclude these agreements so as not to lose particular markets to their competitors.

In addition to bilateral agreements, there are also a growing number of what could be termed 'loose' regional trade agreements. These are concluded among several countries in the same 'region', with the term region more loosely defined than in previous eras. These agreements are, in essence, plurilateral agreements among countries which may or may not be in somewhat close proximity to each other, but do not necessarily include all countries from that area. For example, the North American Free Trade Agreement (NAFTA), a more traditional RTA, was signed in 1993 by Canada, the US and Mexico: three contiguous countries of North America. By contrast, in 2006 the Central America–Dominican Republic–United States Free Trade Agreement (CAFTA–DR–US) was signed by the US, a few Central American countries, and the Dominican Republic. All are in the same general region, but there are many other countries within that region which were not included. On the other hand, the Trans-Pacific Strategic Economic Partnership Agreement (P4) between Brunei, Chile, New Zealand and Singapore cannot be said to even remotely resemble nations in close proximity to one another (although admittedly all members are linked by the Pacific Ocean).

The result of the proliferation of these agreements is that today's international trade rules now consist of a number of instruments. At the forefront, there is the multilateral WTO Agreement, which includes 151 countries or customs territories. In addition, there are the traditional regional trading blocs, each with their own agreements, some of which provide for deep integration or customs unions among the member countries. Then, there is the complex web of bilateral trade agreements between individual countries. Finally, there are a growing number of 'loose' regional agreements. All of these agreements – over 300 in total – exist together, creating a mish-mash of overlapping, supporting, and possibly conflicting, obligations.

Perhaps even more importantly than the sheer quantity of trade agreements are their scope and coverage. While the nineteenth and early twentieth century bilateral agreements were often narrowly focused on reducing tariffs, the more recent ones contain obligations that are wide-ranging and controversial, from investment provisions to intellectual property rights affecting access to medicines to protections for labour/human rights and the environment. While the full impact that these agreements will have on domestic policy-making is uncertain, it is clear that a number of agreements are going beyond the coverage of the WTO as well as the regional and bilateral agreements negotiated prior to 1999 and reaching a new level of international policy-making.

Before turning to the structure of this volume, it is worth noting an important definitional point: What should this recent wave of agreements be called? Above, we

have referred to 'bilateral trade agreements' and 'loose' 'regional trade agreements'. Most often, these agreements are referred to as 'free trade' agreements, and, in fact, many of the agreements have 'free trade' in the title (although others use more general terms such as 'economic partnership' agreements). Some commentators have also taken to referring to the collection of bilateral and regional trade agreements as 'preferential trade agreements'.

The term 'free trade agreements' (FTAs) has advantages in that it is the most commonly used term and is the term used in many agreements. On the negative side, it excludes customs unions, which these agreements sometimes are, and it perhaps puts the agreements in an overly positive, not to mention inaccurate, light. For instance, it could be argued that favouring certain countries in trade relations, as these agreements do, is not 'free trade' at all, but rather discriminatory trade. Moreover, the vast majority of these agreements do not actually create 'free' trade between partner countries. For these reasons, the term 'preferential trade agreements' (PTAs) was created. The term PTAs is not used as often, and is not used in any of the agreements themselves. On the other hand, it is a common term for these agreements, and it is arguably more accurate in describing what these agreements do (they establish preferences for some countries over others in trade relations). The term PTAs also has the advantage in that it can include both free trade agreements and customs unions. In a sense, bilateral and regional trade agreements, as we have titled the book, is the most all encompassing and accurate term. But it is wordy, and does not have an acronym that is commonly recognised (i.e., few people will be used to seeing the term BRTA). As a result, we preferred the use of the term PTA throughout this collection, but have given the authors the freedom to vary their terminology as they see fit. We do not intend there to be any negative connotations with the choice or use of any of the terms.

The structure of the book

The spread of PTAs raises a number of interesting questions in terms of politics, international relations, international law, economics and global governance:

- What are the reasons for the recent interest in and growth of these agreements?
- How do the benefits of bilateral trade liberalisation compare with those of multilateral trade liberalisation?
- How do these new agreements relate to existing multilateral and regional trade agreements, and to international law more generally?
- What is the substantive scope of these agreements? That is, what policies do they promote and what obligations do they contain?
- How are these agreements negotiated among the various governments, and what is the role of non-state actors who have an interest in the agreements?

This book attempts to provide some preliminary answers to these questions. We say 'preliminary' because the development of these agreements is still ongoing. The end does not appear to be in sight yet, especially as the Doha Round continues on (and on) with no set timetable for completion. Thus, the analysis offered here is necessarily limited to what has occurred so far.

The book is structured as follows. Parts II and III will put these issues in context by providing some general background on the economics, politics, international relations and international law aspects of PTAs. For instance, Part II contains a chapter by Pravin Krishna of Johns Hopkins University, School of Advanced International Studies, evaluating the economics of PTAs. More specifically, Professor Krishna expands upon existing literature to find that the welfare effects of PTAs are ambiguous at best. The chapter also provides, *inter alia*, an interesting analysis on the design of PTAs with welfare-improving effects. Part II also contains a chapter on the political and international relations considerations of PTAs. Written by Olivier Cattaneo of the International Trade Department at the World Bank, the chapter asks the question 'Why do countries conclude PTAs?' and provides a unique assessment of both the historical and present situation, ultimately concluding that the political economy of PTAs revolves more around politics than economics. The final chapter is a practical analysis of some of the differences between bilateral PTAs and multi-party ones. In the chapter, David Evans of the New Zealand Ministry of Foreign Affairs and Trade, demonstrates how the 'new generation' of plurilateral PTAs are a break from traditional bilateral PTAs and offer some challenging procedural and substantive issues, such as how are such agreements to be negotiated and structured to meet the needs (and ambitions) of all parties.

Part III tries to situate PTAs in the larger context in which they exist. There are two aspects to this: (1) How do PTAs fit with the WTO, which prohibits discrimination among WTO Members but has an exception for free trade agreements and customs unions? and (2) How do PTAs fit within international law more generally? Part III begins with a chapter by Andrew Mitchell of the University of Melbourne, Faculty of Law, and Nicholas Lockhart of the law firm of Sidley Austin, examining the nature of the exception for PTAs under WTO rules. It outlines, in substantial detail, the conditions of the exception and concludes with an assessment of the likelihood of legal challenge to a PTA if it did not meet all of the conditions of the exception. Chapter 6, by Andrew Mitchell and Tania Voon, also of the University of Melbourne, Faculty of Law, provides a comprehensive analysis of the under-explored and often murky relationship of PTAs to international law. More specifically, Mitchell and Voon provide examples of difficult and unsettled issues surrounding the overlap between PTAs and public international law, including the particularly thorny issues of conflicting norms between two treaties/agreements and multiple dispute settlement systems that are capable of hearing the same dispute.

Part IV provides a detailed look at specific subject areas that are part of PTAs. In essence, this part offers a comparison across the various agreements, examining the

scope of the law that is being created in seven important policy areas. First, Timothy Josling of Stanford University, Food Research Institute, analyses the contentious area of agriculture with reference to historical data as well as differences between bilateral and regional PTAs. Next, Federico Ortino of King's College London provides a review of services in the multilateral forum before comprehensively detailing how certain PTAs are creating GATS-Plus obligations. Joshua Meltzer from the Australia Department of Foreign Affairs and Trade then contributes a thorough and detailed chapter on investment and focuses on both the wide-ranging obligations undertaken in the area as well as those areas which have caused much disagreement and dispute. Arwel Davies of Swansea University, Faculty of Law, next provides a chapter on government procurement which illustrates how many agreements are hesitant to move substantially beyond the WTO model. Michael Handler of the University of New South Wales, Faculty of Law and Bryan Mercurio of The Chinese University of Hong Kong, Faculty of Law, provide a chapter on intellectual property which looks at three TRIPS-Plus areas of intellectual property: copyright, geographical indications and patents. Lorand Bartels of Cambridge University then analyses the inclusion of social issues, such as labour, environment and human rights, into PTAs. Finally, Simon Lester of WorldTradeLaw.net and Victoria Donaldson of the WTO Secretariat conclude with a detailed review of various dispute settlement provisions in PTAs, finding a general, but not perfect, correlation to the WTO model set out in the Dispute Settlement Understanding.

The companion volume to this book (to be published later) will be made up of case studies of various PTAs. At this stage, we are not offering a complete set of case studies of all PTAs. Rather, we have tried to select a group that includes a good sampling in terms of countries and regions covered, and also a sampling of agreements that address key issues (such as intellectual property and agriculture). Authored by leading scholars, practitioners and governmental officials, each case study provides a comprehensive review of particular agreements. The first case study, authored by Andrew Mitchell and Tania Voon, is the Australia–United States Free Trade Agreement (AUSFTA). Mauricio Salas, of the law firm Facio & Caňas in San Jose, Costa Rica, next reviews the CAFTA–DR–US. Bradly Condon of the Instituto Tecnológico Autónomo de México (ITAM) then provides a review of the European Union–Mexico Economic Partnership, Political Co-ordination and Co-operation Agreement. The Mexico–Japan Economic Partnership Agreement is then reviewed by Bryan Mercurio before Jason Kearns of the US House of Representatives, Committee on Ways and Means outlines the United States–Morocco Free Trade Agreement. Peter Draper and Nkululeko Khumal, both of the South African Institute of International Affairs, then review the EFTA–SACU before Luz Sosa of the General Directorate for International Economic Affairs (Chile) outlines the China–Chile Free Trade Agreement. The book concludes with a review of the China-ASEAN Free Trade Agreement, authored by Jiangyu Wang of the Chinese University of Hong Kong, Faculty of Law.

In later editions of the book, we plan to supplement this work by providing case studies of additional agreements, eventually compiling a comprehensive resource providing case studies of as many PTAs as is practicable. Such a resource should be useful in a number of ways. For example, each study can serve as an in-depth study of a particular PTA. Moreover, the group of case studies can be used to compare and contrast the coverage of different PTAs, or to examine the PTAs signed by a particular country.

As mentioned above, the expansion of PTAs as a key part of the world trading system is a fairly recent development. As things continue to evolve, we will expand this study through future editions. For the chapters covering specific substantive areas, we will update these to take into account new agreements as they are signed. In addition, as noted, we will add more case studies with each new edition. In this way, we hope this book and its future editions will serve as a comprehensive and essential resource for understanding the role of PTAs in the international trade regime.

PART II

Economics and politics of PTAs

2

The economics of PTAs

PRAVIN KRISHNA*

I. Introduction

Strongly influenced by the perception that restricted commerce and preferences in trade relations had contributed to the economic depression of the 1930s and the subsequent outbreak of war, the discussions leading to the General Agreement on Tariffs and Trade (GATT) in 1947 were driven by the desire to create an international economic order based on a liberal and non-discriminatory multilateral trade system. Enshrined in Article I of the GATT, the principle of non-discrimination (commonly referred to as the most-favoured-nation or MFN clause) precludes member countries from discriminating against imports based upon the country of origin. However, in an important exception to this central prescript, the GATT, through its Article XXIV, permits its members to enter into preferential trade agreements (PTAs), provided these preferences are complete. In so doing, it sanctions the formation of Free Trade Areas (FTAs), whose members are obligated to eliminate internal import barriers, and Customs Unions (CUs), whose members additionally agree on a common external tariff against imports from non-members. Additional derogations to the principle of non-discrimination now include the enabling clause, which allows tariff preferences to be granted to developing countries (in accordance with the generalised system of preferences) and permits preferential trade among developing countries.

Such PTAs are now in vogue. Even as multilateral approaches to trade liberalisation – through negotiations organised by the GATT/WTO – have made substantial progress in reducing international barriers to trade, GATT/WTO-sanctioned PTAs have rapidly increased in number in recent years. Among the more prominent existing PTAs are the North American Free Trade Agreement (NAFTA), the European Economic Community (EEC), both formed under Article XXIV, and the MERCOSUR (the CU between the Argentine Republic, Brazil, Paraguay, and Uruguay), formed under the Enabling Clause. All in all, hundreds of PTAs are

* This chapter draws substantially on my earlier research, particularly my works of 2004 and 2005 (cited below).

currently in existence, with nearly every member country of the WTO belonging to at least one PTA.[1]

That a country liberalising its trade preferentially against select partners is doing something distinct from multilateral liberalisation (where it eliminates tariffs against all imports regardless of country of origin) should be easy to see. What this implies for the liberalising country is a little more difficult to understand. Even a good half century after the economic implications of trade preferences were first articulated by Viner,[2] the differences between preferential and multilateral liberalisation (or free trade areas versus free trade) remain a nuance that most policy analysts (and occasionally even distinguished economists) appear to miss.

It is with a discussion of these issues concerning the distinction between preferential and non-discriminatory trade liberalisation that we begin the analytical section of this chapter, which is intended as a brief and accessible primer on the economics of PTAs. Specifically, Section II develops the classic analysis of Viner and demonstrates the generally ambiguous welfare effects of preferential trade liberalisation. Section III discusses the role geographic proximity ('regionalism') may play in this discussion. Section IV discusses the design of welfare-improving preferential trade agreements. Section V reviews GATT/WTO regulations concerning PTA formation and asks how the existing provisions compare with the welfare improving designs for PTAs described in Section IV. Section VI concludes.

II. Welfare analysis

A. Trade creation and trade diversion

Does preferential trade liberalisation in favour of particular trading partners have the same welfare consequences as non-discriminatory trade liberalisation in favour of all imports? Does a simple proportion of the welfare benefits of non-discriminatory free trade accrue with preferential liberalisation?

A thorough answer to these questions would require the reader to take a deep plunge into the abstruse world of the second-best (whose existence and complexities were, indeed, first discovered and developed by analysts working on the economics of PTAs). But the idea may be introduced in a rudimentary fashion using the following 'textbook' representation of Viner's analysis: Consider the case of two countries, A and B, and the rest of the world W. A is our 'home' country. A produces a good and trades it for the exports of its trading partners B and W. Both B and W are assumed to export the same good and offer it to A at a fixed (but different) price. Initially, imports from B and W are subject to non-discriminatory trade restrictions: tariffs against B and W are equal. Imagine now that A eliminates its tariffs against B while maintaining its tariffs

1 For a listing of all bilateral and regional trade agreements notified to the WTO, see www.worldtradelaw.net/fta/ftadatabase/ftas.asp.

2 Jacob Viner, *The Customs Unions Issue* (New York: Carnegie Endowment for International Peace, 1950).

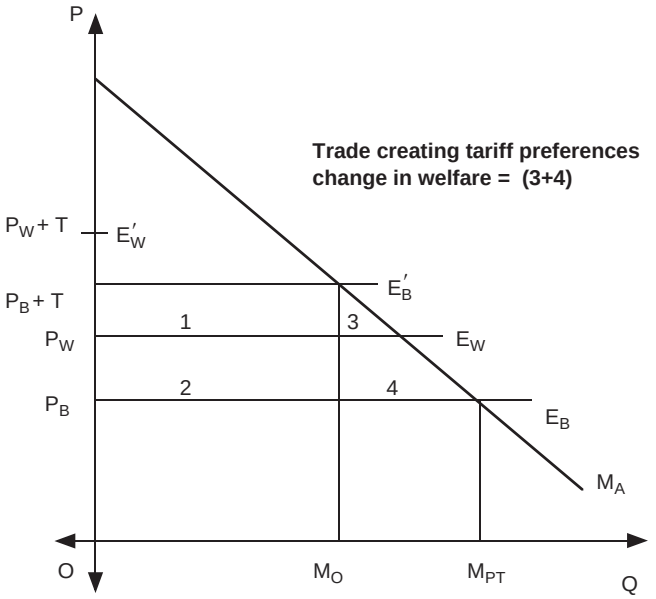


Figure 2.1

against W. This is preferential tariff reduction as opposed to free trade, since the latter would require that tariffs against W be removed as well. It is very tempting to think that this reduction of tariffs against B is a step in the direction of free trade and therefore that this ought to deliver to country A a proportionate fraction of the benefits of complete free trade. But Viner showed that this need not (and generally would not) be the case. Indeed, while a complete move towards free trade would be welfare improving for country A, Viner demonstrated that the tariff preference granted to B through the FTA could in fact worsen A's welfare.

Figures 2.1 and 2.2 illustrate preferential tariff reform as respectively welfare-enhancing and welfare worsening. The y-axes denote price and the x-axes denote quantities. M_A denotes the import demand curve of country A. E_B and E_W denote the price at which countries B and W are willing to supply A's demand; they represent the export supply curves of B and W respectively. In Figure 2.1, B is assumed to be a more efficient supplier of A's import than is W: E_B is drawn below E_W, and its export price P_B is less than W's export price P_W. Let 'T' denote the non-discriminatory per-unit tariff that is applied against B and W. This renders the tariff-inclusive price to importers in A as $P_B + T$ and $P_W + T$ respectively. With this non-discriminatory tariff in place, imports initially equal M_0 and the good is entirely imported from B. Tariff revenues in this initial situation equal the areas (1+2). When tariffs against B are eliminated preferentially, imports rise to M_{PT}. Imports continue to come entirely from B (since the import price from B now, P_B, is lower than the tariff-inclusive

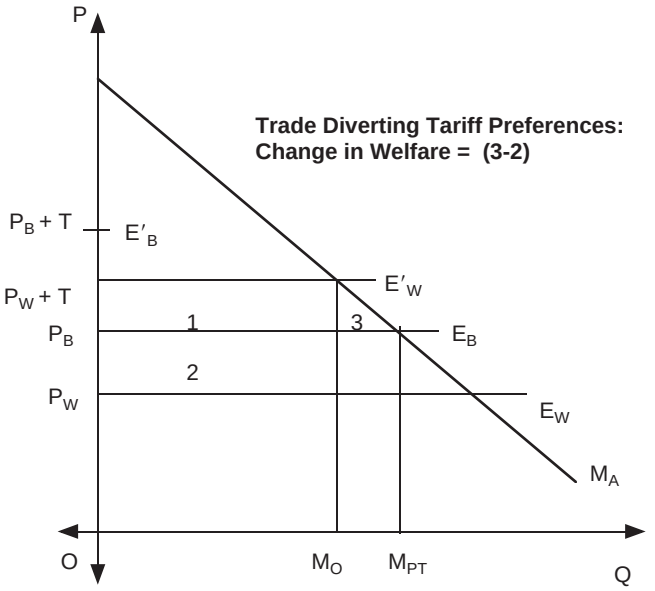


Figure 2.2

price of imports from W, $P_W + T$). The tariff preferences granted to B simply increase the volume of imports. This increase in the volume of trade with the country whose exports were initially being purchased by A anyway (i.e., with the more efficient producer) when tariffs against it are preferentially reduced is referred to as 'trade creation'. Trade creation here can be shown to be welfare improving. The increase in benefit to consumers (consumer surplus) in A following the reduction in consumption prices from $P_B + T$ to P_B equals the areas $(1 + 2 + 3 + 4)$. No tariff revenue is now earned and so the loss of tariff revenue equals areas $(1+2)$. The overall gain to A from this preferential tariff reduction equals areas $(1+2+3+4) - (1+2) =$ areas $(3+4)$, a positive number. The trade-creating tariff preference is thus welfare improving.

In demonstrating that the tariff preference we have considered is welfare improving for the home country, A, we have assumed that the partner which receives this tariff preference, B, is the more efficient supplier of the good. Figure 2.2 reverses this assumption, making W, the rest of the world, the more efficient supplier of the good. E_W is thus drawn below E_B. Initial imports are M_0. The tariff revenue collected is equal to the areas $(1+2)$. When tariffs are eliminated against B, the less efficient partner, the tariff-inclusive price of imports from W is higher than the tariff-exclusive price from B (this need not necessarily be the case, it is simply so as drawn). This implies that all trade is now 'diverted' away from W to B. What is the welfare consequence of this trade diversion? The increase in consumer surplus is

equal to the areas (1+3) since consumers now pay a price equal to P_B for this good. The loss in tariff revenue is (1+2). The overall gain to A equals the area (3−2), which may or may not be positive. Thus a trade diverting tariff preference may lead to a welfare reduction.

The preceding examples illustrate a central issue emphasised in the academic literature on the welfare consequences of preferential trade. Preferential trade liberalisation towards the country from whom the good was imported in the initial non-discriminatory situation creates more trade and increases welfare; preferential liberalisation that diverts trade instead may reduce welfare. Subsequent analysis also developed examples of both welfare improving trade-diversion and welfare-decreasing trade creation in general equilibrium contexts broader than those considered by Viner. However, the intuitive appeal of the concepts of trade creation and trade diversion has ensured their continued use in the economic analysis of preferential trade agreements, especially in policy analysis.[3]

Many recent empirical studies have quantified the adverse consequences of trade diversion and underscore the fact that trade diversion is not merely a theoretical concern. Yeats investigated the question of trade diversion within PTAs by performing an evaluation of trade patterns within MERCOSUR.[4] To describe the orientation of MERCOSUR trade, goods were characterised using two measures. The first measure is a 'regional orientation' index which is the ratio of the share of that good in exports to the region to its share in exports to third countries. The second measure is the 'revealed comparative advantage' measure which is the ratio of the share of a good in MERCOSUR's exports to third countries to its share in world exports (exclusive of intra-MERCOSUR trade). Yeats then compares the change in goods' regional orientation index between 1988 and 1994 (before and after MERCOSUR) with their revealed comparative advantage ranking. The results of his study are striking. As he notes, the goods with the largest increase in regional orientation are goods with very low revealed comparative advantage rankings. Specifically, for the 30 groups of goods with the largest increases in regional orientation, only two had revealed comparative advantage indices above unity. That is, the largest increases in intra-MERCOSUR trade have been in goods in which MERCOSUR countries lack comparative advantage, suggesting strong trade diversionary effects.

B. Internal terms of trade and revenue transfer effects

The Vinerian analysis illustrated in Figures 2.1 and 2.2 has assumed that the home country is small relative to both the partner country and the rest of the world, with the exportable goods from the partner and the rest of the world being perfect

3 For a comprehensive survey, see Arvind Panagariya, 'Preferential Trade Liberalization: The Traditional Theory and New Developments' (2000) 38(2) *Journal of Economic Literature* 287–331.

4 Alexander J. Yeats, 'Does MERCOSUR's Trade Performance Raise Concerns about the Effects of Regional Trade Arrangements?' (1998) 12(1) *The World Bank Economic Review* 1–28.

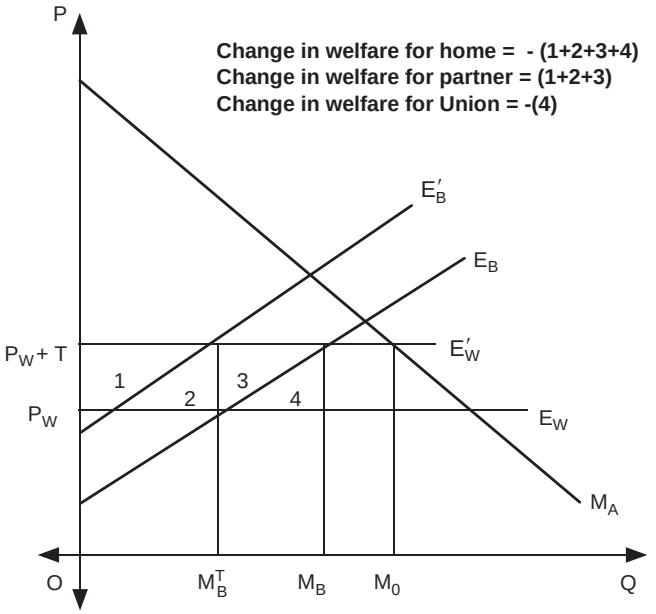


Figure 2.3

substitutes. Specifically, when consumption is switched from the rest of the world to the partner country, the partner country is assumed to be able to satisfy all of the demand of the home country. What happens if B is so small that after receiving the tariff preference from A it is unable to satisfy all of A's demand for its imported goods? This implies that A continues to import some amount from the rest of the world W (which we assume for the moment is so large that it is able to handle all of the changes in A's demand without letting this affect its supply price) even after granting preferential access to B. Here, it can be shown that the home country loses unambiguously. The following example, provided by Panagariya,[5] illustrates this.

In Figure 2.3, the export supply curve of country B is shown to be rising. The tariff inclusive supply curve faced by the home country is E_B^T. Total consumption of the importable initially is M_0 and imports from B are M_B^T. A tariff preference in favour of B simply shifts the effective export supply curve to E_B and the imports from B to M_B. Total imports stay at M_0. The domestic price of the imported good in the home market in A is set by W (which continues to supply to A) and is the same as before (i.e., it stays at E_W^T). The outcomes in this case are quite stark. Since consumption of the imported good continues to be at M_0, there is no change in consumer surplus in

5 Panagariya, above n. 3.

the home country. There is, however, a direct tariff revenue loss since no tariff revenue is now earned on imports from the partner. The loss in tariff revenue (which is equal to the overall loss to A) equals the areas (1+2+3+4). In what can effectively be seen as a tariff revenue transfer to B, a gain of areas (1+2+3) accrues to B in the form of an increase in producer surplus. Thus, preferential tariff liberalisation leads to a loss in welfare for the liberalising country, a (smaller) gain in welfare for its partner and a net loss of area (4) to the union as a whole.

In general, in the context of an exchange in tariff preferences negotiated under a preferential trade agreement, we may expect that tariff revenue losses to the home country in some sectors are made up by gains in other sectors in which the home country gets preferential access to its partner's markets. Who gains more will depend upon the extent of tariff preferences exchanged and specific market circumstances (shapes of the supply and demand curves). The outcome is uncertain.

C. External terms of trade

Thus far, we have focused our discussion on the welfare consequences of preferential trade liberalisation on the countries undertaking the liberalisation. While we have not explicitly considered this so far, it should be easy to see that changes in demand by PTA members for the rest of the world's exports could lower the relative price of these exports (i.e., worsens the rest of the world's terms of trade). In general, the overall effect on the external terms of trade may be seen as a combination of income and substitution effects. The former represents the effect of real income changes due to the PTA on demand for imports from non-members and the latter reflects the substitution in trade towards partner countries (and away from non-members) due to the preferences in trade. In the case of a real-income reducing PTA, both effects would combine to lower demand from the rest of the world. This is also the case when substitution effects dominate the income effect.[6] The rest of the world experiences deterioration in its terms of trade and is therefore adversely impacted. Some indication of how the terms of trade may change for non-member countries in practice is provided by the empirical analysis of Chang and Winters who examine the impact of MERCOSUR (specifically, the exemption in tariffs that Brazil provided to its MERCOSUR partners) on the terms-of-trade (export prices) of countries excluded from the agreement.[7] Theory would suggest that trade diversion

6 See Mundell for an analysis of how such extra-union terms of trade effects may complicate matters further for the tariff-reducing country, whose terms of trade with respect to the rest of the world may rise or fall following a preferential reduction in its tariffs against a particular partner: Robert A. Mundell, 'Tariff Preferences and the Terms of Trade' (1964) 32 *Manchester School of Economic and Social Studies* 1–13. On this point, see also the recent analysis by Panagariya: Arvind Panagariya, 'Preferential Trading and the Myth of Natural Trading Partners' (1997) 9(4) *Japan and the World Economy* 471–89.

7 Won Chang and L. Alan Winters, 'How Regional Trade Blocs Affect Excluded Countries: The Price Effects of MERCOSUR' (2002) 92(4) *American Economic Review* 889–904.

would worsen the terms of trade of excluded countries and this indeed is what they find. Specifically, their analysis reports a significant decline in the export prices of Brazil's major trading partners (the United States (US), Japan, Germany and Korea) following MERCOSUR. These associated welfare losses sustained by the excluded countries are also significant – amounting to roughly 10 per cent of the value of their exports to Brazil.[8]

III. Geography and preferential trade agreements: Is regionalism 'natural'?

The previous section has discussed some of the reasons why economists have been divided on the wisdom of preferential trade arrangements (PTAs). Following Viner's demonstration that the net welfare effects of PTAs are unpredictable and possibly negative, many attempts were made to refine the theory and identify member country characteristics that would ensure welfare improvement and thus eliminate the welfare ambiguities associated with preferential trade. However, these efforts yielded results that did not have any greater direct operational significance than did Viner. This is to say that they did not yield any direct insights on what partner country characteristics would make trade creation rather than trade diversion a likely outcome.

More recently, however, increasing emphasis has been placed on geographic proximity as a criterion for membership in a PTA. Regionalism in preferential trade has been argued by some authors[9] as being key to generating better economic outcomes, with regional trading partners described as 'natural trading partners' in the context of preferential trade. The question of natural trading partners is immensely interesting for policy reasons. Many existing preferential trading arrangements are indeed regional. In addition, many extensions of existing arrangements along regional lines, such as the expansion of the NAFTA to include Chile, Argentina, and other South American countries, or that of the European Union (EU) to include other regional countries are currently being debated and discussed in policy circles.

To evaluate the argument for geographic proximity as a membership criterion, we may start by noting that this argument itself rests on two economic hypotheses. First, that trade creation is greater and trade diversion lower when the initial volume of trade between the partners is higher (and trade with the rest of the world is lower) and second, that geographically proximate countries have larger volumes of trade with each other.

8 For instance, the United States is estimated to lose somewhere between $550 to $600 m on exports of about $5.5 bn with Germany losing between $170 and $236 m on exports of about $2 bn.

9 See, for instance, Paul Wonnacott and Mark Lutz, 'Is There A Case For Free Trade Areas?', in Jeffrey Schott (ed.), *Free Trade Areas and US Trade Policy* (Washington, DC: Institute for International Economics, 1989), pp. 59–84; Paul Krugman, 'The Move To Free Trade Zones', in Federal Reserve Bank of Kansas City, *Policy Implications of Trade and Currency Zones* (Kansas City: Federal Reserve Bank of Kansas City, 1991), pp. 7–41; and Lawrence H. Summers, 'Regionalism and the World Trading System', in Federal Reserve Bank of Kansas City, above, pp. 295–301.

As Bhagwati[10] and Bhagwati and Panagariya[11] have pointed out, however, these are not robust principles. For instance, the contention that geographically proximate countries trade more with each other is generally only valid as a conditional statement. That is to say, it is only after we 'control' for a variety of other variables (such as income levels of the partner country) that we are able to say that trade is higher between countries which are closer to each other. Importantly, however, the choice of partners in a PTA need not be conditioned on these same variables – diluting the relevance of proximity in discussions over trade preferences. An example may serve to clarify this point. In a hypothetical world, where the incomes of Japan and Mexico are equal (i.e., 'controlling' for income), US trade with Mexico may well be higher than trade with Japan. As it stands, however, Japan has a much higher income level than does Mexico. Its trade volume with the US is also much higher. Thus, even if initial trade volumes were to be used as a criterion by the US for choosing PTA members, the distant country (Japan) ought to be a preferred partner.

Furthermore it is incorrect to suggest that preferences towards the more significant partner are more likely to result in trade creation. Panagariya[12] offers a very clear argument on this point. Thus consider the economy discussed in section II.2 and illustrated in Figure 2.3. Recall that when trade preferences towards country B result in a loss of welfare for the liberalising country A. Importantly, note that the losses (areas 1+2+3+4) are greater, the greater the initial volume of trade. Thus, with changing internal terms of trade, the argument that greater initial volumes of trade result in larger increases in welfare is directly contradicted.

Finally, it should be noted that the argument concerning trade creation and larger initial volumes of trade is not robust – even when internal terms of trade do not change. To see this, note that welfare gains with trade policy changes generally depend upon substitutions at the margin (changes in trade volumes – with partners and the rest of the world) as well as the initial levels of trade. This raises two issues. First, the relevant substitution elasticities do not generally depend on the initial volumes of trade. Differences in trade elasticities may therefore offset any differences in initial trade volumes. Second and more importantly, significant trading partners generally also compete to a greater extent with the rest of the world than do less significant trading partners. For example, Japan is a more significant trading partner of the US than is Ecuador, but it also competes in a wider range of markets and in larger volumes, say with EU suppliers, than Ecuador, which competes in a narrower and economically less significant set of markets. Importantly, while trade creation

10 Jagdish Bhagwati, 'Regionalism and Multilateralism: An Overview', in Jaime de Melo and Arvind Panagariya (eds.), *New Dimensions in Regional Integration* (Cambridge: Cambridge University Press, 1993), pp. 22–51.

11 Jagdish Bhagwati and Arvind Panagariya (eds.), *Free Trade Areas or Free Trade? The Economics of Preferential Trade Areas* (Washington, DC: AEI Press, 1996).

12 Arvind Panagariya, 'The Free Trade Area of the Americas: Good for Latin America?' (1996) 19(5) *World Economy* 485–515.

may be larger with significant partners, so may trade diversion. (In the preceding example, this implies that trade preferences granted by the US to Japan will divert larger volumes of trade – away from the EU – than trade preferences towards Ecuador). The empirical analysis of Krishna[13] finds evidence of just these effects in US data. In an econometric investigation of US trade, aimed at estimating trade creation and trade diversion effects under (hypothetical) trade preferences towards a variety of countries, trade creation and trade diversion are found to be correlated in their magnitudes. In his analysis, net welfare gains (i.e., gains from trade creation net of trade diversion losses) are found to be wholly uncorrelated with distance. All in all, arguments for regionalism in trade preferences do not appear to have a substantial basis in economic theory and are not supported by empirical analysis.

IV. Necessarily welfare-improving preferential trade areas

The generally ambiguous welfare results with trade preferences provoked an important question in the economic literature relating to the design of necessarily welfare-improving PTAs. A classic result due to Kemp and Wan[14] and Ohyama[15] provides a welfare-improving solution for the case of CUs. Starting from a situation with an arbitrary structure of trade barriers, if two or more countries freeze their net external trade vector with the rest of the world through a set of common external tariffs and eliminate the barriers to internal trade (implying the formation of a CU), the welfare of the union as a whole necessarily improves (weakly) and that of the rest of the world does not fall. The logic behind the Kemp–Wan theorem is as follows: By fixing the combined, net extra-union trade vector of member countries at its pre-union level, non-member countries are guaranteed their original level of welfare. Since there is no diversion of trade in this case, the welfare of the member countries is also not adversely affected. The PTA thus constructed has a common internal price vector, implying further a common external tariff for member countries. The Kemp-Wan-Ohyama design, by freezing the external trade vector and thus eliminating trade diversion, offers a way to sidestep the complexities and ambiguities inherent in the analysis of PTAs.

The Kemp-Wan-Ohyama analysis of welfare-improving CUs does not extend easily to FTAs since member-specific tariff vectors in the case of FTAs imply that domestic prices will differ across member countries. Panagariya and Krishna have, nevertheless, recently provided a corresponding construction of necessarily welfare-improving FTAs in complete analogy with the Kemp-Wan CU, with the essential difference that the trade vector of each member country with the rest of the

13 Pravin Krishna, 'Are Regional Trading Partners Natural?' (2003) 111(1) *Journal of Political Economy* 202–31.

14 Murray C. Kemp and Henry Wan Jr, 'An Elementary Proposition Concerning The Formation Of Customs Unions' (1976) 6(1) *Journal of International Economics* 95–7.

15 Michihiro Ohyama, 'Trade and Welfare in General Equilibrium' (1972) 9(1) *Keio Economic Studies* 37–73.

world is frozen at the pre-FTA level.[16] Since, in FTAs, different member countries impose different external tariffs, it is necessary to specify a set of rules of origin (ROO) to prevent a subversion of FTA tariffs by importing through the lower-tariff member country and directly trans-shipping goods to the higher-tariff country (which, if allowed, would bring the FTA arbitrarily close to a CU). The Panagariya-Krishna solution requires that all goods with any value added within the FTA are to be traded freely. Goods which enter the FTA as final goods are to be wholly prevented from trans-shipment by suitable ROO.

Theory thus suggests that ensuring welfare improvement requires that along with elimination of internal barriers, external tariff vectors should eliminate trade diversion – member countries should continue to import the same amounts from the rest of the world as they did initially. The next section, examines how these theoretical prescriptions compare with WTO rules concerning the formation of PTAs.

V. PTA implementation and the WTO

The preceding discussion of necessarily welfare improving CUs and FTAs provided a precise description of the tariff vectors that ought to be implemented in these agreements. Specifically, internal barriers are to be completely eliminated and the external tariff vector in both cases (i.e., the CU or the FTA) should eliminate trade diversion. Member countries should continue to import the same amounts from the rest of the world as they did initially. Can these be implemented in practice? And where do existing GATT/WTO provisions stand in relation to the theoretical specification?

Article XXIV of the GATT, which permits the formation of PTAs, also originally stipulated that internal preferences needed to be complete (i.e., that internal barriers between the members were to be completely eliminated) and that external trade barriers were not to be more restrictive than initially. As we will discuss below, a number of questions arose in connection with GATT regulations regarding both internal and external tariffs – some having to do with their economic merit, others to do with implementation and possible abuse given the ambiguous and imprecise wording adopted in the original text of the GATT. As we will discuss further, while the more recent 'Understanding on the Interpretation' of Article XXIV issued by the GATT in 1994 clarified some of these issues, other questions still remain.

A. Internal barriers to trade

On internal barriers to trade, two questions arise. The first relates to coverage – do GATT regulations require a removal of all internal barriers? The second relates to

16 Arvind Panagariya and Pravin Krishna, 'On the Existence of Necessarily Welfare Improving Free Trade Areas' (2002) 57(2) *Journal of International Economics* 353–67.

timing – how much time do countries have to comply with the rules? On the former issue, it should be stated that while the putative intent of the GATT was to require that internal barriers be eliminated completely, the actual text of the GATT only required that restrictions be eliminated on 'substantially all trade'. The ambiguous phrasing through the use of the qualifier 'substantially' opened up a number of possibilities for abuse. Whether 'substantially' should have been taken to imply a full 100 per cent or something smaller was not clear and has not yet been clarified. In this context, it is worth noting that for a given level of external tariffs, member country welfare is not necessarily maximised with zero internal barriers.[17] From a purely economic standpoint, given the level of external tariffs, welfare may well be maximised by maintaining some particular level of internal restrictions. It may therefore be argued that the ambiguous phrasing permitting non-elimination of internal barriers allowed member countries to aim at welfare-maximising outcomes. This, however, is quite unlikely. Any retention of internal barriers within PTAs is probably better explained by selective protectionist motivations on the part of country governments. Separately, it may be imagined that non-member countries would have an incentive to monitor and ensure the full dismantling of internal trade barriers within PTAs. However, it is also quite likely that the welfare of countries outside the union is higher when the discrimination against them is lower (i.e., when internal preferences are less than complete). Ex-post, the external monitoring incentive is therefore minimal. On the question of the timing and the phasing out of internal barriers to trade, GATT rules, rather than requiring an immediate removal of internal barriers in a PTA, allowed for this to take place within a 'reasonable length of time', once again permitting substantial ambiguity in understanding and providing room for abuse.[18]

B. External barriers to trade

On external tariffs, the original GATT requirement was that external barriers not be more restrictive than initially. For FTAs, since countries retain individual tariff vectors, this could be taken to imply that no tariff was to rise. For CUs, since a common external tariff was to be chosen, and initial tariffs on the same good probably varied across countries, the tariff vector would necessarily change for each country. The expectation was then that the 'general incidence' of trade barriers would not be higher or more restrictive than before. Given the imprecise phrasing, there was once more substantial ambiguity as to what is implied – should the

17 It is important to keep in mind here that the elimination of internal tariffs maximises the welfare of member countries for a given level of external trade (as in Kemp–Wan) and not for a given level of the external tariffs. With fixed tariffs, member country welfare may well be maximised with internal tariffs that are non-zero.

18 The more recent 'Understanding on the Interpretation' of Article XXIV issued in 1994 clarifies that the 'reasonable length of time' should exceed ten years in only 'exceptional cases'.

common external tariff equal the un-weighted mean of initial tariffs in the member countries? Should it be the trade-weighted mean? Or something else? As Dam,[19] Bhagwati[20] and several others have noted, it is clear that Article XXIV's ambiguity in this regard left plenty of room for opportunistic (i.e., protectionist) behaviour by member countries against non-members. The 1994 'Understanding on the Interpretation' of Article XXIV issued by the GATT provided substantial clarity on the issue of measurement and choice of the common external tariff – indicating that the GATT secretariat would compute weighted average tariff rates and duties collected in accordance with the methodology used in the assessment of tariff offers in the Uruguay round of trade negotiations and examine trade flow and other data to arrive at suitable measures of non-tariff barriers. While this relieves, at least partially, the issue of measurement of external barriers and the comparison with barriers in place initially, the economic concern regarding trade diversion is not addressed. Clearly, leaving external barriers at their initial level and removing internal barriers does not eliminate trade diversion (as theoretically required in the Kemp-Wan and Panagariya-Krishna constructions of welfare-improving PTAs). Indeed, with this configuration, trade diversion is practically guaranteed.

Having pointed to the deficiencies in existing GATT regulations in relation to the elimination of trade diversion, it may be noted that picking or designing tariff vectors *ex ante* that would ensure zero trade diversion, good by good, is a rather difficult task; the necessary measures of the exact sensitivity of external trade flows to external barriers of the CU or the FTA would be hard if not impossible to estimate accurately. So there is little prospect of identifying the exact trade-diversion-eliminating Kemp–Wan tariff vector and implementing it in practice.[21] Nevertheless, designing other disciplines to minimise diversion is less difficult; one can certainly say that lowering external barriers simultaneously with the formation of a CU or an FTA is likely to lower the degree of trade diversion (by minimising the substitution away from the goods supplied by the rest of the world to within-union goods). McMillan[22] has suggested as a test of admissibility of any PTA the measurement (estimation) of whether that PTA will result in less trade with the rest of the world.[23] In a similar spirit,

19 Kenneth W. Dam, *The GATT: Law and International Economic Organization* (Chicago: University of Chicago Press, 1970).

20 Bhagwati, above n. 10.

21 See, however, the paper by Srinivasan which attempts to identify and characterise the Kemp-Wan tariff vector in the context of a particular economic model: T. N. Srinivasan, 'Common External Tariffs of a Customs Union: The Case of Identical Cobb Douglas Tastes' (1997) 9 *Japan and the World Economy* 447–65.

22 John McMillan, 'Does Regional Integration Foster Open Trade? Economic Theory and GATT's Article XXIV', in Kym Anderson and Richard Blackhurst (eds.), *Regional Integration and the Global Trading System* (New York: St Martin's Press, 1993), pp. 292–310.

23 Of course, the Kemp-Wan and Panagariya-Krishna schemes both require that the PTA trade exactly the same amount as before. A PTA that trades no less, as in the McMillan test, is not necessarily welfare improving, as Winters has argued: L. Alan Winters, 'Regionalism and the Rest of the World: The Irrelevance of the Kemp-Wan Theorem' (1997) 49 *Oxford Economic Papers* 228–34.

Bhagwati[24] has suggested that the requirement of a simultaneous pro rata reduction of external trade barriers with the progressive elimination of internal barriers could replace the current requirements.

C. *Rules of origin*

In free trade areas, importers have a potential incentive to import goods into the bloc through the member country imposing the lowest tariff on that good and then to tranship that good into higher tariff member countries by availing themselves of the duty free treatment within the bloc. To prevent this circumvention of the independent tariffs desired by member countries, however, FTAs need to be supported by ROO, which specify the circumstances under which a good may be given duty free treatment within the union.[25]

The discussion in the previous section has provided a welfare-theoretic basis for very simple rules of origin – goods which undergo any genuine value-added transformation within the union must be allowed to move duty free within the union. For any good entirely produced outside the union, trade deflection is to be prevented by imposing on direct imports and also any trans-shipped units the external tariff that is chosen by the member country where the good is eventually consumed. However, rules of origin are more complex in practice. They are differently concerned (depending on the good) with the fractional content of the good that is required to be produced within the union for the good to qualify for duty-free status.[26] More importantly, while the putative intention of rules of origin is to simply to prevent deflection of trade, it has been argued that these rules have been used more flexibly as instruments of commercial policy.[27]

That the opportunity to set rules of origin would be abused to achieve other ends should come as no surprise to anyone even moderately familiar with the political economy of trade policy determination. While we may hope for FTA rules to be designed by welfare-maximising governments concerned with the enhancement of internal efficiency and equity towards non-members, in practice, the rules of origin are determined in intensely political contexts in which a variety of additional factors influence policy. Governments are under great pressure to deviate from the high path of choosing rules of origin to simply prevent trade deflection towards fixing

24 See Bhagwati, above n. 10.

25 Since, in practice, at least some traded goods are not covered by the common external barriers of a CU, ROO are often used in CU as well.

26 For a detailed discussion of the different ways in which rules of origin are specified in practice, see Krishna, above n. 13.

27 See, for instance, Kala Krishna and Anne O. Krueger, 'Implementing Free Trade Agreements: Rules of Origin and Hidden Protection', in Alan V. Deardorff, James A. Levinsohn and Robert M. Stern (eds.), *New Directions in Trade Theory* (Ann Arbor: University of Michigan Press, 1995), pp. 149–87.

rules that favour politically active and aggressive constituencies in the economy. Because in an FTA, there are no internal tariffs and because external tariffs themselves cannot be raised to further disadvantage non-member countries, it has been argued that, to please their constituencies and protect them from the economic changes that come about due to entry into the free trade area, governments manipulate rules of origin to protect both domestic suppliers of final and intermediate goods.[28] This may happen in the following ways:

(a) *Protection for final good suppliers*: Consider a final goods supplier in a member country facing greater competition from suppliers in other member countries due to the impending elimination of internal barriers of trade within the FTA. Consider further that this foreign competition uses in its production intermediates from outside of the FTA. Due to the political pressures brought to bear on the domestic government, whether it is from capitalists, affected voters, or displaced workers, that government will have reason to negotiate intra-union content criteria severe enough to push those competing goods out of the duty-free category. In so doing they will insulate the home country supplier from that greater competition, but also undermine the intended competitive enhancement from joining an FTA.
(b) *Protection for intermediate goods suppliers*: Governments can negotiate for rules of origin that specify a high degree of domestic (i.e., within-bloc) content, significantly diverting demand from goods produced with foreign intermediates to goods produced using intermediates from within the FTA.

However, this use of rules of origin undermines the two key rules imposed by the WTO on its members for FTA formation. While complete internal liberalisation is sought by the WTO, this is negated by the selective use of rules of origin. Further, while the WTO requires that trade barriers against non-members cannot be raised by FTA members, the use of stringent rules of origin would divert imports of intermediates away from non-member exporters even if external tariffs are maintained at the same level as before.[29]

To what extent rules of origin are used to prevent trade deflection and to what extent they are politically motivated commercial policy instruments is ultimately an empirical question. While empirical research in this area is still in its infancy, Cadot, Estevadeordal and Suwa-Eisenmann[30] have recently provided some interesting

28 Of course, it may be just such protection that enables a government to generate enough political support for the FTA in the first place, as Duttagupta and Panagariya have argued: Rupa Duttagupta and Arvind Panagariya, 'Free Trade Areas and Rules of Origin: Economics and Politics', mimeo, 2001.

29 Ironically, however, highly severe rules of origin may result in greater imports from the rest of the world than before, owing to the preference of importers to pay the external tariff rather than comply with demanding domestic-content standards.

30 Olivier Cadot, Antoni Estevadeordal and Akiko Suwa-Eisenman, 'Rules of Origin as Export Subsidies', mimeo, 2003.

results. They directly examined the possible use of rules of origin to achieve protection for final goods producers and the creation of a captive market for intra-union suppliers of intermediate goods. Specifically, they measured the effects of rules of origin on Mexican imports to the US market and found that rules of origin were a large enough negative influence on intra-union trade flows so as to offset the tariff preferences granted by the trade agreement. Further, the creation of a protected market for intermediate goods producers also appears to be a key determinant of the rules of origin chosen.

D. Non-trade issues in preferential integration

Some proponents of preferential integration have argued[31] that PTAs achieve 'deep' integration. That is, rather than simply achieving trade liberalisation, as in multilateral liberalisation contexts, PTAs involve 'deep' integration through co-ordination, or harmonisation, of other non-trade policies such as competition policies, environmental policies, labour standards, product standards and investment codes. It is further argued that such harmonisation of policies will be efficiency enhancing and beneficial to member countries.

The proposition that harmonisation of policies is uniformly beneficial to all of the member countries in a PTA has been met with scepticism by others[32] who note that there are good reasons for diversity in domestic policies and standards and that harmonisation is not automatically a welfare enhancing policy. For instance, the choice of optimal pollution levels and labour standards generally depends on income level. While every country may prefer lower pollution levels, countries may reasonably disagree on what the optimal pollution levels are, what costs they should bear to lower pollution and where these efforts are best directed (e.g., developing countries may prefer to lower water pollution, while air pollution may be a greater concern for richer countries). Similarly, countries may disagree on minimum wage levels, worker-safety issues and on the merits of permitting voluntary child labour. Thus, while harmonisation may indeed bring some forms of efficiency enhancement, it is far from clear that such harmonisation of policies will be beneficial overall or that any benefits will accrue uniformly to all the member countries. A practical concern is that under the guise of 'deep integration' the larger and more powerful countries in a PTA negotiation may be able to extract concessions not merely in trade but in other 'non-trade' matters as well.

31 See, for instance, Robert Z. Lawrence, *Regionalism, Multilateralism and Deeper Integration* (Washington, DC: The Brookings Institution, 1997).

32 See, for instance, Arvind Panagariya, 'The Regionalism Debate: An Overview' (1999) 22(4) *World Economy* 477–511.

VI. Conclusion

PTAs, while conceived originally as minor exceptions to the GATT's central principle of non-discrimination, and only to be permitted under strict conditions, now number in the hundreds. A half-century of research has advanced significantly our understanding of the implications of trade discrimination even if the frequently equivocal theoretical and empirical results have established among economists and policy-makers an ambivalent attitude towards preferential trade agreements. However, concerns regarding the fragmentation of the world trade system have grown with the rapid proliferation of PTAs in recent years. Several hundred PTAs are currently in existence (with many countries belonging to multiple PTAs) and many more are in process. With this inexorable erosion of non-discriminatory disciplines within the trade system, research on preferential trade is certain to remain central to the field of international trade policy for many years to come.

3

The political economy of PTAs

OLIVIER CATTANEO

I. Introduction: Re-thinking the paradigm of Bilateral/Regional Trade Agreements

Why do countries conclude bilateral/regional trade agreements? Numerous researchers have sought to answer this question, most often through creating a typology of the agreements. Such efforts, however, have been in vain. A bilateral/regional trade agreement is rarely, if ever, based on a single motive, and two or more parties to an agreement can often have different and sometimes even conflicting objectives (e.g., one seeking market access and the other political support). In fact, different actors within each country itself can also have different objectives (e.g., one sector seeking trade creation whilst another trade diversion). Thus, any typology is bound to create artificial categories, and would not necessarily give a proper or accurate answer to the original question.

Sometimes, countries fall into a similar trap by trying to explain the rationale behind their bilateral/regional trade policy. For example, the European Commission recently acknowledged that it had been predominantly motivated by political considerations in concluding trade agreements with countries that were candidates for European Union (EU) membership (with the exception of Mexico, South Africa, and Chile). Although such a policy is in line with the EU's neighbourhood and development objectives, it does little to serve the EU's central trade interests.[1] The EU has since designed a new strategy (so-called 'Global Europe'), where economics is restored as the chief criterion for future bilateral agreements and the selection of future partners will be based on:

- their market potential (economic size and growth),
- their level of protection against EU export interests (tariffs and non-tariff barriers), and
- the state of negotiations with EU competitors (to measure the likely impact of a bilateral agreement with a competitor on EU markets and economy, as well as the

1 European Commission, *Global Europe: Competing in the World. A Contribution to the EU's Growth and Jobs Strategy*, Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, COM/2006/0567 of 4 October 2006, Brussels, at p. 11.

risk of erosion of the preferential access to EU markets currently enjoyed by the EU's neighbouring and developing country partners).[2]

On this basis, the Commission concluded that the Association of Southeast Asian Nations (ASEAN), Korea, and the Common Market of the Southern Cone (MERCOSUR) were 'priorities'; while India, Russia, and the Gulf Co-operation Council (GCC) were 'of direct interest'; and China, although meeting the criteria, 'required special attention' because of both the potential and risks it presented.[3] Some commentators have, however, already contested the objectivity of this selection: 'The fact that, on Commission's own numbers, its new targets for free trade agreements account for only a third of the potential markets in Asia, takes the shine off this argument'.[4] According to Evenett, the latest communication of the European Commission is probably best thought of as an evolution of EU trade policy rather than an abrupt break with the past.[5] Thus, apart from the re-packaging, the EU bilateral trade policy remains a combination of economic and other (political) factors.

The United States (US) offers a similar opinion. A 2004 report of the US General Accounting Office (GAO) lists six factors driving the selection of potential preferential trade agreement (PTA) partners:

- country readiness,
- economic/commercial benefit,
- benefits to the broader trade liberalisation strategy,
- compatibility with US interests,
- Congressional/private sector support, and
- US government resource constraints.[6]

These factors are vague enough to make the claim that decisions 'are not mechanical' and furthermore 'reflect US trade strategy, foreign policy, and foreign economic development goals'.[7] As a result, PTAs cannot be placed in clean-cut boxes, as it is widely recognised that they are not primarily driven by economics.

Questioning the objectives of US trade policy, the Ways and Means Committee of the House, at the end of January 2007, called for a hearing on trade and globalisation with a view to elicit responses from witnesses concerning: (1) the theory that more trade is always better, no matter its terms or contents; (2) recommendations on

2 *Ibid.* 3 *Ibid.*

4 Simon J. Evenett, 'The New EU Trade Policy: Grand Strategy or Stop-Gap?', *WTO News from the Swiss Institute for International Economics and Applied Economic Research*, Issue No. 15, January 2007, at p. 1.

5 Simon J. Evenett, 'Global Europe: An Initial Assessment of the European Commission's New Trade Policy' (January 2007) 61(4) *Aussenwirtschaft* 377–402.

6 USGAO, *International Trade: Intensifying Free Trade Negotiating Agenda Calls for Better Allocation of Staff and Resources*, GAO-04-233 (January 2004), available at www.gao.gov/new.items/d04233.pdf.

7 *Ibid.*, at p. 2.

specific changes to US trade policy and international trading rules in order to maximise the benefits and minimise the costs of liberalisation; and (3) what have been some of the most important successes of US trade policy in the recent past.[8] In other words, the philosophy of trade agreements (bilateral, regional and multilateral) is itself being brought into question. Far from being a 'mechanical decision' based on precise economic criteria, the negotiation of new trade agreements remains at the mercy of political and ideological arbitrages between advocates and opponents of free trade.

Based on these preliminary considerations, this chapter does not attempt to create yet another typology of trade agreements. Instead, it attempts to explain the key role of bilateral/regional trade agreements in international trade history (Part II); it argues for the revocation of the idea that trade agreements are strictly economically driven (Part III); and it stresses their political dimension (Part IV). It therefore, challenges some basic assumptions on which the usual critics of bilateralism/regionalism are based. The first challenged assumption is that multilateralism is the rule and bilateralism/regionalism the exception; from a historical perspective, it is the opposite, and bilateral/regional agreements are the most common trade policy instruments. The second challenged assumption is that trade policy, and bilateral/regional agreements in particular, always have to make economic sense when in fact it is only a political arbitrage/compromise between free trade and protectionist views (two economic doctrines, but where economic rationale competes with ideology), driven by foreign or domestic policy considerations.

II. Multilateralism is the exception, not the rule

Bilateral/regional trade agreements are not new: they pre-date multilateral trade agreements by centuries. The proliferation of bilateral/regional trade agreements – the source of most comments and fears about PTAs today – is not a new phenomenon either. In the 1860s, following the conclusion of an FTA between France and Britain (the Cobden–Chevalier Treaty), trading nations rushed into a 'free trade epidemic'.[9] According to Accominotti and Flandreau, the 14 trading nations of the time concluded more than 50 bilateral treaties,[10] i.e., more than half of the technically possible combinations ($14 \times 13 \div 2 = 91$).[11] By comparison, today,

8 Hearing archives are available at www.waysandmeans.house.gov/hearings.asp (Hearing on Trade and Globalization of 30 January 2007).

9 Olivier Accominotti and Marc Flandreau, 'Does Bilateralism Promote Trade? Nineteenth Century Liberalization Revisited', Center for Economic Policy Research Discussion Paper Series No. 5423 (December 2005), at p. 3.

10 United Kingdom, France, Zollverein, Austria–Hungary, Italy, Spain, Norway–Sweden, Belgium, Denmark, Russia, US, Portugal, Switzerland, and the Netherlands.

11 Accominotti and Flandreau, above n. 9, at p. 22.

the 152 members of the WTO have notified roughly 350 trade agreements, i.e., 'only' 3 per cent of the technically possible combinations ($152 \times 151 \div 2 = 11{,}476$).[12]

Nor was the long history of bilateral/regional trade agreements meant to end with the emergence of multilateralism. Bilateralism/regionalism and multilateralism have long co-existed. Article I of the General Agreement on Tariffs and Trade (GATT 1947) excluded *existing* preferential schemes from the most-favoured-nation (MFN) treatment (grand-father rights). In addition, Article XXIV provided a legal framework for *future* bilateral/regional trade agreements, stressing their role in the trade-liberalisation process. Despite the emergence of a multilateral regulatory framework for trade, embodied in the World Trade Organisation (WTO) since 1995, countries have continued to use bilateral/regional agreements as a common tool of trade and foreign policy.

A. An historical perspective on the respective roles of bilateralism and multilateralism

History has consisted of successive waves of liberalism and protectionism, and bilateral/regional trade agreements have often served both purposes: some agreements securing trade monopolies, while some others liberalising trade, including on an MFN basis. These agreements have pre-dated modern states. In 1157, the Hanseatic League (an alliance of trading guilds representing German cities) negotiated a trade agreement with England, which included special trading privileges and market rights, exemptions from all London tolls, and the authorisation to trade at fairs throughout England.[13] While the globalisation of free trade was advocated early (e.g., Hugo Grotius published his *Mare Liberum* treatise [in 1604], where he advocated open-use of the sea for the maritime trade of all nations), multilateral agreements appeared only at the end of the nineteenth century. At first they were confined to specific commodities (e.g., multilateral negotiations regarding international sugar trade started in the 1850s and led to the 1902 Brussels Sugar Convention)[14] or trade-related topics (e.g., the 1883 Paris Convention for the Protection of Industrial Property or the 1886 Berne Convention for the Protection of Literary and Artistic Works). It was not until the next wave of trade liberalisation, in the aftermath of World War II, that a multilateral instrument (the GATT 1947) aimed to discipline all trade – with significant exceptions such as trade in agriculture or services (neither being properly addressed until 1995).

12 Note that the 350 trade agreements notified to the WTO include regional (as opposed to bilateral) trade agreements, both increasing the number of technically possible combinations and the potential coverage of each of the agreements. The comparison therefore only gives a rough element of comparison.

13 Philippe Dollinger, 'The German Hansa', vol. 1 of *The Emergence of International Business, 1200–1800; with a new introduction by Mark Casson* (London: Routledge/Thoemmes Press, 1999).

14 Heitor Pinto de Moura Filho, 'Pioneering Multilateralism: The Sugar Agreements 1864–1914', Paper presented at the XIVth International Economic History Congress, Helsinki, 2006, Session 109.

According to some authors, trade policy has long rested on bilateral negotiations, proving that they could be an effective instrument of liberalisation and trade promotion.[15] For others, however, trade liberalisation and growth have happened *in spite of* these bilateral agreements.[16] This controversy largely results from confusing the act of liberalising trade (signing an agreement and, for example, reducing tariffs) and the effects of such an action. It is therefore possible that during the period when free trade reached its peak in Europe in the 1860s (when dozens of PTAs were signed) there was a serious decline in trade (and economic) growth.[17] Some empirical studies on the 1860s suggest that bilateralism did not promote trade.[18] This is not a critique of bilateral trade agreements (BTAs) (as opposed to, for example, multilateral agreements) per se, it is merely a query of the impact of trade liberalisation on trade growth. Recent economic literature has similarly suggested that the WTO (and its predecessor GATT) do not actually promote trade.[19]

We do know that *de facto* 'FTAs' corrupted the universal doctrine of free trade by introducing the concept of 'reciprocity'. These were in response to the findings of John Stuart Mill who suggested that more economic surplus from trade could accrue to a country following reciprocal, rather than completely free, trade policies. Compared to unilateral liberalisation, which had until then prevailed both in theory (models based on absolute or comparative advantages) and in practice (England, in the 1860s, bound some concessions in trade agreements it had unilaterally made since the 1840s), reciprocity was a backward step.[20] Some authors have even suggested that England at that time promoted FTAs with a view to preserving its technological advantage (acquired with the help of high tariff protection) – kicking away the ladder, so to speak, or confining its trade partners to the production of commodities and agricultural products (trade in which was promoted by the suppression of the Corn Laws) while flooding their markets with its manufactured goods.[21] Interestingly enough, the same critics are today opposed to the WTO and its most advanced members.

Nineteenth century BTAs included an MFN clause: after two countries concluded a trade agreement, all additional concessions made by one of the countries to a third party in subsequent agreements would systematically be extended to its partner. In other words, the proliferation of agreements created a

15 Douglas A. Irwin, 'Multilateral and Bilateral Trade Policies in the World Trading System: An Historical Perspective', in Jaime de Melo and Arvind Panagariya (eds.), *New Dimensions in Regional Integration* (Cambridge: Cambridge University Press, 1993), pp. 90–119.

16 See, e.g., Paul Bairoch, *Economics and World History, Myths and Paradoxes* (Chicago: University of Chicago Press, 1993), at pp. 44–5; and Accominotti and Flandreau above, n. 9.

17 See Bairoch above, n. 16, at pp. 46–7. 18 See Accominotti and Flandreau above, n. 9.

19 Andrew K. Rose, 'Do We Really Know that the WTO Increases Trade?' (2004) 94(1) *American Economic Review* 98–114.

20 Unless one country was forced into unilateral concession by another, e.g., in the so-called 'unequal treaties' presented in Part IV of this chapter, in which case reciprocity was a step forward.

21 Charles P. Kindleberger, *Economic Response: Comparative Studies in Trade, Finance, and Growth* (Cambridge MA and London: Harvard University Press, 1978).

virtuous circle of tariff reductions, where new concessions would be automatically propagated through the entire web of PTAs.

This original version of the MFN clause has, however, been corrupted over time, once again by the concept of reciprocity. With the Great Depression of the last quarter of the nineteenth century, countries reverted to protectionism and high tariffs: in 1879, Bismarck abandoned the German free trade policy; in 1888, Benjamin Harrison won the US presidency on a protectionist ticket; and in 1892, France introduced the Méline Tariff. This 'tariff war' reached its peak in the aftermath of the 1929 crash, as famously illustrated by the adoption of the Smoot-Hawley Tariff Act that doubled US tariffs. In this difficult economic and political context, it became clear that countries would not give away concessions by making them available to all without some form of recompense. The concept of *conditional* MFN was thus introduced and followed for a time, for example by the US, where concessions would be generalised, but only at the price of *reciprocal* concessions.[22] This ideological transition was best illustrated by the adoption of the 1934 Reciprocal Trade Agreements Act (RTAA), which allowed for BTAs that did not include an MFN clause. However, this ideological shift created a greater complexity in negotiations, and discrimination became the rule. Aware of both these complications and the political vulnerabilities of offering unconditional MFN again, Cordell Hull and others found a motive for moving to a multilateral forum. In their minds, the conclusion of a multilateral deal could help to extract concessions from otherwise unreciprocating beneficiaries.[23] This strategic move is comparable to Arthur Dunkel's 1990 proposal to create a world trade organisation, in the hopes of unlocking the Uruguay Round negotiations (which started in 1986), forcing concessions from all in a package deal, and putting an end to the 'GATT-à-la-carte' discriminatory approach consecrated by the Tokyo Round (concluded in 1979).

In other words, the GATT 1947 was the only solution that could be found to restore unconditional MFN without having to give away concessions whilst receiving no benefit in return – and once again, the mandate of the US President was to negotiate *reciprocal* trade agreements. The GATT was therefore not fundamentally different in spirit from any of the bilateral PTAs concluded in the late nineteenth century. One could even say that the GATT was the largest PTA the US had ever concluded – history having changed the once pragmatic solution dictated by US domestic policy constraints into an icon of post-war solidarity spirit. For some commentators at the time, the motives of the US behind the conclusion of the GATT were quite similar to those of the United Kingdom (UK) in 1860 – to secure technological advances and market shares for a booming manufacturing sector:

> One should not forget that the US is in a peculiar position. After doubling its production capacities during the war, it will have, tomorrow, in order to avoid

22 Kenneth W. Dam, 'Cordell Hull, The Reciprocal Trade Agreement Act, and the WTO', University of Chicago Law & Economics, Olin Working Paper No. 228 (October 2004), at p. 6.

23 *Ibid.*

> unemployment, to increase its exports in vast proportions. Some already quote numbers that are hard to believe. The US policy will therefore be a large scale expansionist trade policy, facilitated by the needs of countries hit by the war.[24]

It should also be remembered that only twenty-three countries participated in the first round of GATT negotiations (Geneva Round, 1947), and thirteen in the second (Annecy Round, 1949) – less than the number of countries in the web of PTAs at the end of the nineteenth century. It is also worth noting that the 'regional' (and to some extent preferential) character of the GATT was reinforced by the non-participation of the Soviet countries; the GATT has historically been used as an instrument of reinforcement of economic (and political) solidarities within the Western bloc.

As mentioned earlier, the GATT 1947 did not ban bilateral/regional trade agreements, but instead granted grandfather rights to existing preferential schemes and secured the possibility of contracting parties concluding more such agreements in the future. The MFN clause became lost in the web of PTAs, however, with important consequences for the world trading system. While in the late nineteenth century the proliferation of PTAs resulted in a general lowering of tariffs, the current proliferation of PTAs simply creates more discrimination. Bilateralism/regionalism is not to blame: the GATT contracting parties have continuously tried to circumvent the MFN clause through the use of FTAs, among other avenues (e.g., the 1979 Enabling Clause authorised GATT contracting parties to maintain generalised systems of preferences in favour of developing countries). This has led some commentators to rename MFN treatment in the WTO 'least-favoured-nation' treatment.

In sum, the motivations behind PTAs and multilateral deals are not fundamentally different. In the past, different circumstances have led countries to opt for either one or the other instrument. When the free trade spirit blows over a country or a region, whatever instrument is most readily available will be instinctively used. In exceptional cases, multilateral deals – which are the most efficient method of trade acceleration – will be used but bilateral/regional trade agreements will remain the bread and butter of international trade policies.[25]

B. Multilateralism and bilateralism/regionalism: supplements or substitutes?

The above conclusion is very pragmatic – when it comes to trade liberalisation, bilateral/regional and multilateral agreements have been interchangeably used (even if results differ). The partial shift from bilateralism to multilateralism in 1947 was primarily the result of a conjunction of exceptional political and historical

24 'Les Accords de Bretton-Woods', *Le Monde*, 26 July 1945, at p. 1 (author's translation).

25 An interesting topic for further research would be to investigate whether the GATT 1947 was closer in spirit to an PTA than it is to the WTO, justifying current disaffection for the latter and the proliferation of bilateral/regional trade agreements.

circumstances. In practice, countries will use whichever instrument offers the best chance of success in the promotion of specific trade interests.

Naturally, countries first turn to the WTO, because of the potential higher return on negotiation time and costs. However, commitment to multilateralism ends there. This is perfectly illustrated by the EU trade strategy. The 'Global Europe' Communication of the Commission stresses that the EU remains committed to the WTO, but that the Doha Development Agenda (DDA) cannot be the only trade policy tool used to enhance the competitiveness of the EU economy.[26] According to the same document:

> FTAs, if approached with care, can build on WTO and other international rules by going further and faster in promoting openness and integration, by tackling issues which are not ready for multilateral discussion and by preparing the ground for the next level of multilateral liberalization.[27]

Issues of particular economic importance referred to by the EU (also qualified as 'new areas of growth') are, notably intellectual property, services, investment, public procurement and competition.[28] The EU first turned to the WTO to address these issues, and became the main promoter of the so-called 'Singapore issues' (investment, competition, trade facilitation, and transparency in government procurement) in the DDA. However, absent any consensus on the modalities of negotiations, the ambition of the DDA on 'Singapore issues' was largely scaled down: the so-called 'July Package' (2004) removed three out of four issues from the Doha work programme.[29] Similarly, on the intellectual property front, the EU tried to promote the extension of rules on geographical indications at the WTO, but encountered serious opposition from other members (thereby vindicating the EU's assertion that the WTO could not be the only trade policy tool to promote its trade interests in certain new areas).

The EU is not the only actor to use 'new age' bilateral/regional trade agreements that explore areas not covered, or insufficiently covered, by the WTO. The objective of these FTAs could be to break new ground and tackle new obstacles to trade (e.g., competition or investment rules), or to go further than the WTO on certain topics (e.g., intellectual property, labour or environmental regulations). For example, most US trade agreements include provisions that go beyond WTO rules in patenting and other intellectual property rules (so-called 'TRIPS+' or 'WTO+' provisions) – e.g., the United States–Singapore Free Trade Agreement; the North American Free Trade Agreement (NAFTA) and the United States–Jordan Free Trade Agreement both contain labour standards and environmental regulations.[30] These 'WTO+' rules are important to the US and the EU for securing market access and fair competition of some specific products (e.g., European wines and US

26 European Commission, above n. 1, at p. 10. 27 *Ibid.* 28 *Ibid.*, at p. 7.
29 WTO, Decision Adopted by the General Council on 1 August 2004, WT/L/579, 2 August 2004.
30 See Chapters 11 and 12 of this volume.

pharmaceutical products). The long-term objective is more subtle: some EU and US standards (e.g., genetically modified organisms) or rules (e.g., moral rights, geographical indications, and patenting of genes and certain organisms in intellectual property law, or competition law) are incompatible; thus, PTAs are designed by the US and the EU to lock as many countries as possible into a specific set of rules, and either prepare the ground for the next round of multilateral trade negotiations that would include these areas (i.e., build a coalition of like-minded countries), or secure the widest possible diffusion of these rules in the absence of multilateral disciplines (see Part IV below on the race for power between the major trading nations).

The flexibility of PTAs also allows trade to move faster in certain areas where a country has clear offensive interests (e.g., services), while slowing the pace of liberalisation in other areas where defensive interests prevail (e.g., agriculture). In the same vein, an PTA can be concluded with a country with a complementary production structure, with a view to avoiding conflicts of interest – although this significantly reduces the potential economic benefits of the agreement (from an economic perspective, the benefits of liberalisation and competition arise when the two countries trade similar products). Because of the MFN clause, this selectivity is not possible in a multilateral framework, and global deals necessarily imply more politically painful decisions. Examples of such selective agreements include the Japan–Singapore New-Age Economic Partnership Agreement (Japan–Singapore EPA), where the absence of a significant agricultural sector in Singapore facilitated the signing of an agreement; however, the Japan–Singapore EPA also excluded the very few agricultural products that Singapore does export, such as cut flowers and ornamental fish.[31] The downside, however, is that governments are more exposed to lobby pressures, and might not be able to liberalise as much as they had initially intended, or as they could have in a multilateral forum (where they have the advantage of blaming international peer pressure). For this reason, some voices are being raised in the US Congress against FTAs, arguing that PTAs put US legislative and executive bodies under too much domestic pressure.

In sum, while history has shown that it could be argued that PTAs act as substitutes for multilateralism, the reverse is *not always* true. Countries may choose to supplement multilateral interaction with bilateral/regional agreements where (e.g., in new trade areas such as investment) and when a consensus cannot be reached at the multilateral level. Evidence suggests that there is no strong empirical link between multilateral and regional agendas, despite frequent allegations of the kind. For example, the US Trade Representative Robert Zoellick wrote a famous op-ed after the 2003 Cancun Ministerial, suggesting that 'America will not wait for the won't do countries' and will 'move towards free trade with can-do

31 Jayant Menon, 'Bilateral Trade Agreements and the World Trading System', Asian Development Bank Institute Discussion Paper No. 57 (28 November 2006), at p. 8.

countries'.[32] The US had, however, already started most of its bilateral negotiations at the time, and these would probably have continued even if the Cancun Ministerial had been a success. Lack of progress in multilateral negotiations is more often a convenient *a posteriori* justification than a motive for moving trade policy in a bilateral direction.

III. Bilateral/regional agreements are the result of a political arbitrage between free trade and protectionist views, only partially driven by economic principles

The decision to negotiate a trade agreement of any kind is based on a political arbitrage between free trade and protectionist views. Here again, multilateral and bilateral/regional agreements are not fundamentally different. However, bilateral/regional agreements are more flexible than their multilateral counterparts. This makes the political cost of an arbitrage in favour of free trade lower in this context for two main reasons: (1) sensitive sectors can be carved out of the agreement (defensive interests); and (2) new disciplines can be promoted in some sectors of high interest where multilateral consensus is yet to emerge (offensive interests). In other terms, opposition to the conclusion of the agreement is likely to be lower while support is higher.

From an economic perspective, this level of political facility drives the agreement to far less than an optimal conclusion: interests of the most vocal lobbyists prevail over consumers' interest at large. This is already the case at the multilateral level, but even more so at the bilateral/regional level because of built-in flexibilities. Thus, while some political economy concepts (e.g., free trade), backed by economic theory (e.g., the theory of comparative advantages) are at the centre of the decision to negotiate trade agreements, in practice, political compromises can nullify or impair the positive economic impact of the agreements. This, in turn, supports the opponents of free trade in making their point that free trade can be harmful, creating a vicious circle: more concessions are likely to be made to groups representing defensive interests and, in the end, trade diversion overshadows trade creation.

A. A political decision with a varnish of economic rationale

The hypothesis that bilateral/regional trade agreements are driven by economics could be empirically tested. However, it is unclear what economic theory recommends as even PTAs have their fervent opponents and supporters among economists. A useful step was made in the 1950s, when Jacob Viner, followed

32 Robert B. Zoellick, 'America will not Wait for the Won't Do Countries', *The Financial Times*, 22 September 2003, p. 23.

by James Meade, articulated the concepts of trade creation and trade diversion.[33] Since then, theories of economic integration have flourished[34] and a certain number of conditions, which help trade creation effects outweigh trade diversion effects, have tentatively appeared. In the 1990s, the belief remained, however, that traditional trade theory did not adequately explain the attractiveness of bilateralism/regionalism (the theory was, incidentally, likewise unable to sufficiently explain the potential benefits of non-discriminatory trade liberalisation). As a result, a new trade theory began to explore the implications of imperfect competition in an increasingly integrated world economy.[35] Subsequently, a distinction was also made between deep and shallow integration.[36] Did, however, this vast economic literature and quest for the optimal FTA influence policy makers at any stage?

Jacob Viner intuitively provided an answer to this question when he concluded that:

> [Customs unions] are unlikely to yield more economic benefit than harm, unless they are between sizable countries which practice substantial protection of substantially similar industries. But customs unions of this character have always been extremely difficult to negotiate in a nationalistic and protectionist world.[37]

A few decades later, Viner's conclusion remains valid: without regard to economists' recommendations, countries have continued to negotiate PTAs with countries of different sizes and exclude sensitive sectors when doing so. Similarly, the model of deep integration is rarely adopted, despite the potentially higher welfare gains.[38] Put another way, most PTAs remain based on a model of 'shallow' integration. The best illustration of this disregard for economics (and any form of guideline for the conclusion of PTAs) is that of the WTO Committee on Regional Trade Agreements. While this committee was set up to review all agreements of which the WTO is notified, it has never properly functioned, and neither has it adequately ensured the adherence of PTAs to WTO rules.[39] These rules, as contained in Article XXIV of the GATT, were designed to ensure that bilateral/regional trade agreements facilitated trade between the contracting parties without raising barriers

33 Jacob Viner, *The Customs Union Issue* (New York: The Carnegie Endowment for Development, 1950); and James E. Meade, *The Theory of Customs Unions* (Amsterdam: North Holland, 1955).

34 See, e.g., the literature review in Alfred Tovias, 'A Survey of the Theory of Economic Integration' (1991) 15(1) *Journal of European Integration* 5–23.

35 Dean A. DeRosa and John Gilbert, 'Technical Appendix: Quantitative Estimates of the Economic Impacts of US Bilateral Free-Trade Agreements', Background Paper Prepared For the Conference on Free-Trade Agreements and US Trade Policy, Washington, DC, Institute for International Economics, 7–8 May 2003, at p. 4.

36 *Ibid.*, at p. 5. 37 Viner, above n. 33, at p. 135.

38 See, e.g., the recommendations made in David Evans *et al.*, *Assessing Regional Trade Agreements with Developing Countries: Shallow and Deep Integration, Trade, Productivity, and Economic Performance*, Report prepared for DFID by the University of Sussex (March 2006), DFID Project No. 045881.

39 See commentary by Simon Lester and Bryan Mercurio at www.worldtradelaw.net.

to trade with the rest of the world. Such rules transcribed an economic rationale that would be theorised just a few years later. But here again, members treated the implementation of these rules as a political issue (despite their logic and economic merits), and no agreement could ever be reached on their interpretation e.g., on the portion of trade that should be fully liberalised in PTAs.[40]

In sum, if bilateral/regional trade agreements were totally driven by economics, they would probably have a different shape or coverage and involve different groupings of countries. Members of the WTO would also be less fearful of the conclusions of the Committee on Regional Trade Agreements and decisions would remain mostly political. However, political and economical doctrines are intertwined. To quote John M. Keynes:

> [T]he ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed, the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slave of some defunct economist.[41]

History is composed of a succession of phases of protectionism and trade openings with trade policies (including decisions to negotiate bilateral/regional agreements) varying according to the changes in political regimes and majorities of the day. For example, Louis Napoleon Bonaparte (Napoleon III) was exposed to the liberal model while in exile in England and, shortly after the restoration of the French Empire, he amended the Constitution so as to gain the power to conclude BTAs with legal effect.[42] This was the origin of the 1860 French trade agreement with England and the 'free trade epidemic' that soon swept Europe. At the time, the opposition in France treated this move toward liberalism as a 'coup d'Etat douanier', revealing the strong ideological content of Napoleon III's decision.[43] A few years later, the next shift to protectionism in Europe also coincided with a change in political leadership (Bismarck in Germany). It was influenced less by liberal economic theories (Friedrich List, who suggested the use of tariff protection to allow Germany to catch up with England – free trade remained the objective, but protectionism was the way to reach it).[44] This fight between advocates and opponents of free trade goes on and since then, bilateral/regional trade agreements have been used, more or less successfully, by those in the

40 The WTO Members did agree, however, to clarify the rules on regional trade agreements as part of the DDA, and adopted a new transparency mechanism in 2006.

41 John M. Keynes, *The General Theory of Employment, Interest and Money* (New York: Harcourt, Brace and Company, 1936), at p. 383.

42 Article 6 of the 14 January 1852 Constitution and Article 3 of the 25 December 1852 Sénatus-consulte 'portant interpretation et modification de la Constitution du 14 janvier 1852' (texts available at www.conseil-constitutionnel.fr/textes/constitution/c1852.htm).

43 Pierre Bezbakh, 'Napoleon III et le libre-échange', *Le Monde Economie*, 2 December 2003.

44 Friedrich List, *The National System of Political Economy* (London: Longmans, Green and Co, 1909) (translated 1885 from German, first published in 1841).

free trade camp to anchor their reforms and bind future governments. For example, the NAFTA helped the Mexican government commit its country to liberalism.

As any change in either the terms or volume of trade has corresponding effects on every person's life in a country affected by the change, the liberalisation of trade (whether unilateral, bilateral/regional or multilateral) creates both winners and losers. The decision to liberalise trade and negotiate PTAs is necessarily thus a political one. In the US, this has in turn translated into the necessity for the President to obtain a delegation of power from Congress to negotiate trade agreements. Given the multiplicity of views on trade, the renouncement of Congress of its constitutional right to amend trade treaties was crucial to enable the President to make a political decision and conclude agreements. Debates concerning the renewal of the Trade Promotion Authority (previously known as 'fast-track') continue to reveal the lack of unanimity on the economics and politics of trade.

B. Trade diversion and the domino effect of bilateral/regional trade agreements

Because of the economic controversy over the desirability of trade liberalisation, bilateral/regional trade agreements have also been used to promote protectionism and segment markets. The most famous example is probably the 1834 *Deutscher Zollverein* (German customs union) where under the Prussian leadership, German states established a customs union with the aim of facilitating trade among themselves whilst simultaneously allowing the adoption of high common external tariffs to protect German infant industries from foreign competition, in particular that of England. Trade diversion was clearly the short-term objective, although in List's mind economic catch up would eventually facilitate free trade.[45] With this historical precedent in mind Article XXIV(4) of the GATT stipulates that 'the objective of a customs union or a free trade agreement 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 absence of institutionalised reviews of modern FTAs contributed, however, to the survival of trade diversion effects.

These trade diversion effects, whether as the objective or just an undesired result of a bilateral/regional trade agreement, are the main factor for the proliferation of these agreements.[46] This is, in a way, an example of economics having the last laugh in that even where a bilateral/regional agreement is initially concluded for non-economic reasons, countries not originally party to the agreement will still have an incentive to join the agreement or conclude side agreements to restore market access

45 *Ibid*., Book II, Chapter XXVI 'Customs Duties as a Chief Means of Establishing and Protecting the Internal Manufacturing Power'.

46 David Lazer, 'The Free-Trade Epidemic of the 1860's and Other Outbreaks of Economic Discrimination' (1999) 51(4) *The Journal of World Politics* 447–83.

(and remedy the effects of trade diversion). This is what some authors have called a 'domino effect'.[47] History abounds in examples of this effect of PTA proliferation. The above-mentioned *Zollverein* is a good illustration of the phenomenon as initially, only a few German states had formed the customs union, but the threat of trade diversion to exporters within the *Zollverein* led to the eventual adhesion of all German states.[48] In the 1860s, the conclusion of a PTA between Europe's two major powers (France and England) led to a 'free trade epidemic'. In modern history, the progressive enlargement of the European Economic Community (EEC) and its subsequent transformation into the EU is yet another example, for although Britain initially stayed out of the EEC to maintain political independence, it eventually sought membership when its share of intra-European trade declined as a result of trade diversion. What began with only six original members now has twenty-seven.[49] The 2000 European Union–Mexico Free Trade Agreement had similar roots: as a result of the NAFTA, the share of the EU in Mexican trade dropped from 10.6% in 1991 to 6.5% in 1999, and the average Mexican tariffs on EU goods stood at 8.7%, compared to only 2% on US goods. The EU responded by concluding an PTA with Mexico, and less than a year after that agreement had entered into force, Mexican exports to the EU had grown by 40%, and EU exports to Mexico by 60%.[50] In other words, the trade diverting effects of the NAFTA on the EU had been restricted through the latter's proactive response.

The proliferation of PTAs has, however, had very different effects at different times in history. In the nineteenth century, the proliferation of PTAs resulted in a general lowering of tariffs because of the MFN clause contained in the agreements. Modern PTAs do not include an MFN clause but are instead conceived as exceptions to the MFN treatment granted by the WTO. Thus, the proliferation of PTAs does not necessarily offer a harmonising effect. On the contrary, the 'spaghetti bowl' effect prevails, and contributes to the increased differentiation of treatment among countries. This effect is further aggravated by the complexity of rules contained in modern PTAs, which no longer simply concern tariffs, but are rather comprised of a complex set of rules and disciplines on trade and trade-related issues. This proliferation of rules has itself come at the price of a reduction in the security of transactions and additional administrative burdens for exporters (e.g., to comply with different rules of origin). Eventually, it is likely that this will lead exporters operating in world markets to ask for a further harmonisation of rules – a 'multilateralisation of regionalism'.[51] While the WTO (multilateralism) will have an important role to play toward this end, bilateral/regional trade agreements will

47 Richard E. Baldwin, 'Multilateralising Regionalism: Spaghetti Bowls as Building Blocs on the Path to Global Free-Trade' (2006) 29(11) *The World Economy* 1451–518.

48 Lazer, above n. 46, at 479. 49 *Ibid.*, at 480.

50 Pascal Lamy, 'La politique commerciale envers l'Amérique Latine : Priorité de l'Union européenne', Speech, Casa de America, Madrid, 26 July 2001.

51 See, e.g., Baldwin, above n. 47.

not disappear. The jury is still out on many issues where the US and EU positions remain irreconcilable. Since provisions contained in the agreements concluded by the US and the EU tend to be uniform, a likely intermediary step could therefore be the polarisation of the world through the use, by each trade superpower, of a web of bilateral/regional trade agreements. Enlargement of such spheres of influence will, however, take time, and the EU experience shows that the next stage of 'deepening' trade agreements will be a difficult one.

In sum, bilateral/regional agreements are here to stay, and the proliferation of FTAs is likely to continue at a fast pace.

IV. Bilateral/regional agreements are primarily driven by political considerations and are an instrument of foreign policy

The 'domino effect' is the revenge of economics. It also reveals a fundamental inequality among countries *vis-à-vis* bilateral/regional trade agreements and explains why a typology of these agreements does not make sense: namely that the proliferation of bilateral/regional trade agreements is driven by the race for leadership for some, and the fear of exclusion for others. In other words, the motives behind PTAs are often quite different for two parties to the same agreement. This is only a partial revenge, however, as the 'domino effect' does not explain why regional trading powers in the first place decide to negotiate trade agreements, nor, more importantly, how they choose their partners. It also does not explain the reason behind the use of bilateral/regional trade agreements between countries of the same economic size. Indeed, politics remains the main driver of FTAs both domestically and geopolitically.

A. The political objectives behind bilateral/regional trade agreements

In the period of history that pre-dates the introduction of trade agreements, trade provisions were included in navigation acts – understandably since freedom to trade was predominantly concerned with the access of foreign merchants to ports and the open use of the sea. Trade policy was an appendage to geopolitics, and vice versa, and the control of main navigation roads was seen as a strategic objective from both a military/security and commercial perspective. For example, in 1580, Portugal's loss of independence to Spain created a monopoly on trade in spices from the Indies. Without competition, Spain could raise European prices and shut the free-trading Dutch out of the market. Similarly, Prussia's main objective for the German *Zollverein* was to create a unified Germany under its political influence while its deliberate decision to exclude Austria from the customs union was a purely geopolitical move. Since then, trade policy and geopolitics have remained intertwined, but the strategic focuses have changed.

The best illustration of the geopolitical dimension of trade, and the role of bilateral/regional agreements, is the race for power between the EU and the US.

When the EU negotiates a trade agreement with Mexico, Chile, or MERCOSUR, it is partially to avoid trade diversion effects prompted by the similar negotiations of these states with the US (see above). Nonetheless, it is also a geopolitical decision:

> The success of MERCOSUR is in Europe's best interest. Let's remember the results of MERCOSUR: not so long ago, Brazil and Argentina were nuclear powers. With MERCOSUR, it is not the case anymore. Let's remember also the fundamental role played by MERCOSUR in the consolidation of democracy in the Southern Cone, for instance in Paraguay. The trade negotiations engaged by the EU with MERCOSUR fit into the frame: the objective is political. (. . .) During the last session of negotiations that took place in Montevideo at the beginning of July (2001), we presented concrete proposals to open our market to their industrial and agricultural goods and to their services. We could have waited because MERCOSUR was not ready. We choose to do it for political reasons. For posing a political act. (. . .) And this, a year before negotiations on the Free Trade of Americas Act (FTAA) is seriously discussed.[52]

Obviously, trade policy is no longer simply concerned with securing navigation routes, and neither is it only about reducing tariff protection. Instead, the trade policies of today appear to centre more on the race for leadership between the US and the EU to impose a set of rules (e.g., on competition, investment, and intellectual property) and standards (e.g., on agricultural products) on the rest of the world.[53] Bilateral/regional trade agreements have become the main vehicles of this competition to extend normative and economic influence much in the same way the US and the Soviet Union(USSR) vied to conclude bilateral/regional 'pacts' in order to extend their respective spheres of influence during the Cold War. The current proliferation of FTAs could be referred to as a real 'pactomania'.[54] Referring again to the FTAA, then European Commissioner Pascal Lamy warned:

> With the Pan-American zone, the US has an opportunity to impose its regulatory system to the whole continent, which would cause a serious problem to the EU. (. . .) We are in competition with the US. On agriculture, services, investment regimes, intellectual property, and public procurement, offers will escalate. Ultimately, the countries of the Southern Cone will need to decide which type of 'geo-economic-political' equilibrium they desire between the US and the EU.[55]

For the two major trading powers, the political importance of bilateral/regional trade agreements goes beyond the competition for regulatory leadership. For the EU,

52 Lamy, above n. 50 (Author's translation).

53 Olivier Cattaneo, *Quelles ambitions pour la politique commerciale de l'Union européenne?* (Paris: Institut Français des Relations Internationales, 2002), at pp. 22–3.

54 *Ibid.*

55 Pascal Lamy, 'Les règles de l'OMC doivent être revues', *La Tribune*, 14 May 2001 (Author's translation).

it is obvious as the Union itself is based on a single market, that is a model of regional deep trade integration. The initial objective of the EEC was to create economic solidarities among European countries (starting with steel and coal production) that would make another war between France and Germany 'not only unimaginable, but also technically impossible'.[56] In the mind of its founding fathers, like Jean Monnet and Robert Schuman, building Europe was building peace. Trade integration (free movement of goods, services, capital, and people) was just a means whereas political stability was the end. This original concept largely shaped the bilateral trade policy of the EU, and in particular the so-called 'neighbourhood policy' where economic integration is seen as a preparatory step to political integration for some, or a gauge of prosperity, stability and security for others.[57] Only recently, when the EU had integrated most of its like-minded neighbouring countries, could the Commission revert to an ostensibly more economically-driven bilateral/regional trade policy.

The organic peculiarity of the EU (not a sovereign state, but a union of countries, with common institutions and shared powers) makes its trade policy even more of a political tool. Indeed, the EU uses trade policy as a weapon to struggle for power abroad *and* domestically. Since 1970, trade policy has been the prerogative of the European Communities (EC); at the WTO or in bilateral trade negotiations, the EC represents its members and negotiates with a mandate. Qualified majority voting is used at the European Council upstream and downstream (i.e., one member alone cannot block the decision to conclude an agreement). In other fields of foreign policy, members have not transferred their powers, and unanimity is required. While the EU is a main actor on the WTO/trade scene, it is absent at the United Nations (UN) or Bretton Woods institutions (International Monetary Fund, World Bank). The helplessness of the EU was illustrated during the ex-Yugoslavia war and other major international political crises. As a result of these organic constraints, the European Commission has tended to use trade policy as a tool box for foreign policy: European FTAs and preferential schemes include provisions that far exceed the scope of (*stricto sensu*) trade policy.[58] For example, the new Generalised System of Tariff Preferences (GSP) requires, for additional concessions (GSP+), the ratification and effective application of 27 key international conventions on sustainable development and good governance. As another example, the Cotonou Agreement promotes, among others, democracy, transparent and accountable governance, the fight against corruption and bribery, social dialogue and respect for basic rights including gender equity, environment

56 See, e.g., the famous *Discours de l'horloge* given by Robert Schuman on 9 May 1950 at the Ministry of Foreign Affairs in Paris, France.

57 See, e.g., the Stability Pact concluded with the Balkan countries in 2001 (half of them have joined the EU already), or the European Neighbourhood Policy in place since 2004.

58 Olivier Cattaneo, 'La politique commerciale, fer de lance de l'action extérieure de l'Europe' (May–June 2002) 99 *Défense* 53–4.

protection, etc.[59] Thus, bilateral/regional trade agreements are a key foreign policy instrument for the EU, and at the same time an important instrument for domestic policy, extending the powers of the Commission *vis-à-vis* its members. For example, both the Amsterdam and Nice treaties extended the scope of trade policy to include intellectual property and services, and there was a similar attempt at the inclusion of investment in the prerogatives of the Commission under Article 133 of the EU Treaty.[60] In other words, motives behind the conclusion of trade agreements (including bilateral/regional) are only remotely trade related.

The US is in a different position. As a sovereign state, it has other instruments to promote foreign policy objectives. Bilateral/regional trade agreements can also be backed by other purely political treaties (e.g., on security). This did not, however, prevent the US from using PTAs as a foreign policy instrument. 'Compatibility with US interests' is one of the six factors that guide the discussion in selecting future PTA partners: 'A potential PTA partner is examined for its compatibility with broad US interests, including its support for US foreign policy positions'.[61] This compatibility criterion has proven prevalent in US trade relations and it is worth remembering that the first PTA concluded by the US since the creation of the GATT was with Israel in 1985 – an agreement that commentators observe has a special importance to US foreign policy that extends far beyond its trade coverage.[62] PTAs have been used, more recently, as an instrument of the 'war on terror' and a reward for countries supporting US efforts in Iraq (the 'coalition of the willing'); about half of the countries selected by the US for PTA negotiations supported the US policy in Iraq.[63] The US entered into an agreement with Australia (who is also part of the coalition) but not with its neighbour New Zealand (who is not part of the coalition and furthermore has an anti-nuclear position that caused friction with the US).[64] Summarising the motives behind the PTA with Morocco, the USGAO noted:

> Although a US–Morocco FTA would have a minimal trade benefit to the United States, one USTR official stated that this FTA would further the administration's goal of promoting openness, tolerance, and economic growth across the volatile Middle-East. Morocco, a moderate Muslim country, also signaled its readiness to enter into a comprehensive FTA by demonstrating its willingness to liberalize its economy and make domestic reforms.[65]

59 Olivier Cattaneo and Christian Pitschas, 'The Link Between the Trade and Development Policies of the European Union' (Autumn–Winter 2005) 3 *The European Enterprise Journal* 12–8.

60 Cattaneo, above n. 53, at p. 48. 61 USGAO, above n. 6, at p. 10.

62 Howard Rosen, 'Free-Trade Agreements as Foreign Policy Tools: The US–Israel and US–Jordan PTAs', in Jeffrey J. Schott (ed.), *Free-Trade Agreements: US Strategies and Priorities* (Washington: Institute for International Economics, 2004), pp. 51–77.

63 Murray Gibbs and Swarnim Wagle, 'Fear of Exclusion: The Driving Force Behind North-South PTAs', UNDP Discussion Paper (2005), at pp. 6–7.

64 *Ibid.* 65 USGAO at p. 12.

Similarly, for the United States–Bahrain Free Trade Agreement, the USGAO concluded: 'Although Bahrain represents a small share of US trade, an PTA with this US ally and moderate Muslim nation would support US security and political goals by fostering prosperity in the region'.[66] Of course, motives behind PTAs are just as diverse as US foreign policy objectives; for example, the US could negotiate PTAs with members of the G20 with a view to weaken this coalition.[67]

Similar to Europe, these agreements can also serve *domestic* policy objectives. For example, the agreement with Mexico was partially aimed at containing migration pressures and the insistence of the new majority in Congress in 2007 to include more ambitious labour provisions in PTAs is meant to put pressure on domestic reforms. The vote on the Trade Promotion Authority is therefore only partially driven by trade considerations. But, bilateral/regional trade agreements are just one of the available instruments that serve these domestic and foreign policy objectives. For example, unilateral trade preferences are also driven by political factors, as illustrated by the new denomination of the 2002 Andean Trade Promotion and Drug Eradication Act (previously known as the Andean Trade Preference Act first enacted in 1991 to combat drug production and trafficking in Bolivia, Colombia, Ecuador and Peru). Unilateral trade sanctions on Libya and Cuba have also long served strictly political objectives.

The use of bilateral/regional trade agreements as instruments of foreign policy is not, however, the privilege of the US and the EU. In recent years, the multiplication of PTAs in Asia has been one of the responses to the 'China challenge' with its economic (e.g., maintaining the capacity of neighbouring countries to attract foreign direct investment) and geopolitical dimensions (e.g., stability in the region).[68] Taiwan, thus far excluded from major regional agreements (such as ASEAN), is now urging the US to conclude a bilateral PTA:

> Taiwan's trading partners are looking for the leadership in the US before considering the negotiation of FTAs with Taiwan. As a consequence, Taiwan risks becoming isolated and weakened economically. Taiwan is an important force in maintaining peace and stability in the Asia Pacific. A marginalised and economically weakened Taiwan will not be in a position to contribute to the long-term stability of the region.[69]

Conversely, China has recently become active in negotiating PTAs to isolate Taiwan. Other motives behind the Chinese PTAs include the decision by PTA partners not to

66 *Ibid.*, at p. 11. 67 Gibbs and Wagle, above n. 63, at p. 7.

68 Christopher Findlay, Mohd Hafleh Piei and Mari Pangestu, 'Trading with Favorites: Risks, Motives and Implications of PTAs in Asia Pacific', Background Paper to the Pacific Economic Co-operation Council (PECC) Trade Forum, 22–23 April 2003, Washington, DC, at p. 12.

69 Sheng-Cheng Hu (Minister of State and Chairman, Council for Economic Planning and Development, Executive Yuan), 'Taiwan's Economy and the Role of a US–Taiwan PTA', Speech to the Annual Board of Directors of the US–Taiwan Business Council (28 November 2006), p. 3.

apply provisions contained in its terms of accession to the WTO, which permit WTO members to impose restrictions against China that would otherwise be prohibited by WTO rules, including provisions specific to the 'non-market economy status' of China.[70] For instance, Singapore has used its PTAs as a 'door-opener' to gain access to 'other strategic, security-related agreements'.[71] Energy security is also a possible motive: for example, Japan is seeking security of supply commitments in its PTA negotiations with Indonesia, a member of the Organization of Petroleum-Exporting Countries (OPEC).[72] In India, foreign policy considerations prevail. Similarly, on the African continent, PTAs with little substance or economic sense proliferate, raising serious implementation issues.

If PTAs were not primarily driven by politics, how could we explain the negotiation of an agreement between Singapore and Kuwait, Sri Lanka and Iran, Taiwan and Nicaragua, etc.? In the context of proliferation, both rational and irrational fear of exclusion and mimesis drive new negotiations. Sally summarises:

> [Most PTAs] tend to be driven by foreign policy aspirations, but with justifications that are all too often vague, muddled and trivial, having little relevance to commercial realities and the economic nuts and bolts of trade agreements. This can amount to little more than symbolic copycatting of other countries' FTA activity and otherwise empty gesture politics. In such cases economic strategy is conspicuous by its absence.[73]

B. The imbalance of powers resulting from the prevalence of political objectives

The fact that most PTAs are driven by politics has important consequences. First, it is difficult to assess the results – and even more so the success – of a PTA. Too often commentators judge PTAs in light of their economic effects, when the objective of the parties could have been purely political. How does one measure, for instance, the contribution of a trade agreement to the political stability of a region? On the other hand, the absence of economic evaluation helps to hide the imbalance of some agreements and the uneven sharing of their costs and benefits. Also worth noting is the fact that foreign policy ambitions and geopolitical power vary significantly from country to country – the effectiveness of PTAs as a means of achieving foreign policy objectives thus varies accordingly. While merely political gesticulations for some, PTAs can be an effective means of imposing extra-territorial reforms for others. This again can lead to significant imbalances.

Before reciprocity was introduced in bilateral/regional trade agreements, trade concessions were made unilaterally, either voluntarily or forced through so-called

70 Gibbs and Wagle, above n. 63, at p. 4

71 Razeen Sally, 'FTAs and the Prospects for Regional Integration in Asia', European Centre for International Political Economy (ECIPE) Working Paper No. 1, Brussels (2006) at p. 5.

72 Gibbs and Wagle, above n. 63, at p. 6. 73 Sally, above n. 71, at p. 6.

'unequal treaties'. At the time, the link between geopolitics and trade was obvious: unequal treaties were signed with China as a result of the First Opium War (e.g., the Treaty of Nanking, 1842); similar treaties were concluded with Japan (between 1854 and 1858) and Korea (between 1876 and 1910). The objective was for the European powers to gain access to Asian ports and exhort lower tariffs for their exports. Similarly, Britain obtained important trade concessions from the Ottoman Empire in consideration for its military assistance, for example against Syria (Treaty of Balta Liman, 1838). Modern agreements cannot be compared to these instruments of imperialism – nonetheless, despite the introduction of the concept of reciprocity, some imbalances remain. While the regional or world trade superpowers can choose conditions attached to a PTA (rule-makers), smaller countries often have no choice but to accept these conditions (rule-takers) or run the risk of exclusion.

In their analysis of the process of accession to the WTO, Evenett and Primo Braga concluded that, since 1995, 'the price of joining the WTO is steadily rising, (. . . and) now includes commitments that go beyond the GATT/WTO agreements'.[74] The question is whether the same logic applies to PTAs, in other words, whether the price to pay for PTAs (scope of commitments) increases with time, as the fear of exclusion and diversion effects reduce the bargaining power of a country. A positive answer would give a premium to the first mover(s), and explain the 'FTA epidemic'. In practice, however, there is no such evidence: for example, not all FTAs negotiated by the US included comparable (if at all) provisions on labour or environmental standards, and the content of the PTAs has fluctuated more with the majority in Congress at the time of negotiation than with time. On the other hand, it remains true that the US and the EU, as noted earlier, have 'pet' provisions that appear in all their PTAs (e.g., geographical indications for the EU, and TRIPS+ provisions on patents for the US). With time and the multiplication of non-tariff barriers to trade, PTAs have also become more sophisticated: for example, in its new 'Global Europe' strategy, the EU called for a 'new generation' of EU competitiveness-driven PTAs that would include stronger rules in 'new trade areas' of importance to the EU, notably intellectual property, services, investment, public procurement and competition.[75] In practice, it also appears that the EU expects from its future partners a level of concession at least equal to the one conceded to the US in earlier agreements: for example, the Central America–Dominican Republic–United States Free Trade Agreement (CAFTA–DR–US), which was the starting point of the European Economic Partnership Agreement (EPA) negotiations in the Caribbean region. Thus, the cost of PTAs is increasing with their proliferation, but does not discriminate between first movers and late comers.

74 Simon J. Evenett and Carlos A. Primo Braga, 'WTO Accession: Lesson from Experience', World Bank Trade Note Series No. 22 (6 June 2005), at p. 2.

75 European Commission, above n. 1, at p. 7.

Reciprocity in PTAs is largely illusory: concessions are reciprocal, but the 'anchor' country can choose the level and content of these concessions, and impose them on any country willing to join its PTA web. Often, in North–South agreements, the developing country also enters into the agreement with a view to ensuring the maintenance of tariff preferences that the anchor country had previously granted unilaterally. In other words, reciprocity consists in consolidating *old* concessions for the anchor and making *new* concessions for the developing country. The current negotiation of the EPAs is a good example: required by the WTO to reform its system of preferences in favour of the Africa Caribbean Pacific (ACP) countries, the EU offered to negotiate a regional trade agreement (RTA) with each sub-section of the group.[76] While these agreements would restore reciprocity and compatibility with WTO law, many critics suggested that the ACP countries were the only ones paying the cost of these new regional agreements.[77] In August 2006, the US Administration also launched a review of its GSP programme, seeking comments on eligibility criteria and competitive need limitation (CNL) waivers.[78] The threat of possible removal of GSP eligibility might create an incentive for some countries to negotiate a PTA with the US with a view to preserving their access to the US market; these countries would, however, have to reciprocate the US concessions.

At different stages of development, countries seem to have different needs, which are reflected in the sophistication of the bilateral/regional trade agreements they negotiate. The problem, with the asymmetry of the bilateral/regional trade negotiations, comes when agreements negotiated by the US or the EU might not best suit the needs of their partners. At an early stage of industrialisation and development in the nineteenth century, England negotiated PTAs that merely attempted to secure market access (see Part II above). With the 'new generation' of bilateral/regional trade agreements, market access is just one part of the deal and for most developing countries, participation in a 'new generation' agreement requires significant regulatory reforms, e.g., in the fields of competition, investment or intellectual property laws. Some of these reforms go further than what is required by the WTO and can be costly, e.g., the establishment of a sophisticated system of registry and monitoring of geographical indications. Here again, the cost of joining a 'reciprocal' agreement is uneven as the 'anchor' country does not need to reform in any way, given that its own regulatory framework serves as a model. PTAs of the kind negotiated by the European nations in the 1860s would therefore be better suited to the needs of developing countries, as current North–South FTAs are trapped in the paradox of being used by developed countries to go further than the

76 See, e.g., www.ec.europa.eu/trade/issues/bilateral/regions/acp/index_en.htm, or www.acp-eu-trade.org for further details about the EPAs.

77 See, e.g., www.epawatch.net, which contains documents prepared by state and non-state actors, and shows the diversity of views and concerns about the EPA negotiations.

78 Office of the USTR, 'Administration to Review Whether to Continue Trade Benefits under the GSP Program', *Press Release*, 7 August 2006.

WTO when developing countries already have problems implementing the reforms necessary for full compliance with their multilateral commitments.

South–South and North–North agreements should suffer less from this imbalance. Here again, however, the largely political dimension of bilateral/regional trade agreements alters this logic: a transatlantic PTA would make most sense from an economic perspective, but despite numerous attempts and initiatives, the political gaps between the US and the EU have not been easily bridged. In the South, the number of bilateral/regional trade agreements has flourished, but political will has often been lacking at the implementation stage. Most of these agreements have thus remained empty shells (e.g., the Greater Arab Free Trade Area (GAFTA), where the principle of free trade was adopted, but export licenses are hardly ever granted). In sum, given the political nature of PTAs, it is not surprising that the best results are obtained where *political integration* is as much an objective as *economic integration*. This helps to explain the success of European economic integration, both as an instrument of growth/development and political stability in the region.

V. Conclusion

There is no straight answer to the original question 'Why do countries conclude PTAs?' and the multiplicity of objectives assigned to PTAs makes a typology of the agreements largely impossible. It seems clear, however, that the political economy of bilateral/regional trade agreements revolves more around politics than economics. If this were not the case, the shape of the agreements and the participating countries themselves would be different – for example, the transatlantic partnership would be reinforced and most African RTAs would either disappear or be more thoroughly implemented. This does not exclude a role for economics in the decision-making process as the fear of exclusion and that of the negative trade diversion effects of PTAs largely explain the current proliferation of agreements. An agreement concluded on political grounds can give birth to a stream of agreements driven by economic considerations.

The fact that bilateral/regional trade agreements are primarily a political phenomenon explains the fact that they might be fashionable one day, and in disgrace the next. The free trade epidemic that Europe experienced in the 1860s was followed by a complete return to protectionism. In more recent US history, the arrival of the George W. Bush Administration coincided with an acceleration of the negotiation of FTAs in the name of the so-called 'competitive liberalisation'. Similarly, the content of FTAs can change with the majority in Congress – after the Democratic Party won the 2006 congressional elections, it asked for a re-negotiation of the FTAs with Peru and Colombia to include provisions on labour standards.

Despite all criticisms and fears, bilateral/regional agreements are here to stay. From an historical perspective, multilateralism is the exception rather than the rule. Taking a provocative stance, one could say that the GATT 1947 was only a hiccup of history, and probably the largest PTA the US has ever concluded. From the

twenty-three original contracting parties of the GATT to the 150 members of the WTO, the practicality of multilateralism has diminished. The MFN clause that most commentators associate today with the multilateral trading system (and the WTO) was originally embodied in bilateral/regional trade agreements but nowadays, these agreements are perceived as exceptions to the MFN clause. This fundamental change has affected the desirability of PTAs: in the 1860s, their proliferation resulted in a virtuous circle of trade liberalisation, because they embodied an MFN clause. Today, however, the proliferation of bilateral/regional trade agreements creates a vicious circle, in which discrimination becomes the rule and the MFN treatment in the WTO a 'least-favoured treatment' of sorts. Accepting that the GATT was the largest PTA ever concluded and that every single agreement should include an MFN clause[79] would restore some equity and positive spin. That would require, however, a complete revolution of the system.

The continuous use of bilateral/regional trade agreements in history should not mask the fact that these agreements have dramatically changed over time. The suppression of the MFN clause is not their only mutation. Partially, the agreements changed with the needs of the trading nation: in the 1860s market access was the central goal (the opening of ports and the reduction of tariffs). Today non-tariff barriers play a more important role. It is common practice that modern PTAs tackle those barriers. Sometimes, however, countries use trade agreements to pursue objectives that are far removed from trade itself. As a result, these agreements can be poorly suited to the development needs of their poorest participants. The main problem here is that trade facilitation has the potential to equate to the adoption of more sophisticated rules and bodies to supervise the implementation of the rules: it is not only about removing barriers, but also adopting new laws or creating new administrative bodies. This requires significant technical assistance. If bilateral/regional agreements are to make sense and not be confined to political gesticulation, they should be accompanied by the transfer of technical and financial means that would help their implementation and enforcement. It should be remembered that the GATT, if treated as the largest PTA ever concluded by the US, was accompanied by a Marshall Plan and vast transfers of wealth to Europe. Similarly, the European integration was a success because of internal transfers in favour of lagging regions (European Regional Development Fund). The main challenge is therefore to develop a method of monitoring aid for trade in bilateral/regional agreements rather than exclusively focusing on multilateral issues, given that PTAs often demand much more extensive effort than do the WTO agreements from developing countries.

79 Often, the MFN clause is misinterpreted: it applies only to contracting parties to an agreement. For example, if the US concludes a PTA with Israel, and subsequently concludes a PTA with Canada, the application of the MFN clause would require that the US applies to both countries the most favourable conditions contained in either of the treaties. It does not mean that the US would have to extend any of these treatments to the rest of the world. Similarly, the MFN clause in the GATT applies only to WTO members, but the quasi-universal membership creates some confusion.

4

Bilateral and plurilateral PTAs

DAVID EVANS*

I. Introduction

The immense level of international effort being devoted to free trade agreements (FTA) negotiations shows no sign of abating. Negotiating PTAs has been elevated from a sideshow to the World Trade Organisation (WTO) to centre stage in many countries' trade policies. The halting pace of the Doha Round has increased the pressure to find alternatives. Many of the obvious and easy deals and partnerships have been formed, but the search for new partners continues.

A significant portion of recent PTA activity is directed at negotiating plurilateral PTAs. This is nothing new. Many of the best-known and most successful PTAs are multipartite unions, such as the European Union (EU) and North American Free Trade Agreement (NAFTA). Likewise the phenomenon of the 'hub and spoke' pattern of agreements is also well recognised, whereby an established 'hub' such as the EU seeks out separate PTAs with a number of 'spoke' countries.

An examination of a number of recent plurilateral PTA negotiations, however, reveals that they do not fit so easily into this pattern. There seems to be a growing tendency to negotiate plurilateral PTAs amongst more tenuous groupings with looser underlying linkages. Some involve disparate countries that are unlikely to ever have the cohesion or concentration to operate as a hub. Others may bear a certain resemblance to the 'hub and spoke' pattern, but on closer examination show significant differences resulting from the fact that the 'hub' or the 'spoke' is comprised of a group of countries that is still in the process of pursuing internal economic integration at the same time as it is negotiating externally with third countries.

These 'new generation' plurilateral PTAs pose new complexities and challenges. Academic writing has tried to keep apace. A smorgasbord of food-related metaphors has emerged, and whether the preference is for Italian (spaghetti) or Asian (noodles), the general view is of a bowl beginning to overflow. Attempts are made to grapple with the important but complex question of whether this constitutes a building bloc or stumbling bloc to global economic well being. Analysis in that

* The views expressed in this Chapter are those of the author alone and not of the New Zealand Ministry of Foreign Affairs and Trade.

context, understandably, focuses on qualitative analysis of the nature and scope of PTA obligations.

However there are also more practical issues and complexities to address in the context of these 'new generation' plurilateral PTAs. How are such agreements to be negotiated? How are they to be structured so as to best reflect the negotiating objectives of the parties? How can differing levels of ambition and development be accommodated? How should existing and overlapping PTAs be handled? This chapter seeks to provide an initial examination of some of these issues, and starts to explore some options for addressing them.

II. The emergence of a 'new generation' of plurilateral PTAs

A. Traditional plurilateral PTAs

Plurilateral PTAs[1] constitute almost half of all PTAs notified to the WTO.[2] Indeed, some of the best-known PTAs, such as the NAFTA, the EU[3] and the European Free Trade Association (EFTA) are plurilateral. These long-established PTAs are characterised by close geographic proximity, and a reasonably high degree of economic (and in the case of the EU in particular, political) integration. Liberalisation under these traditional plurilateral PTAs tends to be broad in scope and run deep in terms of the level of commitments undertaken.

It is also clear from looking at a list of existing PTAs, that a substantial subset of plurilateral PTAs involve negotiations between a 'pre-existing bloc' of countries, such as the EU or EFTA, and a third country. These types of PTAs fall under the rubric of 'hub and spoke' agreements. The pre-existing bloc of (traditionally highly integrated) countries is the 'hub' that negotiates PTAs with other countries outside the sphere of the more integrated bloc, the 'spoke'.

The EU is the most prolific practitioner of this type of hub and spoke PTA. It has concluded over twenty PTAs with third countries ranging from Bulgaria and Norway to Egypt, South Africa and Chile.[4] Closely following (and in some respects shadowing) the EU is EFTA, which has concluded thirteen PTAs with third

1 The term 'plurilateral PTA' is used in this chapter to mean a free trade agreement or customs union with more than two parties. The term is used in contrast to bilateral PTAs, which are PTAs with only two parties. The term 'plurilateral' is used rather than 'regional' as a number of the 'new generation' plurilateral PTAs discussed in this chapter reach beyond regional boundaries.

2 See 'Bilateral/Regional Trade Agreements Notified to the WTO', at www.worldtradelaw.net.

3 The EU is, of course, much more than simply a 'plurilateral PTA', however for the purposes of this chapter the term is used as useful shorthand. In the case of trade in goods, the EU comprises a customs union rather than a PTA. As we shall see, this affects the structure of PTAs concluded between the EU and third countries.

4 The EU has concluded similar agreements with: Algeria, Andorra, Bulgaria, Chile, Croatia, Egypt, Faroe Islands, Macedonia, Iceland, Israel, Jordan, Lebanon, Mexico, Morocco, Norway, OCTs, Palestinian Authority, Romania, South Africa, Switzerland, Liechtenstein, Syria and Tunisia.

countries both inside and outside Europe.[5] Indeed, in combination, the hub and spoke PTAs of the EU and EFTA account for just over one-fifth of all PTAs notified to the WTO and 40 per cent of all notified plurilateral PTAs.

A characteristic of these traditional plurilateral hub and spoke agreements is the degree of pre-existing integration of the 'hub'. As will be discussed in the next section, the intention of such 'hubs' is not to further liberalise amongst its own members. The intention, rather, is to offer certain trade preferences to a third country, in return for reciprocal trade preferences offered to the hub.

In many senses, then, this traditional type of hub and spoke agreement resembles a bilateral PTA, more than a truly plurilateral agreement. The negotiation takes place between two main 'actors' (the hub and the spoke), rather than an array of countries each negotiating solely on its own behalf,[6] and rights and obligations generally flow bilaterally, not multi-directionally between all parties to the PTA. The members of the pre-existing bloc (the hub) do not take on additional obligations *vis-à-vis* one another, only *vis-à-vis* the third country (the spoke).

B. Newer trends

It is widely recognised that the last decade has witnessed a surge in PTA negotiations, both bilateral and plurilateral.[7] Figures recently released by the Asian Development Bank (ADB) are particularly striking. In 1995 only three PTAs notified to the WTO involved developing member countries of the ADB. By 2005 there were twenty-seven such agreements, forty-two more were being negotiated, and another 55 potential agreements were the subject of feasibility studies.[8]

The reason for this increase in PTA activity is partially explained by the slow pace of multilateral trade reform at the WTO, punctuated by high-profile failures such as the 2003 collapse of talks in Cancún, and the more recent break-down in mid-2006. And there is something of a 'domino' effect at play. As more countries engage in PTAs, the cost of staying on the sidelines increases.[9] Even countries that continue to advocate the benefits of multilateralism over bilateral or plurilateral alternatives have, out of

5 EFTA has concluded agreements with Bulgaria, Chile, Croatia, Macedonia, Israel, Jordan, Mexico, Morocco, Palestinian Authority, Romania, Singapore, Tunisia and Turkey.

6 Indeed, with respect to many areas of a negotiation, the 'hub' may have a single 'lead negotiator' that represents the interests of all members of the pre-existing bloc.

7 In fact, bilateral and plurilateral approaches to trade liberalisation have operated in tandem with multilateral approaches since the end of World War II. The dynamic between the two is complex. A recent article identifies a number of 'phases' over the last fifty years in which bilateral or plurilateral approaches to trade liberalisation have developed. See Richard E. Baldwin, 'Multilateralising Regionalism: Spaghetti Bowls as Building Blocks on the Path to Global Free Trade' (2006) 29(11) *The World Economy* 1451–518.

8 Asian Development Bank (ADB), *Asian Development Outlook 2006: Routes for Asia's Trade* (2006), at pp. 276–8, available at www.adb.org/documents/books/ado/2006/default.asp.

9 Baldwin also explains that as global tariffs are lowered, the small advantages created by relative tariff differentials matter more – another explanation for the recent surge in PTA activity. See Baldwin, above n. 7, at 1472.

necessity, focused increasingly on PTAs.[10] As the ADB bank figures indicate, in the new millennium this trend has been nowhere more evident than in Asia.

While the current ebb in multilateral approaches to trade liberalisation continues, the pressure to find alternatives increases. One outcome of this is a push for new and more ambitious plurilateral PTAs. A recent high-profile example of this was the decision by Asia Pacific Economic Co-operation (APEC) leaders in late 2006 to undertake a study into the feasibility of a free trade agreement spanning the twenty-one economies making up APEC.

More generally, one can observe a proliferation of a 'new generation' of plurilateral free trade negotiations that differ in some important respects from their traditional counterparts. First, they are more likely to involve constellations of nations based less on immediate geography than on an assessment of economic and political mutual advantage. Second, plurilateral 'hub and spoke' agreements are being negotiated by groupings or blocs of countries that are less integrated than in the past.

An example of a PTA that differs in the first respect from traditional plurilateral PTAs is the Trans-Pacific Strategic Economic Partnership Agreement (Trans-Pacific SEP). The Trans-Pacific SEP was negotiated initially between three countries from three different regions – South America (Chile), Asia (Singapore), and Australasia (New Zealand). Brunei later joined the negotiations making it an example of a 'four-party' PTA (hence it is sometimes referred to as the P4). The ethos behind the Trans-Pacific SEP is that of open regionalism – it is open to accession by other countries, and this is actively encouraged.

Although currently stalled, another negotiation that falls into this category, but on a much grander scale, is the Free Trade Agreement of the Americas (FTAA). A full-blown FTAA would cover thirty-four countries and span the Western Hemisphere. The concept of an Asia–Pacific Free Trade Agreement also falls into this category of new generation plurilateral PTA. A twenty-one-member APEC Free Trade Area, stretching from the United States (US) and South America to Japan, China, and Australia, would represent roughly half of total world trade and 57% of global gross domestic product.

The Association of South East Asian Nations (ASEAN) provides an example of the second point of differentiation – a more recent group of countries first establishing itself as a regional bloc, and then going on to negotiate PTAs with third countries. ASEAN was first formed as a regional group in 1967. The ASEAN Free Trade Agreement (AFTA) came into force in 1992, and was originally negotiated between Brunei, Indonesia, Malaysia, Philippines, Singapore and Thailand. AFTA has since expanded to accommodate the recently acceding ASEAN countries, Cambodia, Laos, Myanmar and Vietnam. While ASEAN continues a programme of internal liberalisation amongst its own members, it also negotiates 'as a bloc' with third

10 For example, Japan, New Zealand and Australia have traditionally been, and continue to be, staunch advocates of the multilateral process. At the time of writing all three countries are involved in multiple PTA negotiations.

countries.[11] ASEAN has already concluded a Framework Agreement,[12] a Goods Agreement,[13] and a Dispute Settlement Mechanism[14] with China, and is continuing to negotiate with China on services and investment. ASEAN is also currently negotiating PTAs with Australia and New Zealand (jointly), India, Japan and Korea.

The European Commission has also recently sought a mandate to negotiate with ASEAN. This mandate is part of the Commission's strategy to negotiate a 'new generation' of PTAs, which includes a proposal to negotiate Association Agreements with the Central American and Andean countries. The EU is already negotiating with two regional groupings, the Common Market of the Southern Cone (MERCUSOR) and the Gulf Co-operation Council (the GCC). In the words of Trade Commissioner Peter Mandelson, '[w]ith MERCOSUR and ASEAN, the Gulf Co-operation Council and the Central American and Andean countries, our goal is to reach agreement not with individual countries but with regional groupings who want, in their own ways, to draw the lessons of Europe's successful experience of economic integration'.[15]

The primary reason that groups of countries might want to negotiate as a 'bloc' is summarised in a recent publication by the EFTA Secretariat:

> The main reason why Iceland, Liechtenstein, Norway and Switzerland use EFTA as their common vehicle for free trade negotiations is that, as a trade grouping, the EFTA countries carry more weight as economic players and are thus more interesting for potential trade partners.[16]

As competition for PTAs intensifies, this logic suggests more countries may seek to group together to increase their attractiveness as negotiating partners, either as a 'hub', or as a 'plurilateral spoke'.[17] Examples of similar plurilateral PTAs might include the free trade agreement between Central American countries, the

11 In fact, for various reasons, very little intra-ASEAN trade occurs under AFTA's preferential arrangements. However, ASEAN has become sufficiently cohesive to hold itself out as a 'bloc' of countries ready to negotiate PTAs with third countries. As noted, the first example of this was ASEAN's PTA negotiations with China.

12 Framework Agreement on Comprehensive Economic Cooperation Between the Association of South East Asian Nations and the People's Republic of China (ASEAN–China Framework Agreement).

13 Agreement on Trade in Goods of the Framework Agreement on Comprehensive Economic Co-operation between the Association of Southeast Asian Nations and the People's Republic of China (ASEAN–China Goods Agreement).

14 Agreement on Dispute Settlement Mechanism for the Framework Agreement on Comprehensive Economic Co-operation Between the Association of Southeast Asian Nations and the People's Republic of China (ASEAN–China DSM).

15 Speech by Peter Mandelson at the London School of Economics, London, 9 October 2006.

16 EFTA Secretariat, *This is EFTA* (2006), available at www.secretariat.efta.int/Web/Publications/this_is_EFTA/note/.

17 There is some academic debate about what characteristics define a 'hub'. Certainly market size is an important factor. Whether ASEAN would be considered a 'hub' or a 'spoke', for example, may depend on the negotiation. Negotiating with the EU it could perhaps be considered a 'plurilateral spoke'. Likewise when negotiating with China. Nevertheless, ASEAN certainly appears to be seeking to establish itself as an East Asian hub in its own right. For the purposes of this article, whether ASEAN, or other regional groupings such as the Central American countries, are characterised as 'hubs' or 'spokes' is less important

Dominican Republic and the US (CAFTA–DR–US), the negotiations currently being conducted by the Gulf Co-operation Council (GCC) and third countries, and negotiations by the South African Customs Union (SACU) and third countries.

These 'new generation' plurilateral PTAs present both new opportunities and new challenges. There is a large and growing literature analysing the merits of PTAs in terms of their contribution (or otherwise) to global welfare. This is often presented in terms of a building bloc/stumbling bloc dichotomy. The focus tends to be on the nature of obligations contained in any particular PTA. Some argue that the broader and deeper the commitments, and the more open and less 'reciprocal' or discriminatory such agreements are, the more likely they are to be building blocs to global economic welfare.[18]

The complexities that arise from different and overlapping rules of origin are central to this debate. One recent analysis suggests that the unbundling or fragmentation of manufacturing processes may create a political economy favourable to 'taming the tangle' of multiple rules of origin, and predicts the eventual harmonisation of such rules. The analysis is, therefore, cautiously optimistic regarding the spaghetti-bowl-as-building-bloc scenario.[19] Others are more sceptical.[20]

Whatever view one may take on these important matters, this 'new generation' of plurilateral PTAs unquestionably also presents new challenges at a more practical level. They raise a set of issues that are more complex than those raised by their traditional counterparts. For a start, the groupings of countries involved are often more diverse geographically and economically, encompassing countries at different levels of development, not to mention political and cultural differences. The groupings may already be partially integrated themselves, or still in the process of integration.

How are such agreements to be negotiated? How are they to be structured so as to best reflect the negotiating objectives of the parties? How can differing levels of ambition and development be accommodated? How should existing and overlapping PTAs be handled? These questions are addressed in the next section.

III. Issues, options and challenges in negotiating new generation plurilateral PTAs

This section will examine in more detail some of the particular negotiating issues that arise in the context of plurilateral PTAs, particularly where these differ from traditional types of plurilateral PTAs. It will look first at the negotiating process, and then consider some options for structuring plurilateral PTAs. Following that, the issue of how to deal with prior PTAs is considered, including in cases where

than the fact that they are a grouping of partially integrated countries negotiating PTAs 'as a group' with one or more third countries.

18 See ADB, above note 8, at p. 290. 19 See Baldwin, above n. 7.

20 See, e.g., Razeen Sally, 'Free Trade Agreements and the Prospects for Regional Integration in East Asia', (2006) 1(2) *Asian Economic Policy Review* 306–21.

agreements contain most favoured nation (MFN) provisions. Finally, some of the issues unique to plurilateral PTAs that arise in the context of dispute settlement provisions, institutional mechanisms, and final provisions will be examined.

A. The negotiating process

Whether bilateral or plurilateral, the broad process by which a PTA is negotiated is likely to be similar. A primary negotiating committee (often called the Trade Negotiating Committee or TNC) will usually be established that brings together the lead negotiators of each country. The detailed negotiating work will take place in smaller working groups or committees made up of representatives of the countries negotiating the PTA. The working groups are often divided according to subject area – so there will be a goods negotiating group which is responsible for drafting the goods chapter of the PTA, a services negotiating group which drafts the services chapter of the PTA, and so on. Typically, separate working groups are set up for each different topic or chapter in a PTA. In addition, a legal group made up of the international lawyers from each country will discuss the dispute settlement mechanism, the institutional framework for the agreement, the exceptions, and the final provisions.

Once these working groups have completed their work (say, in the form of a draft goods chapter), the TNC will be called upon to endorse the outcome. Issues that cannot be resolved in the detailed negotiating groups are also commonly referred to the TNC for resolution by lead negotiators of each country. If the TNC cannot resolve the issue, Ministerial involvement may be required to break the deadlock.

The process described above applies equally to the negotiation of bilateral and plurilateral PTAs – only that in the case of a plurilateral PTA there will be more countries around the table at each level of the negotiating process. This alone adds a layer of complexity to the negotiation. Generally speaking, the more countries involved, the more complex it will become.

Particular challenges are also faced where there are significant differences in the level of development among negotiating parties. This may affect not only levels of ambition, but also the ability of countries to fully participate in the negotiating process. PTA negotiations are extremely resource intensive and often involve highly technical and specialised discussions. For this reason, technical assistance and capacity building will need to become (and, in some cases, have become) important aspects of the actual negotiating process itself, as well as being reflected in substantive PTA commitments.

The situation is more complex still when it comes to negotiating specific market access commitments, which lie at the heart of PTA negotiations.[21] The practical

21 In order to be consistent with WTO rules, a PTA must meet certain thresholds regarding market access established in the GATT, GATS, and the Enabling Clause. For example, tariffs must be eliminated on substantially all the trade between the PTA parties (GATT Article XXIV(8)(b)).

focus of market access negotiations is the goods, services and investment schedules of a PTA. These schedules contain the tariff reduction commitments, and services and investment market access and national treatment commitments.

In the context of a bilateral PTA, market access negotiations are, naturally, bilateral in nature. There is also an important bilateral component when negotiating plurilateral PTAs. Market access negotiations are typically driven by a bilateral 'request and offer' process. A country will make a specific bilateral request for market access to each negotiating partner. The content of each request is likely to differ for each negotiating partner, as it will reflect the particular trade profile between the two countries. The two countries then negotiate bilaterally, without the presence of the other countries, until agreement is reached between them. The various outcomes of these bilateral negotiations are usually 'plurilateralised' so that they apply to all countries in the negotiation. This is achieved by each country having a single identical tariff schedule, services schedule, and investment schedule that applies to every party to the PTA. In many ways, this reflects the way market access negotiations are conducted in the WTO.

Also mirroring WTO practice, 'negotiating modalities' can also be developed to assist market access negotiations. 'Negotiating modalities' generally refer to certain negotiated parameters or minimum requirements that guide or underpin the bilateral market access negotiations. The extent to which this occurs depends on the negotiation. The goods negotiation under the Trans-Pacific SEP, for example, relied primarily on bilateral request and offer negotiations rather than a pre-negotiated modality. The tariff schedules in the ASEAN–China Goods Agreement, by contrast, are based on a very complex and detailed modality, leaving more limited room for bilateral negotiations. Indeed, under that Agreement, it is primarily a *unilateral* decision for each party to determine exactly which tariff lines to place on the 'normal' track and which tariff lines to place on the 'sensitive' track (containing longer phase-out periods), provided such decisions conform with the parameters set out in the modalities. The modalities are themselves incorporated into the Agreement.[22]

How does the process described above relate to negotiations involving pre-existing blocs? As we have seen, when the EU reaches out to third countries to negotiate PTAs, it does so not so much as a group of individual countries, but as a pre-existing economic, political and legal entity. If you ask a negotiator from Chile, for example, 'who were you negotiating with', they can answer with a single acronym (the EU), and not a list of the various Member States. As we shall see, this is particularly the case in the context of goods negotiations, where for reasons of competence, it is the European Commission that enters into bilateral goods agreements with third countries. The EFTA Secretariat is also heavily involved when

22 Annexes 1 and 2 of the ASEAN–China Goods Agreement.

EFTA negotiates with third countries, although unlike the European Commission it does not enter into agreements as a party in its own right.

When it comes to plurilateral PTA negotiations involving less integrated or newer groupings of countries, the situation is likely to be more complicated. Of course, it is possible for such groups of countries to negotiate as a 'true' hub like the EU or EFTA, with a single voice reflecting a common position.[23] However, the less integrated the 'bloc' of countries is to begin with, the less likely that common positions on all issues will be possible. Common positions require pre-negotiation, and this can take considerable time and resources. The EU, for example, relies on a large and well-resourced institutional structure and the work of the Commission to arrive at common positions. Few other groupings have such resources at their disposal.

The result is likely to be a process that will take longer to complete, and require more flexible negotiating methods. Time may have to be allocated to allow for internal co-ordination, for example. It may be that on some issues a pre-existing bloc has a common position, while on others the individual members of the bloc will speak on their own behalf. There is also a close connection between the way the parties intend to structure the PTA, and the way the negotiating process will be conducted.

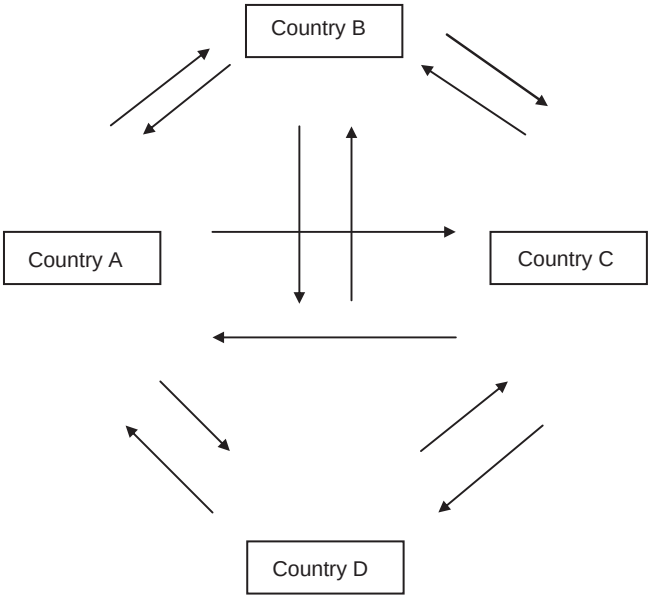
B. Structuring plurilateral PTAs

The exact scope of a PTA is often a matter for negotiation between the negotiating countries. Some 'PTAs' contain little more than a broad commitment to co-operate and an undertaking to negotiate in the future. However, most PTAs will at least contain commitments relating to the liberalisation of trade in goods ('goods-only' agreements). And the trend is to go further. Many PTAs today also contain commitments on services, investment, non-tariff barriers (such as SPS and TBT), intellectual property, competition policy, government procurement, and co-operation. Some also deal with environment and labour issues.

Across these subject areas, a PTA will contain many different types of rights and obligations. These may range from very specific market access obligations (such as tariff reduction timetables or services market access commitments), to general requirements to conform with WTO commitments, to mechanisms designed to enhance and facilitate ongoing co-operation in certain fields. There may also be broader commitments to promote private sector co-operation in sectors of particular interest.

The question, in the context of negotiating a plurilateral PTA, is how to configure these rights and obligations and assign them amongst the parties – that is, how to

23 As a matter of negotiating tactics, this is likely to be the preferred approach for such countries. A pre-negotiated common position is harder to negotiate against than a series of individual country positions.



Model 1 Multiparty PTA

structure the PTA. This question is inextricably linked to the objectives of the negotiating parties. It is also a question that can never be fully answered in the abstract. Each PTA negotiation has its own set of particular issues and sensitivities that will need to be addressed and accommodated. Nevertheless, it is possible to identify four general ways that rights and obligations could be assigned in a plurilateral PTA.

Under this model the rights and obligations flow between each and every party to the PTA. For example, under Model 1, Country A would have a goods schedule that applies to Countries B, C and D. Country B would have a goods schedule that applies to Countries A, C and D, and so forth. Such an approach could also be taken to services, investment, SPS, TBT – in fact any subject area covered by a PTA. This approach reflects an intention that each party should take on the same commitments and receive the same rights *vis-à-vis* each other party to the PTA.

The Trans-Pacific SEP is based upon this model. The obligations contained in the Trans-Pacific SEP are generally expressed as those of 'the Parties' and apply with respect to each other 'Party'. NAFTA is also based on this general model, although under NAFTA each country had two different goods schedules, one for each of its negotiating partners. This reflects the fact that NAFTA originated out of two bilateral processes - the Canada–United States Free Trade Agreement (CUSFTA) on the one hand, and negotiations toward establishing a Mexican–United States Free Trade Agreement on the other.

When it comes to negotiations with a pre-existing bloc, one of the key questions is whether the objective is to further liberalise amongst the members of the pre-existing bloc. If the answer is no, then Models 2 and 3 (below) provide possible approaches.

Model 2 can be appropriate where there is a high degree of integration already amongst the members of the pre-existing bloc. As can be seen, rights and obligations flow in just two directions. In this sense the situation is identical to a bilateral PTA.

The European Community's hub and spoke agreements provide a good example, most notably in the goods area. Because the European Community is a customs union with a common external tariff, in its hub and spoke PTAs it has a single 'Community tariff schedule' rather than separate tariff schedules for each of the EU member States. The objective is clearly to create commitments as between the EU and the third country, and not to create any obligations among the EU member States themselves. The pursuit of these types of PTAs is sometimes referred to as 'hub and spoke bilateralism'.[24]

In the services area things are a little more complex as there is no equivalent to a common external tariff, and there continue to be differences between the regulatory environments in the EU member States. Nevertheless, the EU does negotiate a common 'Community schedule' for services in its hub and spoke PTAs.[25] Many of the commitments in the Community schedule apply universally to all EU member States. However some country-specific limitations on commitments are also identified within the common schedule. As the Introductory notes to the Community's schedule in the EU–Chile Association Agreement (EU–Chile AA) makes clear:

> These commitments apply only to the relations between the Community and its Member States on the one hand, and non-Community countries on the other. They do not affect the rights and obligations of Member States arising from Community law.[26]

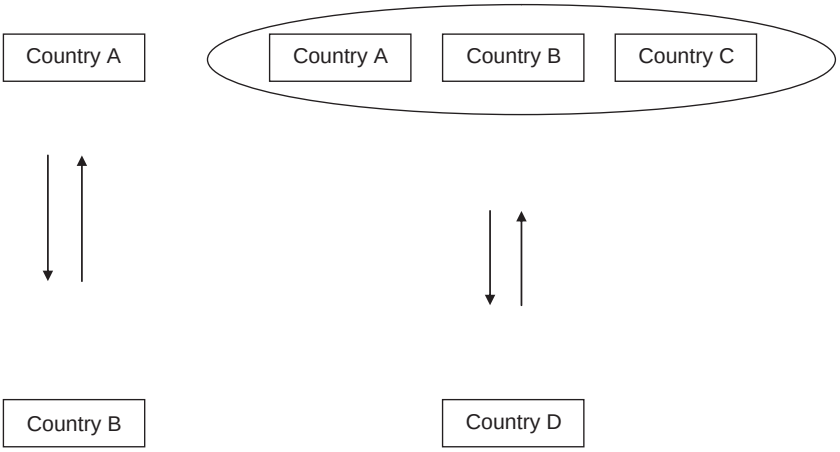
More generally, under the EU's hub and spoke agreements the extent to which the rights and obligations are assigned in accordance with Models 2 or 3 (below) depends on the subject area and issues of competence within the EU. A provision in the EU–Chile AA reflects the EU's approach:

> For the purposes of this Agreement, 'the parties' shall mean the Community or its Member States or the Community and its Member States, within their respective areas of competence as derived from the Treaty establishing the European Community, on the one hand, and the Republic of Chile, on the other.[27]

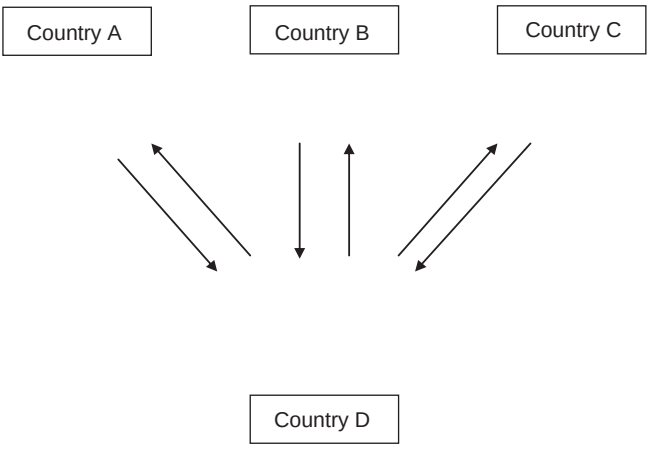
24 See Baldwin, above n. 7, at 1483. 25 See, e.g., EU–Chile AA.

26 Paragraph 1 of the Introductory Notes to the EU's services schedule, EU–Chile AA.

27 Article 197 of the EU–Chile AA. See also Article 55 of the European Union–Mexico Economic Partnership, Political Coordination and Co-operation Agreement.



Model 2 Pre-existing bloc and a third country (option A)



Model 3 Pre-existing bloc and third country (option B)

Rights and obligations under PTAs can only be assigned to 'parties' to the Agreement. This definition of 'parties' indicates that whether a particular obligation in a PTA involving the EU rests on the Community or on individual member States, or both, would require a situation-specific analysis.

Absent the degree of integration in the EU, Model 2 is not likely to be appropriate. As has been seen above, even in the context of the EU there are areas where a universal Community-wide approach is not possible or appropriate. Model 3 provides an alternative approach. Again, the intention here is to not undertake

further commitments *vis-à-vis* the members of the pre-existing bloc, only *vis-à-vis* a third country.

A key point from a legal (or drafting) perspective is that commitments in a PTA are generally expressed as those of 'the parties', and each state involved in the negotiation of a PTA will usually be a party in its own right.[28] As a result, if the objective is to limit the application of rights and obligations to certain parties and not others, this must be provided for expressly in the agreement.

The EFTA hub and spoke agreements provide an example. In the EFTA–Singapore Free Trade Agreement, Article 3 is headed '*Trade and Economic Relations Governed by this Agreement*'. Article 3.1 provides that:

> The provisions of this Agreement apply to the trade and economic relations between, on the one side, the EFTA states and, on the other side, Singapore, but not to the trade relations between individual EFTA states, unless otherwise provided for in this Agreement.

This provision effectively reverses the default position mentioned above. Instead of having to expressly 'carve out' commitments where you do not want them to apply as between certain parties, as a result of this clause it would be necessary to expressly 'carve-in' provisions that do apply as between the EFTA states.[29] The general intention of the EFTA states is to create obligations only *vis-à-vis* each EFTA state and the third country, and not between EFTA states themselves.

Where one of the objectives of the members of a pre-existing bloc in negotiating with a third country is to further liberalise amongst its own members, then Model 4 provides an appropriate approach. Under Model 4, each party has rights and obligations *vis-à-vis* every other party. In fact, in this sense, this model is identical to Model 1. However under this model, there is a degree of pre-existing integration among some of the parties to the PTA negotiations. Such an approach might be called 'hub and spoke plurilateralism'.

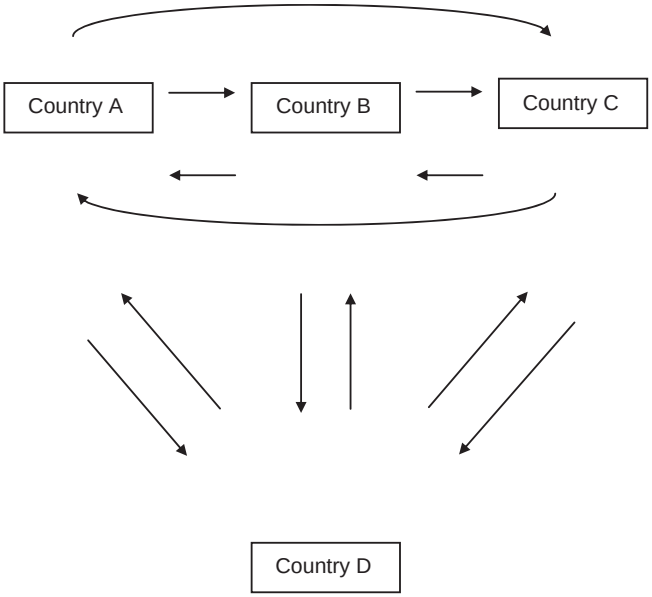
CAFTA–DR–US provides an example.[30] In general, CAFTA–DR–US expresses obligations as applying between 'the Parties', and a party is defined as any State for which the Agreement is in force. So in the goods chapter, for example, the national treatment obligation is expressed in terms of 'each Party' providing national treatment to 'the goods of another Party'.[31] Likewise, 'no Party' may increase customs duties except as otherwise provided in the Agreement,[32] and 'each Party' shall progressively eliminate customs duties in accordance with Annex 3.3.[33] These

28 As we have seen above, the situation with respect to the EU is more complicated.

29 The ability to 'carve-in' areas where the PTA would apply to EFTA states arises from the phrase 'unless otherwise provided for in this Agreement'.

30 As noted above, the US is the 'hub' in this negotiation, and the Central American states are perhaps best thought of as a 'plurilateral spoke'.

31 CAFTA–DR–US, Article 3.2.1. 32 Ibid., Article 3.3.1 33 Ibid., Article 3.3.2.



Model 4 Pre-existing bloc and third country (option C)

provisions indicate a general intention to apply the primary goods commitments in CAFTA–DR–US not only *vis-à-vis* the US and the Central American states, but *vis-à-vis* the Central American states themselves.[34] Although the phrase 'except as otherwise provided in this Agreement' preserves some flexibility to 'carve-out' the application of certain provisions in certain circumstances, the default position is universal application among all parties.

Likewise in the services[35] and investment chapters,[36] the key obligations are expressed in terms of 'each Party' owing obligations to 'any other Party'. While it would have been possible to exclude the application of these obligations for the Central American states *vis-à-vis* each other by taking out an appropriately worded reservation in the services and investment schedules, this does not appear to be have been done. The effect is that key commitments in the services and investment chapters undertaken by a Central American party apply not just *vis-à-vis* the US, but *vis-à-vis* every party to the PTA, including other Central American States.

34 Annex 3.3.6 appears to provide a special regime between the Dominican Republic and the Central American states that goes beyond the schedule commitments, and it has the options of claiming access under this Annex or the schedules.

35 CAFTA–DR–US, Chapter Eleven (Cross-Border Trade in Services).

36 CAFTA–DR–US, Chapter Ten (Investment).

1. Variations

Within each of the four general models discussed above there exists a number of possible permutations and variations. For example, as noted above, the approach taken to goods liberalisation in NAFTA contains an important variation. Rather than having an identical goods schedule applying to each other party, the countries have differentiated goods tariff phase-outs for each of the other two parties. Such an approach is likely to become more unwieldy, however, the greater the number of parties that are negotiating the PTA.

The approach that ASEAN has taken to tariff reduction also warrants a brief mention in this context. In the context of AFTA a modality has been utilised based on a complicated notion of reciprocity. For example, as between two parties to the PTA, preferences are only granted on tariff lines that are not contained on either party's 'sensitive list' of products. The result is that 'market access is defined by the interaction of the two lists thus creating different market access for every one of 45 bilateral flows among the ten ASEANs'.[37] AFTA is therefore a rather complex variation to Model 1.

ASEAN's PTAs provide an example of another interesting variation to the models outlined above, in that they create legal distinctions between certain members of a pre-existing bloc. This creates flexibility to reflect different levels of economic development among members of ASEAN. For example, in the ASEAN–China Framework and Goods Agreements a distinction is made between the 'ASEAN 6' (which is defined as referring to Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore, and Thailand), and the 'newer ASEAN Member States' (which is defined as referring to Cambodia, Lao PDR, Myanmar and Vietnam). These two definitions then provide the tool by which newly acceded ASEAN nations are given greater flexibility in terms of, for example, timeframes to complete negotiations,[38] timeframes to phase out tariffs,[39] and the number of tariff lines that can be placed on the 'sensitive list'.[40] In the detailed Annexes containing the precise modalities for tariff reduction, a further distinction is made between Vietnam on the one hand, and Cambodia, Lao PDR, and Myanmar on the other.

Despite these distinctions *between* ASEAN countries, the actual obligations undertaken by each ASEAN country under the ASEAN–China Agreements appear to apply to all 'Parties' to the PTA.[41] That is, tariff reduction commitments undertaken by each ASEAN member State appear to apply not only *vis-à-vis* China, but also to

37 See Baldwin, above n. 7, at note 32.

38 ASEAN–China Framework Agreement, Article 8. 39 ASEAN–China Goods Agreement, Annex 1.

40 Ibid., Annex 2.

41 ASEAN–China, Article 3.3, states that, 'Subject to Annex 1 and Annex 2 of this Agreement, all commitments undertaken by each Party under this Article shall be applied to all the other Parties'.

each other ASEAN member State. If this interpretation is correct, it would be an example of a variation to Model 4.

Another variation that may become increasingly common is free trade negotiations between two pre-existing regional blocs. Depending on the degree of integration of each bloc, this could take the form of a variation of Model 2, Model 3, or Model 4. The failure to date of attempts to conclude a European Union–MERCOSUR Free Trade Agreement perhaps hints at some of the difficulties and complexities that arise in such a context.

2. Mixing and matching models

Commonly, PTAs do not fall neatly within one model or another. While PTAs will often be *based* on one model, they may contain certain areas where rights and obligations are assigned in a different way. This reflects the fact that the parties' objectives may well be different regarding the application of different aspects of the PTA. Provided such differing intentions are clearly expressed in the Agreement, it is certainly possible to take a chapter-specific (or even obligation-specific) approach to assigning commitments in a PTA.

For example, the intention may be to apply some aspects of the PTA to members of a pre-existing bloc but not other aspects. Goods liberalisation is often the starting point for regional economic integration, and it may be that the pre-existing bloc already has a goods agreement in place amongst its members. If it did not want to use the opportunity of negotiations with a third country to further liberalise trade in goods amongst its own members, as noted above, it will need to insert a provision in the agreement that 'carves out' the goods chapter and related tariff schedules as between the members of the pre-existing bloc.

This could take the form of some alternative to the EFTA language discussed above, but limited in application to the goods chapter and schedule, rather than the entire agreement.[42] An alternative approach might be to limit the application of the tariff schedule only to certain parties – so for Model 3 above, the tariff schedules of Countries A, B, and C would apply only to Country D, whereas the tariff schedule of Country D would apply to Countries A, B, and C.

Similar approaches could be taken in services and investment. A general provision at the beginning of the relevant chapter could be used to ensure that the chapter only creates rights and obligations between the third country and each of the members of the pre-existing bloc, but does not create rights and obligations between the members of the bloc.

The alternative approach of limiting the application of the services/investment schedules to only certain parties (which could perhaps be specified in the

42 If this approach is taken, and depending on the structure of the PTA, it may also be useful to clarify the extent to which other goods-related chapters would apply, for example the rules of origin and customs chapters.

headnote of the schedules) could also be used where commitments are scheduled on a positive list basis – that is, where the schedules set out the sectors where specific commitments are undertaken. This would operate in the same way as the exclusion of tariff schedules. Where a negative list approach is taken to scheduling however, it would be necessary to craft a reservation that expressly carves out the application of the market access and national treatment obligations *vis-à-vis* particular countries.[43]

One further point to bear in mind in relation to excluding the application of schedules is that the obligations contained in the relevant chapter would still apply. While the specific tariff reduction or market access obligations are contained in *schedules* to the PTA, other obligations are contained in the relevant goods, services, or investment *chapters*. For example, in NAFTA, although different goods schedules apply to different parties, the same national treatment obligation, contained in the goods chapter, applies equally to all three parties.[44]

In contrast, there may be areas of the PTA where the members of the pre-existing bloc would like to *apply* the outcomes of the PTA with the third country, amongst its members. This may be so where, for example, the new PTA covers new ground not yet tackled by the pre-existing bloc, or goes significantly beyond the level of commitments amongst the members of the bloc.

For example, if the pre-existing bloc had only concluded a goods agreement amongst its members, it may wish to use the negotiations with a third country to establish services commitments amongst its members also. As mentioned, from a drafting perspective, this is easily achieved, as the default position is that such obligations would apply between all of 'the parties'.[45]

So far the focus has been on the goods, services and investment chapters. As noted however, many PTAs today contain chapters covering areas such as non-tariff barriers to trade, intellectual property, competition policy, and transparency to name a few. Subject always to the intentions of the parties, it may be that some of these chapters lend themselves more easily to universal application between all the parties. For example, provisions on the prompt publication of laws, or providing for procedural fairness in administrative rulings.

43 A different approach is required because, unlike the positive list approach, under the negative list approach market access and national treatment obligations are not limited to 'scheduled sectors'. Rather, they apply to the extent that they are not 'carved out' through reservations contained in the services schedule. So the effect of not applying the schedules (i.e., the reservations) to a particular country would be to give unfettered market access and national treatment to that country – the very opposite of what is intended.

44 In addition to the national treatment obligation there will be other obligations in the goods chapter, such as those relating to administrative fees and formalities, export duties, and institutional arrangements, for example. In the services chapter there may well be obligations relating to transparency and monopolies. Under the 'exclusion of schedules' approach these would still apply between all parties for the simple reason that only the obligations in the schedules are excluded.

45 If an EFTA-style 'carve-in' provision is included in the agreement, however, then an express provision will be required applying the services commitments to the pre-existing bloc.

In other areas, the creative use of institutional mechanisms could provide flexibility in terms of the application of certain chapters. For example a chapter on Technical Barriers to Trade may establish consultative frameworks designed to enhance future co-operation in areas including conformance requirements. As it may be difficult to say at the time that the PTA is negotiated whether any particular party will wish to make use of such provisions in the future, it probably will not make sense to exclude any parties from the chapter outright. An alternative might be to allow for voluntary participation in future initiatives by those countries that wish to do so. Provisions that allow parties to 'opt in' or 'opt out' of certain chapters, or parts of chapters, may also offer flexibility. Excluding a particular chapter from the dispute settlement mechanism might be another response to concerns over the effect of applying the chapter to all parties.

In summary, there are a number of ways a plurilateral PTA can be structured, and a number of ways that rights and obligations can be assigned. Various legal mechanisms can be used to mix, match, and modify these general approaches so as to develop a structure for a PTA that best accords with the negotiating objectives of the parties.

C. Prior PTAs

One likely outcome of this proliferation of PTAs, some having a broad membership, is that new PTAs will often overlap with existing PTAs. Such an overlap can, of course, occur in the context of bilateral PTAs. However the issues are likely to be more complicated in the context of a plurilateral PTA.

In the absence of an express provision, the relationship between a pre-existing PTA and a subsequent PTA will be governed by customary international law, as codified in Articles 30 and 59 of the Vienna Convention on the Law of Treaties ('Vienna Convention'[46]).

In the context of a bilateral PTA being negotiated between two states that already have a pre-existing bilateral PTA in force between them, the situation is fairly straightforward. Either the earlier treaty will be terminated or suspended in accordance with Article 59 of the Vienna Convention,[47] or where this is not the case, 'the earlier treaty applies only to the extent that its provisions are compatible with those of the later treaty'.[48] In other words, the new PTA prevails over the pre-existing one to the extent of any conflict. In order to avoid any doubt however, express provisions are usually inserted into the new PTA to govern the relationship

46 Done at Vienna 23 May 1969, in force 27 January 1980, 1155 UNTS 331; (1969) 8 ILM 679, UKTS (1980) 58.

47 This will be the case where the treaty relates to the same subject-matter and it appears from the later treaty, or is otherwise established, that the parties intended that the matter should be governed by the later treaty, or the provisions of the later treaty are so far incompatible with those of the earlier one that the two treaties are not capable of being applied at the same time.

48 Article 30(3) of the Vienna Convention.

between it and a pre-existing PTA between the parties. Often, this is simply to terminate the pre-existing PTA.

In the plurilateral context, the situation can be more complicated in at least two ways. First, the pre-existing PTA may be in force between only some of the parties to the new plurilateral PTA. For example, in the context of the Trans-Pacific SEP, New Zealand had a pre-existing bilateral PTA with Singapore. In the absence of any contrary intention, under the Vienna Convention the situation would be as described above for bilateral PTAs – the new agreement would prevail to the extent of any conflict.

A second complication can arise where the pre-existing PTA includes states other than those that are parties to the new plurilateral PTA. The Trans-Pacific SEP again provides an example – Singapore and Brunei were already parties to AFTA, a wider plurilateral PTA with other ASEAN countries. In the absence of a contrary intention, under the Vienna Convention, rights and obligations *vis-à-vis* Singapore and Brunei would be governed by the same rules as those for bilateral PTAs (the agreement that is later in time, the Trans-Pacific SEP, would prevail in the event of conflict), rights and obligations *vis-à-vis* Singapore and Brunei on the one hand and Chile and New Zealand on the other would be governed by the Trans-Pacific SEP, and rights and obligations between Singapore and Brunei on the one hand and the other ASEAN member states on the other would be governed by AFTA.

Rather than relying on general international law, most countries prefer to insert an express provision in the new PTA that clarifies the relationship between it and pre-existing agreements. Where the intention is to apply both agreements simultaneously, it is best to state this expressly. The Trans-Pacific SEP, for example, specifies that nothing in that Agreement shall derogate from the existing rights and obligations under any other multilateral or bilateral agreement to which it is a party.

In addition, a separate bilateral exchange of letters between New Zealand and Singapore clarifies that:

> Where either the NZSCEP or the Trans-Pacific SEP provides different treatment for an exporter, service supplier or investor of New Zealand or Singapore, that exporter, service supplier or investor is entitled to claim the more favourable of the treatment accorded to that exporter, service supplier or investor under either Agreement.

Plurilateral negotiations involving a pre-existing bloc raise similar issues given that the members of the pre-existing bloc will almost certainly have some form of PTA already in force between them.[49] Deciding on the appropriate relationship between this pre-existing PTA and the new PTA will again turn on the objectives of the

49 The level of integration required before a group of countries would hold themselves out to negotiate as a bloc with third countries is almost certainly going to include economic integration in the form of preferential trade relations of some kind.

parties in undertaking negotiations with third countries. Is the objective to replace the pre-existing agreement in its entirety, or in part? Or is the objective to leave the pre-existing agreement in place and have the two live side-by-side (with the new agreement perhaps augmenting the old in some areas)?

CAFTA–DR–US provides an example of one possible answer to these questions. Article 1.3.2 provides:

> For greater certainty, nothing in this Agreement shall prevent the Central American parties from maintaining their existing legal instruments of Central American integration, adopting new legal instruments of integration, or adopting measures to strengthen and deepen these instruments, provided that such instruments and measures are not inconsistent with this Agreement.

This provision clarifies that the existing legal instruments of Central American integration are not terminated by the CAFTA–DR–US, and nor will the CAFTA–DR–US prevent the adoption of instruments which bring about deeper integration for the Central American parties. At the same time, it makes clear that to the extent that any such existing or future instruments of integration conflict with the CAFTA–DR–US, the CAFTA–DR–US prevails.

1. Pre-existing PTAs and most-favoured-nation (MFN) treatment

The inclusion of MFN clauses in PTAs can have particular implications in the context of negotiations with a pre-existing bloc of countries.

Most-favoured nation treatment is one of the fundamental building blocks of the international trading system, and is expressed in Article I of the General Agreement on Tariffs and Trade (GATT 1994) and Article II of the General Agreement on Trade in Services (GATS). PTAs that provide preferential treatment to the goods and services of particular states, are recognised as exceptions to the fundamental requirement to treat all trading partners as equals, and are only consistent with the WTO if they meet certain stringent requirements regarding the scope and depth of commitments.

PTAs are, therefore, exceptions to a broad MFN obligation. However the use of MFN obligations *within* PTAs themselves is becoming more common, at least in the services and investment contexts.[50]

The basic concept of these PTA-specific MFN clauses is identical to their broader multilateral counterpart – if a party to the PTA extends more favourable treatment to any state it must extend that more favourable treatment to the other parties to the PTA. Whatever the merits of this type of clause in policy terms,[51] it

50 The author is unaware of any existing PTA that contains an MFN provision in relation to goods liberalisation.

51 It could be argued that such clauses promote PTAs as building blocks as they operate to automatically extend benefits achieved in one limited context to a broader group of countries.

does raise a potential issue with respect to pre-existing PTAs, and ongoing integration by a pre-existing bloc. In the absence of any other provision to the contrary, an MFN clause would mean that any integration among the members of the pre-existing bloc (whether extended before or after the conclusion of the new PTA), that goes beyond the benefits extended in the new PTA, have to be extended to the parties of the new PTA.

Again, whether this presents an issue or not depends upon the intentions of the parties. Such an outcome is consistent with an objective to pursue ongoing integration among the parties to the new PTA. Alternatively, a pre-existing bloc may prefer to preserve some flexibility to pursue deeper integration amongst its members only, without having to automatically extend the benefits of such integration to other PTA partners. If this is the intention, it will be necessary to provide for this expressly where a PTA contains an MFN clause.[52]

For example, in CAFTA–DR–US each Central American party took an Annex II reservation against the MFN commitment in the services and investment chapters. The reservation is in the following terms:

> [Name of Central American party] reserves, *vis-à-vis* the United States and the Dominican Republic, the right to adopt or maintain any measure that accords differential treatment to countries under any bilateral or multilateral international agreement in force or signed prior to the date of entry into force of this Agreement.

The effect of this clause is to allow Central American parties to continue to provide preferential treatment to each other (and indeed, to any other country) under any agreement in existence when CAFTA–DR–US enters into force. The US and the Dominican Republic took out similar reservations. Notably the provision is backwards looking in that it does not cover measures taken under future instruments of integration. If the intention is to cover future integration as well, that would have to be made explicit in the reservation.

D. Dispute settlement provisions in plurilateral PTAs

A feature of modern PTAs is the inclusion of a binding dispute settlement mechanism for resolving disputes. This mirrors the development of a binding mechanism in the WTO, and dispute settlement chapters in PTAs are often modeled on the WTO's Dispute Settlement Understanding (DSU).

52 Because there is generally no MFN clause in goods chapters, it is not necessary to preserve this flexibility in that context. Interestingly, however, in the CAFTA–DR–US a provision has been inserted 'for greater certainty'. Article 3.3.3 states: 'For greater certainty, paragraph 2 (progressive elimination of customs duties) shall not prevent a Central American party from providing identical or more favourable tariff treatment to a good as provided for under the legal instruments of Central American integration, provided that the good meets the rules of origin under those instruments'.

The core provisions relating to dispute settlement will be the same regardless of the number of parties to a PTA. However, there are some issues that arise only in the context of plurilateral PTAs, or that become more vexed in such a context.

One of these issues relates to the extent to which 'third parties' can participate in a dispute between other parties to the PTA. This question of 'third party rights' has received a lot of attention in the WTO negotiations aimed at reviewing the DSU. At present under the DSU third parties have limited rights to participate, whereby they only receive documents submitted prior to the first panel hearing, can provide only one written submission, and can attend only a special session scheduled during the first panel hearing.

A number of proposals to 'enhance' these existing rights have received good support from a broad cross-section of the WTO membership. However, disagreement remains over exactly how much third party rights should be enhanced. Most agree that some degree of third party participation is useful as it enables third parties to provide their views on the proper interpretation of the agreement. But this needs to be balanced against the objective of providing an efficient mechanism for resolving a dispute between the primary disputing parties.

Plurilateral PTAs must address this issue. There are two stages of the disputes process where the rights of third parties need to be determined. The first is at the consultation phase, and the second is when the dispute has proceeded to arbitration by a panel. With regards the first, some of the options include: giving third parties an unfettered right to join consultations,[53] giving the complaining party the right to veto the participation of certain third parties (the situation currently in the DSU), giving the complaining party the right to veto the participation of third parties but only if it does so with respect to *all* potential third parties (i.e., not enabling it to pick and choose), and enabling third parties to join unless the complaining and responding party agree otherwise (i.e., where there is joint agreement that a third party should *not* join). The ASEAN–Korea DSM provides a further alternative in that it does not appear to contemplate third parties participating in the consultation phase at all.[54]

Once a dispute has proceeded beyond consultations to the arbitral phase, third parties are generally given an unfettered right to join the process.[55] The issues to consider here are the number of submissions a third party can make, the number of hearings it can attend, and which documents it should receive. For example, the Trans-Pacific SEP contemplates third parties making 'written submissions', attending 'hearings of the tribunal', and receiving all written submissions of the disputing parties. In CAFTA–DR–US third parties are 'entitled to attend all

53 This is the position in CAFTA–DR–US, Article 20.4.3.

54 Agreement on Dispute Settlement Mechanism Under the Framework Agreement on Comprehensive Economic Co-operation Among the Member Countries of the Association of South East Nations and the Republic of Korea (ASEAN–Korea DSM).

55 This is consistent with the position under the DSU.

hearings, to make written and oral submissions to the panel, and to receive written submissions of the disputing parties'.[56] In the ASEAN–Korea DSM third parties only receive the submissions of the disputing parties at the first meeting of the arbitral panel.

A second issue that arises in the context of plurilateral PTAs is how to deal with multiple disputes on the same or similar issue. In the interests of efficiency and procedural fairness, the usual approach is to encourage multiple complainants to 'join' a dispute so that similar disputes are consolidated into a single disputes procedure. In the WTO this has become common and the process is facilitated by the WTO secretariat. In the context of plurilateral PTAs, where the same level of institutional support is not likely to exist, thought needs to be given to how these procedures will operate.

The possibility of more than one complainant raises other issues. For example, how will the process for choosing arbitrators be affected? Commonly, the complainant chooses one of the arbitrators. Where there is more than one complaining party, the complaining parties will presumably have to agree amongst themselves before nominating an arbitrator. This may give rise to some difficulties given the fairly tight timeframes usually contemplated for the composition of arbitral tribunals.

Another issue that becomes more complicated where there are multiple complainants is that of 'choice of forum'. Choice of forum provisions operate where the same dispute could be taken either under the PTA or some other international agreement (most likely the WTO, although it could also be another overlapping PTA). The issues are difficult enough in the context of a bilateral PTA: should the complainant have to make an irreversible choice between alternate forums for pursuing a case, or should it have the freedom to pursue the case in both forums? The latter option gives the complaining party greater flexibility, however risks the development of inconsistent jurisprudence on the same issue, and allows a *de facto* appeal from one forum to another.

In the context of multiple complainants the issues become even more difficult. Should the decision of one complainant to use a particular forum restrict other potential complainants to using that same forum? If not, how should the risk of inconsistent jurisprudence be managed? From a respondent's perspective, how should the risk of multiple challenges in multiple forums on the same issue be managed? At present, while dispute chapters in PTAs are still relatively young and not widely used, these questions remain largely theoretical. However the image of the spaghetti bowl is never more appropriate than when contemplating the prospect of a tangled knot of inconsistent arbitral rulings on essentially the same issues.[57] It is

56 CAFTA–DR–US, Article 20.11.

57 While the formal legal basis of the decisions would be different (as they would be based on provisions contained in different international agreements), the issues being ruled on would be substantially the same. This is particularly the case where PTA provisions simply mirror or cross refer to language used in WTO provisions.

difficult to see how such an outcome could contribute to the swift resolution of trade disputes – the very reason to have binding dispute settlement.

Finally, unlike a bilateral PTA where the obligations are purely reciprocal in nature, under a plurilateral PTA obligations may be considered either 'reciprocal' or obligations owed 'inter se' to all parties. Whether the nature of the different types of obligations should have an impact on the remedies available might also be considered. For example, in the context of the breach of a purely reciprocal obligation, the provision of bilateral compensation – even monetary compensation – may be considered more appropriate than where the breached obligation is owed equally to all parties.

E. Institutional provisions of plurilateral PTAs

The primary role of institutional mechanisms established under PTAs is to oversee the implementation of existing commitments, and facilitate ongoing co-operation, negotiation, and further integration by the parties. There is a fairly common approach across PTAs, whether bilateral or plurilateral. A primary Committee or Commission is usually established, supported by a number of sub-committees that deal with particular areas (such as goods, services, TBT and so on). The agreement will usually set out the functions and powers of the various committees and practical details such as how often they will meet and at what level.

Much like the negotiating process, the obvious difference in the plurilateral context is that there will be more countries represented in the various committees. At a very practical level, this represents a greater logistical challenge. Co-ordinating meetings between two countries is relatively straightforward – co-ordinating meetings between larger groups of countries tends to become exponentially more difficult. As a result, plurilateral PTAs are likely to require a greater level of institutional support.[58] Pre-existing blocs may already benefit from the support of a secretariat (e.g., the ASEAN secretariat and EFTA secretariat), and thought might be given to how these might best be used in the context of PTAs with third countries.

In plurilateral PTAs, an additional institutional layer is provided by the depositary. Unlike their bilateral counterparts, plurilateral PTAs often designate a depositary to carry out the functions specified in Article 77 of the Vienna Convention on the Law of Treaties. In accordance with that Convention the depositary may be a state, a group of states or an international organisation.[59]

58 Although the focus here is on the institutions and institutional support following the entry into force of a PTA, the same basic point applies to the negotiating process itself. The practical and logistical challenges of negotiating a plurilateral PTA should not be underestimated.

59 For example, the Trans-Pacific SEP designates the Government of New Zealand as the depositary, the EFTA–Singapore PTA designates the Government of Norway as the depositary, CAFTA–DR–US designates the General Secretariat of the Organisation of American States as the depositary, and the EU–Chile AA designates the Secretary General of the Council of the European Union as Depositary.

In terms of institutional processes, plurilateral PTAs also raise the question of how decisions by the committees should be made. Clearly the preference in international trade bodies will always be for consensus decision-making, and this is the standard approach taken in plurilateral PTAs. However, larger and more ambitious plurilateral PTAs may need to confront the questions faced in multilateral systems – what if consensus is not possible? Should provision be made for voting in the absence of consensus? If so, what kind of majority should be required? Should voting be limited to issues of a certain kind?

F. Final provisions in plurilateral PTAs

The final provisions of a PTA typically deal with signature and entry into force, amending the agreement, the relationship of the agreement to other agreements, accession, and withdrawal.

In a plurilateral PTA, special attention needs to be paid to the entry into force provisions. A bilateral PTA would usually enter into force when both parties have ratified it, or signalled that they have completed their internal procedures, often given effect through an exchange of notes between the two countries. In a plurilateral PTA not involving a pre-existing bloc of countries, the PTA would typically enter into force when at least two parties have deposited their instrument of ratification or acceptance, or otherwise notified the depositary that they have completed necessary internal procedures. The Trans-Pacific SEP provides an example of this type of entry into force provision.[60]

In a plurilateral PTA that does involve a pre-existing bloc, thought must be given to the conditions under which the agreement should enter into force. One option is to adopt the same approach as that described above, simply requiring two countries to have ratified it. It may, however, be preferable to require the third country and at least one member of the pre-existing bloc to have ratified it. Article 22.5 of the CAFTA–DR–US provides an example of this approach.

Another point to bear in mind is that a plurilateral PTA, in all likelihood, will enter into force on different dates for different countries. It may be desirable to set a limit on when a country can join the agreement beyond the date it first enters into force. In CAFTA–DR–US, for example, unless the parties otherwise agree, a signatory cannot take action to join the agreement later than two years after the date it enters into force.[61]

In addition, a provision may be required to clarify what happens if the agreement enters into force for a country after certain tariff reductions are already supposed to have taken place under that countries tariff schedule. Again, CAFTA–DR–US

60 Trans-Pacific SEP, Article 20.4. 61 CAFTA–DR–US, Article 22.5.2.

provides an example whereby the rates of duty are applied as if the agreement entered into force for that party on the date that it first entered into force.[62]

IV. Conclusion

Countries have turned to PTAs as a quicker and simpler alternative to the multilateral process. But while PTAs may be *relatively* quicker and simpler, this is not to say that they are (by any means) quick and simple. Negotiating bilateral free trade agreements is difficult enough. Plurilateral free trade agreements, especially 'new generation' plurilateral PTAs, offer additional complexities.

This chapter has explored some of the issues that arise in that context. It is worth noting that much of the discussion has been based on an idealised vision of how a PTA negotiation takes place. In reality, however, it is not always possible to follow a linear progression from the formulation of negotiation objectives to their perfect reflection in the architecture of the final agreement. In the pressure and 'fog' of a negotiating process things tend to occur somewhat more organically. Issues are grappled with as they arise, and in the particular circumstances of that negotiation.

All the more reason, however, to reflect further on these issues outside of that context. Exploring innovative and flexible approaches will be increasingly important as more ambitious PTAs are undertaken, and as countries or groups of countries pursue plurilateral PTAs with partners in different geographic regions and with differing levels of economic development.

62 CAFTA–DR–US, Annex 3.3, Article 4.

PART III

Relationship with WTO and international law

5

Legal requirements for PTAs under the WTO

ANDREW D. MITCHELL AND NICOLAS J.S. LOCKHART*

I. Introduction

The global trading system is now comprised of an inter-locking, ever-growing, network of bilateral, plurilateral and multilateral trade agreements. It would be easy to assume that trade agreements, whether bilateral, plurilateral or regional, are necessarily beneficial for trade. After all, such agreements pursue the common goal of trade promotion through liberalisation. More trade agreements of whatever type might, therefore, translate into more trade liberalisation. The shortcoming of this assumption is, however, that bilateral, plurilateral and multilateral agreements pursue this goal in different and often conflicting ways. A core objective of the multilateral trading system is 'the elimination of discriminatory treatment in international trade relations'.[1] In pursuit of this objective, WTO Members must accord equal treatment to the goods and services of all other WTO Members (through 'most-favoured-nation' or 'MFN' treatment).[2] In contrast, bilateral and plurilateral trade agreements – preferential trade agreements (PTAs)[3] – pursue trade liberalisation through precisely this type of discrimination. The parties to a PTA liberalise trade solely among themselves, creating a network of special preferences within the PTA that are not available to other WTO Members. PTAs, therefore, entrench the very discrimination that WTO rules seek to eliminate. This key difference in approach makes the relationship between multilateralism and regionalism both complicated and controversial. In economic terms, it is still not clear whether maintaining an ever-growing network of PTAs alongside multilateral rules produces an overall increase or decrease in economic welfare. In legal terms,

* This chapter expands on previous work by the authors in: 'Regional Trade Agreements Under GATT 1994: An Exception and its Limits', in Andrew D. Mitchell (ed.), *Challenges and Prospects for the WTO* (London: Cameron May, 2005), pp. 217–52; and 'The Relationship between the WTO and an Australia–China FTA', in Gary B. Magee, Sisira K.W. Jayasuriya and Donald MacLaren (eds.), *Negotiating a Preferential Trading Agreement: Lessons from Australia and China* (London: Edward Elgar, 2008 forthcoming). The authors would like to thank Dr Tania Voon (the University of Melbourne) and Dr Lorand Bartels (the University of Cambridge) for their comments on an earlier version of this chapter.

1 WTO Agreement, Preamble. 2 GATT 1994, Article I; and GATS, Article II.

3 It is common in the WTO to refer to such agreements as regional trade agreements. However, many recent agreements lack any regional proximity, such as the United States–Jordan Free Trade Agreement.

the coexistence of the WTO and PTAs among WTO Members creates a complex system of competing international rights and obligations.

As PTAs involve discrimination contrary to the general MFN obligation, they would normally give rise to inconsistencies with WTO rules. However, the WTO Agreements contain a series of exceptions for PTAs that allow limited derogation from WTO rules for PTAs meeting certain conditions. Only PTAs falling within one of these exceptions are valid under WTO law. In other words, a WTO Member must ensure that any PTA to which it is a party complies with the conditions of the relevant WTO exception. Otherwise, the Member risks acting inconsistently with its WTO obligations. The PTA exceptions are contained in: Article XXIV of GATT 1994; paragraph 2(c) of the Enabling Clause;[4] and Article V of GATS. The first two exceptions apply to RTA provisions relating to goods, while the third applies to RTA provisions relating to services. A PTA covering both goods and services would generally need to comply with the relevant exceptions for both goods and services.

Few provisions of the WTO Agreements have inspired as much controversy and disagreement as the PTA exceptions. The WTO Members themselves are divided on almost every issue of significance in these exceptions, with the result that the process for WTO review of PTAs has broken down. Although 175 PTAs have been notified to the WTO since it was established in 1995,[5] none has completed the GATT or GATS examination process to determine its WTO-consistency. Ironically, this systemic failure comes at a time when the WTO exceptions for PTAs should have taken on increasing importance because of the unprecedented proliferation of PTAs among WTO Members.[6] In addition, although the Appellate Body recently issued its first decision on the Enabling Clause,[7] the Appellate Body has provided very little substantive guidance on Article XXIV of GATT 1994 or Article V of GATS. Therefore, it is worth examining these exceptions to identify the main areas of controversy and uncertainty, particularly as they are subject to negotiation in the current Doha Round and may arise in future disputes.

This chapter addresses the substantive aspects of the exception for PTAs in relation to goods under Article XXIV, beginning with an explanation of its structure and scope. The chapter goes on to examine in detail the conditions with which PTAs must comply in order to fall within the exception – these conditions relate to the

4 Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries, GATT Document L/4903, BISD 26S/203 (28 November 1979) (Enabling Clause). As a decision of the GATT CONTRACTING PARTIES, the Enabling Clause forms part of GATT 1994: see para. 1(b)(iv) of the language incorporating GATT 1994 into the WTO Agreement.

5 See www.wto.org/english/tratop_e/region_e/summary_e.xls (calculated as the sum of notifications occurring after 1 January 1995 relating to the enabling clause, GATS Article V and GATT Article XXIV as at 15 September 2006).

6 In 1995 there were sixty-two operative PTAs, in 2000 that number had increased to 104 and by 15 September 2006 the number was 211: see www.wto.org/english/tratop_e/region_e/ summary_e.xls.

7 See Appellate Body Report, *EC–Tariff Preferences*.

elimination of restrictions on trade between the parties to the PTA, and to the nature and level of restrictions that the parties to the PTA impose on trade with WTO Members that are not party to the PTA. The chapter then goes on to briefly consider the substantive aspects of the exception for PTAs in relation to services under Article V of the GATS. Finally, it discusses the activities of the Committee on Regional Trade Agreements as well as the lack of enforcement of the rules before WTO tribunals. This puts into context the likelihood of any legal challenge.

II. Scope of the GATT exception for RTAs: Article XXIV:5

A. Exception as defence

Article XXIV:5 of GATT 1994 provides an exception to certain WTO obligations for 'customs unions' and 'free-trade areas' (FTAs), which are the two possible types of PTAs for the purposes of this chapter. The opening paragraph, or chapeau, of Article XXIV:5 states:

> Accordingly, the provisions of this Agreement shall not prevent, as between the territories of Members, the formation of a customs union or of a free-trade area . . .

The Appellate Body has indicated that the words 'shall not prevent' in Article XXIV:5 mean that 'the provisions of the GATT 1994 *shall not make impossible* the formation of a customs union'[8] or, presumably, an FTA.[9] That is, Article XXIV:5 provides a justification for the adoption of certain PTAs and constitutes a 'defence' to a claim that such a PTA is inconsistent with any provision of GATT 1994.[10] According to the general jurisprudence of WTO panels and the Appellate Body regarding the burden of proof in WTO disputes, this means that it would be for the Member challenging a PTA to establish its inconsistency with a provision of GATT 1994, and for the responding Member to prove that the inconsistency is justified or removed[11] because the PTA falls within the exception in Article XXIV:5.[12]

B. Purpose of the exception

The WTO Agreements, including GATT 1994, are to be interpreted according to the words used in the treaty, read in their context, and in the light of the object and

8 Appellate Body Report, *Turkey–Textiles*, para. 45 (original emphasis).

9 In *Turkey–Textiles*, the Appellate Body was considering a customs union and not an FTA. However, the chapeau of Article XXIV:5 applies to both customs unions (under Article XXIV:5(a)) and FTAs (under Article XXIV:5(b)), so the same reading of the words 'shall not prevent' should also apply to FTAs.

10 Appellate Body Report, *Turkey–Textiles*, para. 45.

11 See Appellate Body Report, *EC–Tariff Preferences*, pp. 100–3.

12 See, e.g., Appellate Body Report, *US–Shirts and Blouses*, p. 14; compare Appellate Body Report, *EC–Tariff Preferences*, paras. 87–8.

purpose of the treaty.[13] Article XXIV:4 sets out the purpose of the exception in Article XXIV:5 and therefore acts as a guide to understanding and applying that exception.[14] Article XXIV:4 states:

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

This statement is complemented by the Understanding on the Interpretation of Article XXIV of the GATT 1994 (RTA Understanding), in which WTO Members expand further on the purpose of Article XXIV:5.[15] In the RTA Understanding, WTO Members:

- recognise 'the contribution to the expansion of world trade' that may be made through the establishment of customs unions and FTAs;
- recognise that the expansion of world trade 'is increased' if internal trade restrictions within an RTA are eliminated for 'all trade' and 'diminished if any major sector of trade is excluded'; and
- reiterate that the establishment of an RTA 'should to the greatest extent possible avoid creating adverse effects on the trade of other Members'.[16]

In *Turkey–Textiles*, the Appellate Body addressed Article XXIV for the first time. The Appellate Body noted that Article XXIV:4 'does not set forth a separate obligation itself but, rather, sets forth the overriding and pervasive purpose for Article XXIV'.[17] It added that the other provisions of Article XXIV 'must be interpreted in the light of the purpose' through a process of 'constant reference to this purpose'.[18]

13 Article 3.2 of the DSU states that the WTO agreements are to be interpreted in accordance with the customary rules of interpretation of public international law. These rules were codified in Articles 31, 32 and 33 of the Vienna Convention on the Law of Treaties, done at Vienna 23 May 1969, in force 27 January 1980, 1155 UNTS 331; and Appellate Body Report, *US–Gasoline*, p. 17.

14 One question that arises in relation to the object and purpose of the WTO Agreements is whether the object and purpose that is relevant is that of the WTO Agreements as a whole (given that they comprise one treaty) or of individual WTO Agreements. Article 31(1) may leave some scope for consideration of both kinds of object and purpose. The Appellate Body in *EC–Chicken Classification* concluded that the reference to 'its' object and purpose in Article 31(1) suggests that it is referring to the object and purpose of 'the treaty itself, in its entirety'. However, the Appellate Body also stated that Article 31(1) does not exclude consideration of the object and purpose of particular treaty terms, if doing so assists the interpreter in determining the treaty's object and purpose on the whole. See generally: Andrew D. Mitchell, *Legal Principles in WTO Disputes* (Cambridge: Cambridge University Press, 2008).

15 The RTA Understanding forms part of GATT 1994 pursuant to paragraph 1(c)(iv) of the language incorporating GATT 1994 into the WTO Agreement. The RTA Understanding was adopted at the conclusion of the Uruguay Round.

16 RTA Understanding, Preamble. 17 Appellate Body Report, *Turkey–Textiles*, para. 57. 18 *Ibid.*

How can we summarise the purpose of the PTA exception in GATT 1994? Perhaps unsurprisingly, the primary goal of the exception, as reflected in Article XXIV:4 and the RTA Understanding, is the promotion of trade. As noted earlier, the parties to a PTA grant each other special trade preferences that are not offered to other WTO Members. The establishment of a PTA, therefore, creates the potential for positive effects on *internal* trade between the parties (who benefit from the preferences) and negative effects on *external* trade with other Members (who are excluded from the preferences). To secure an overall expansion of world trade, the exception in Article XXIV:5 is designed to maximise the internal trade liberalising effects of a PTA and to minimise its external trade-restricting effects.[19]

C. Exception for what?

1. PTAs covered

(a) Customs unions and free-trade areas The exception in Article XXIV:5 of GATT 1994 applies to customs unions and FTAs, as defined in Article XXIV:8(a) and (b) respectively. Broadly, a customs union means 'the substitution of a single customs territory for two or more customs territories, so that'[20] almost all restrictions are eliminated with respect to substantially all trade between the parties (i.e., internal trade),[21] and the parties apply substantially the same restrictions to the trade of other countries (i.e., external trade).[22] Again, in broad terms, an FTA is 'a group of two or more customs territories' in which almost all restrictions are eliminated with respect to substantially all internal trade.

In essence, Article XXIV:8 establishes certain conditions with which an agreement must comply in order to fall within the definition of a customs union or an FTA. In addition, Article XXIV:5 describes certain conditions that a customs union or an FTA must meet in order to benefit from the exception.[23] The conditions imposed on customs unions and FTAs are similar in many respects, as discussed further below.

Many WTO agreements have special rules or flexibilities that apply less onerous disciplines to developing countries as compared to developed countries (an aspect of 'special and differential treatment'). In the context of PTAs, a less onerous definition could have applied to a customs union or an FTA between a developing country WTO Member and a developed country WTO Member.[24] For instance, in forming an FTA, a developing country could have been permitted to liberalise its own market to a lesser degree than a developed country partner (so-called 'asymmetrical' obligations). However, the exception in Article XXIV:5 does not expressly include any such flexibilities.

19 *Ibid.* 20 GATT 1994, Article XXIV:8(a). 21 GATT 1994, Article XXIV:8(a)(i).
22 GATT 1994, Article XXIV:8(a)(ii).
23 Certain special requirements regarding these conditions may apply under Article XXIV:9 in relation to preferences in respect of import duties or charges as described in Article I:2 of GATT 1994.
24 Certain RTAs concluded between developing countries are covered by the Enabling Clause.

(b) Interim agreements The formation of a PTA entails significant trade policy co-ordination among the parties, as well as extensive changes to domestic regulations affecting trade. Article XXIV recognises that WTO Members wishing to enter into a PTA may not be able to achieve the required level of economic integration immediately. Consequently, the exception for PTAs in Article XXIV:5 extends to 'interim agreements' necessary for the formation of customs unions or FTAs, subject to certain requirements. Under Article XXIV:5(c), an interim agreement must lead to the formation of a customs union or FTA 'within a reasonable length of time'. Paragraph 3 of the RTA Understanding specifies that this period 'should exceed 10 years only in exceptional cases'. Although such cases are not defined, where one of the PTA parties is a developing country, the level of development of that party might be an exceptional circumstance justifying an extended period of time for formation of a PTA.

There is some controversy as to when an interim agreement must meet the requirements of Article XXIV:5 and 8. Some Members consider that these requirements need to be fulfilled only at the end of the reasonable period for implementation. Others argue that the requirements of Article XXIV:5 (not raising external barriers to trade) must be met at all stages of implementation.[25] This distinction seems to find support in a textual difference between the two paragraphs. Article XXIV:5 explicitly includes 'interim agreements' in the list of agreements that may not impose 'higher or more restrictive' external trade restrictions. In contrast, Article XXIV:8 does not state that 'interim agreements' are subject to the requirement to eliminate internal restrictions on substantially all trade. This suggests that interim agreements need not fulfil the requirements of paragraph 8 but must fulfil the requirements of paragraph 5. This reading of the text is consistent with the purpose of the PTA exception because it ensures that other WTO Members are not faced with increased barriers to trade at any stage of the implementation process but it allows Members time to eliminate internal trade restrictions.

2. Measures covered

(a) Measures adopted upon formation Article XXIV:5 states that GATT 1994 shall not prevent 'the formation of a customs union or of a free-trade area'. The Appellate Body has interpreted the word 'formation' to mean that measures imposed by WTO Members that would otherwise be inconsistent with GATT 1994 do not fall within the Article XXIV:5 exception unless they are 'introduced upon the formation of a customs union'[26] or, presumably, an FTA. Thus, WTO-inconsistent measures that are added to the terms of a PTA after the PTA has been formed would not fall within the exception.

25 WTO Committee on Regional Trade Agreements, *Synopsis of 'Systemic' Issues Related to Regional Trade Agreements: Note by the Secretariat*, WT/REG/W/37 (2 March 2000), para. 48(c).

26 Appellate Body Report, *Turkey–Textiles*, para. 46.

In some situations, this limitation may create difficulties for PTA parties. One example arose in *US–Line Pipe Safeguards* in relation to safeguard measures, which are emergency actions taken to respond to particular market situations on a temporary basis.[27] The dispute in *US–Line Pipe Safeguards* concerned a specific safeguard measure on line pipe adopted by the United States (US). The US excluded imports from Canada and Mexico from the application of the safeguard measure because these three countries had agreed as a general matter, pursuant to the North American Free Trade Agreement (NAFTA), not to impose safeguard measures on each other.[28] Korea challenged the safeguard under several provisions of GATT 1994 and the Agreement on Safeguards.[29] The panel found that the line pipe measure fell within the exception of Article XXIV:5 of GATT 1994 because 'the mechanism providing for the exclusion of free-trade area partners from safeguard measures' was established upon the formation of NAFTA, even though the specific safeguard on line pipe was adopted after NAFTA's formation.[30] On appeal, the Appellate Body found it unnecessary to review these findings and declared them to be 'moot' and 'of no legal effect'.[31] Therefore, although the panel's reasoning is instructive, it has no formal legal value.

The panel's approach adds a dose of pragmatism to the understanding of the word 'formation' in Article XXIV:5. Often, the parties to a customs union or an FTA will be unable to provide specifically for every conceivable eventuality upon the formation of the agreement. Therefore, a distinction should be drawn between general framework provisions introduced upon formation and specific implementing measures adopted subsequently, pursuant to the framework provisions. The exception under Article XXIV:5 should extend to the framework provisions and the implementing measures. However, to improve transparency and to allow WTO Members to scrutinise a PTA at the time of its adoption, the framework provisions should make plain the nature of the WTO-inconsistent measures envisaged and the circumstances in which they are likely to be adopted.

(b) Measures necessary for formation In *Turkey–Textiles*, the Appellate Body specified that Article XXIV:5 can be used as a defence for inconsistent measures adopted in connection with a customs union 'only to the extent that the formation of the customs union would be prevented if the introduction of the measure[s] were not allowed'.[32] Presumably this 'necessity test' would apply equally to FTAs.

27 GATT 1994, Article XIX:1(a); and the Safeguards Agreement, Articles 6–7.

28 This situation also raised questions regarding the extension of the exception in Article XXIV:5 of GATT 1994 to the Safeguards Agreement, as discussed further in section II.D.2 below.

29 Panel Report, *US–Line Pipe Safeguards*, para. 3.1. 30 *Ibid.*, note 128.

31 Appellate Body Report, *US–Line Pipe Safeguards*, paras. 198–9.

32 Appellate Body Report, *Turkey–Textiles*, para. 46. That appeal concerned a customs union rather than an FTA. However, a similar necessity test presumably applies to FTAs as the chapeau of Article XXIV:5 applies to both types of RTA.

If applied broadly, this test would mean that a PTA can only depart from GATT 1994 rules if the departure is necessary to the formation of the PTA.

However, it is not clear whether the necessity test applies solely to inconsistencies arising from the imposition of *external* trade restrictions or also to inconsistencies arising from the elimination of *internal* trade restrictions. Although the Appellate Body drew no distinction between these types of restrictions in formulating the test, that dispute concerned an inconsistency resulting from the introduction of restrictions on the *external* trade of a customs union. In particular, Turkey introduced nineteen quantitative restrictions on imports from India on the formation of a customs union with the European Union (EU).

In *US–Line Pipe Safeguards*, the panel noted the specific facts addressed in *Turkey–Textiles* and suggested that the necessity test does not apply to inconsistencies arising from the elimination of *internal* trade restrictions. The panel stated:

> [T]he elimination of 'duties and other restrictive regulations of commerce' between parties to a free-trade area . . . is the very raison d'être of any free-trade area. If the alleged violation of GATT 1994 forms part of the elimination of 'duties and other restrictive regulations of commerce', there can be no question of whether it is necessary for the elimination of 'duties and other restrictive regulations of commerce'.[33]

On appeal, the Appellate Body did not specifically address this finding, but it held that the panel's findings on Article XXIV were moot and of no legal effect.[34]

Nonetheless, there are good reasons for confining the Appellate Body's ruling in *Turkey–Textiles* to the facts before it and, therefore, applying a necessity test only to external trade restrictions. This approach is consistent with the purpose of the exception in Article XXIV:5. As discussed above, the exception in Article XXIV:5 aims to prevent increases in the level of external trade restrictions. Therefore it makes sense to impose an additional requirement of necessity on the introduction of any such restrictions. However, as reflected in the RTA Understanding, a key purpose of Article XXIV:5 is to promote the complete elimination of internal trade restrictions. The application of a necessity test to internal trade restrictions would undermine this purpose by requiring PTA parties to demonstrate that the elimination of each and every internal restriction is necessary to the formation of the PTA.

Moreover, as explained below, under Article XXIV:8, the parties to an FTA are required only to eliminate internal restrictions on 'substantially all' – but not all – trade. Therefore, under this provision, it is *never necessary* to eliminate *all* internal trade restrictions. The application of a necessity test, in this situation, could, therefore, mean that parties would be required to maintain some internal restrictions. Yet, the stated purpose of Article XXIV, as set out in the RTA Understanding, seeks

33 Panel Report, *US–Line Pipe Safeguards*, para. 7.148.
34 Appellate Body Report, *US–Line Pipe Safeguards*, paras. 198–9.

precisely to secure the elimination of *all* internal trade restrictions. The application of the necessity test would, therefore, prevent parties to a customs union or an FTA achieving the objectives of Article XXIV.

Moreover, it is difficult to see how WTO Members, panels, or the Appellate Body could determine whether the elimination of a particular trade restriction among PTA parties was necessary for the formation of the PTA, or why they should have jurisdiction to review such questions. Article XXIV:8 of GATT 1994 simply requires a PTA to eliminate trade restrictions on 'substantially all' internal trade. It focuses on the *level* of internal trade restrictions rather than the *type* of trade affected. It does not prescribe which restrictions should be removed and which maintained; nor does it provide criteria in this regard. Thus, the PTA parties have discretion as to which internal trade restrictions to eliminate and in which circumstances,[35] provided that restrictions are eliminated on substantially all trade. It would go beyond the role of panels and the Appellate Body to second-guess such decisions.[36] In addition, the panel in *US–Line Pipe Safeguards* gave the following example of the practical difficulties of applying a necessity test to internal trade restrictions:

> [A]ssume that an FTA eliminates duties on peanuts, but not cars. In the context of a necessity test, third countries could claim that it was not necessary to eliminate duties on peanuts to meet the 'substantially all the trade' threshold of Article XXIV:8(b), as that threshold could have been met by eliminating duties on cars. In such cases, it is difficult to imagine how a necessity requirement could ever be fulfilled.[37]

D. Exception to what? Extending the exception beyond GATT 1994

1. Agreement on textiles and clothing

On its face, the exception in Article XXIV:5 of GATT 1994 applies solely to inconsistencies with the provisions of 'this Agreement', that is GATT 1994 itself. The exception might not, therefore, justify PTA measures that are inconsistent with other WTO agreements. Remarking on this issue in a footnote in *Turkey–Textiles*, the Appellate Body observed that 'legal scholars' have taken the view that Article XXIV:5 provides an exception for inconsistencies with GATT provisions. It went on to note that the chapeau 'refers only to the provisions of the GATT 1994'.[38] Nonetheless, the Appellate Body considered that Article XXIV:5 could provide an exception for an inconsistency with Article 2.4 of the ATC because Article 2.4 itself

35 For example, Article 802.1 of NAFTA limits the exclusion of Canada and Mexico from safeguard measures to situations where imports from these countries do not account for a 'substantial share of total imports' and do not 'contribute importantly' to serious injury. Article 5.3 of the United States–Israel Free Trade Agreement limits the exclusion of safeguard measures to situations where imports from Israel are not 'a substantial cause of the serious injury'.

36 See DSU, Articles 3.2 and 19.2. 37 Panel Report, *US–Line Pipe Safeguards*, n. 137.

38 Appellate Body Report, *Turkey–Textiles*, n. 13.

permits restrictions introduced under 'relevant GATT 1994 provisions'. The Appellate Body considered that this explicit reference to GATT 1994 in Article 2.4 means that the exception in Article XXIV is 'incorporated in the ATC'.[39]

So which WTO provisions, in which other WTO agreements, are covered by the exception in Article XXIV:5? The Appellate Body's reasoning in *Turkey–Textiles* suggests that the exception does not extend automatically to all WTO provisions. In *Turkey–Textiles*, the extension was based on an express reference, in another covered agreement, to GATT 1994. In all likelihood, other extensions will also depend on the wording and context of the relevant provisions. This approach is supported by the general interpretative note to the WTO goods agreements, found in Annex 1A of the WTO Agreement. The note states that 'in the event of a conflict' between provisions of GATT 1994 and provisions of one of the other goods agreements, the latter prevails. If the exception in Article XXIV:5 permits a PTA measure that is inconsistent with another goods agreement, a conflict exists between GATT 1994 and the other agreement. If a panel automatically applied the GATT 1994 exception to the other agreement, without examining the specific context, this would be contrary to Annex 1A of the WTO Agreement.

2. Agreement on safeguards

One fertile area of dispute over the scope of the PTA exception in Article XXIV:5 concerns the Agreement on Safeguards.[40] Safeguard measures are imposed by WTO Members pursuant to both Article XIX of GATT 1994 and the provisions of the Agreement on Safeguards.[41] Articles I, XIII, and XIX of GATT 1994, as well as Article 2.2 of the Agreement on Safeguards, require that safeguard measures be applied on a non-discriminatory, MFN basis to imports of the relevant product from all sources. In some instances, a WTO Member has excluded PTA partner countries from the application of safeguard measures, claiming that such discriminatory application is permitted under Article XXIV. This situation may raise questions regarding the type of measures that benefit from the exception in Article XXIV:5, as discussed above,[42] and the requirement in Article XXIV:8 that PTAs eliminate internal trade restrictions on substantially all trade, as discussed below.[43]

Another problematic aspect of this issue is whether the exception in Article XXIV:5 extends to the MFN obligation in Article 2.2 of the Agreement on Safeguards. So far, the Appellate Body has not answered this question. However, as foreshadowed above,[44] the panel in *US–Line Pipe Safeguards* ruled that Article XXIV:5 of GATT 1994 can provide a defence to Article 2.2 of the Agreement on

39 *Ibid.*

40 See, e.g., Joost Pauwelyn, 'The Puzzle of WTO Safeguards and Regional Trade Agreements' (2004) 7(1) *Journal of International Economic Law* 109–42.

41 Appellate Body Report, *Korea–Dairy Safeguards*, para. 77.

42 See section II.C.2(a) and (b) above. 43 See section III.C and D below.

44 See section II.C.2(a) above.

Safeguards. The panel highlighted the 'close interrelation between Article XIX and the Safeguards Agreement', and the fact that 'safeguard measures subject to the provisions of the Safeguards Agreement are understood to be Article XIX measures'.[45] It noted that Article XXIV:5 provides a defence to the MFN obligations in Articles I, XIII, and XIX of GATT 1994[46] and that it would be 'incongruous' if it did not also provide a defence to the MFN obligation in Article 2.2 of the Agreement on Safeguards for the same measure.[47]

Although the Appellate Body declared the panel's findings on Article XXIV moot and of no legal effect,[48] the panel's reasoning on this issue is both compelling and faithful to the Appellate Body's rulings in *Turkey–Textiles* and in safeguard disputes. The panel extended the exception in Article XXIV:5 to a provision of another WTO agreement on the basis of specific language in the other agreement. Moreover, the Appellate Body has already recognised that the Agreement on Safeguards and Article XIX of GATT 1994 impose a single, cumulative set of obligations on the same measures – that is, safeguard measures.[49] The link is particularly strong in the case of the MFN obligation because this same obligation is imposed in both Article 2.2 of the Agreement on Safeguards and in Articles I, XIII and XIX of GATT 1994.

A further consideration in extending the exceptions in Article XXIV of GATT 1994 to the Agreement on Safeguards is the last sentence of footnote 1 to the latter agreement, which states:

> Nothing in [the Agreement on Safeguards] *prejudges* the interpretation of the relationship between Article XIX and paragraph 8 of Article XXIV of GATT 1994. (Emphasis added.)

The panel in *US–Line Pipe Safeguards* noted that this phrase deals with the relationship between *two provisions of GATT 1994* and *not* the relationship between the Agreement on Safeguards and Article XXIV. The panel, therefore, held that the footnote did not affect its conclusion that the application of Article XXIV to provisions of the Agreement on Safeguards should be determined by an examination of the Agreement on Safeguards itself, together with relevant provisions of GATT 1994.

3. Other WTO goods agreements

Similar questions could arise in relation to the effect of Article XXIV:5 of GATT 1994 on the provisions of other WTO agreements. For instance, a number of PTAs have adopted harmonised rules that differ from the WTO disciplines in the SPS Agreement and the TBT Agreement. Based on the existing jurisprudence on Article XXIV:5, the extension of the exception to provisions of these or other WTO agreements will depend on whether there is a 'close interrelation' between the provisions and GATT 1994.

45 Panel Report, *US–Line Pipe Safeguards*, para. 7.150. 46 *Ibid.*, para. 7.146. 47 *Ibid.*, para. 7.150.
48 Appellate Body Report, *US–Line Pipe Safeguards*, paras. 198–9.
49 Appellate Body Report, *Korea–Dairy Safeguards*, para. 77.

While the approaches of the panel and Appellate Body in *US–Line Pipe Safeguards* are firmly rooted in the language of Article XXIV:5, it may be questioned whether that provision, dating from GATT 1947, remains appropriate for a legal framework that now comprises twelve separate agreements dealing with goods, in addition to GATT 1994. Article XXIV expresses a policy decision by WTO Members to accept the inevitable positive discrimination that PTAs create in favour of the PTA parties. If Members accept this discrimination for all of the obligations in GATT 1994, as well as for certain obligations in other WTO goods agreements that have a 'close interrelation' with GATT 1994, what reason could there be not to extend the exceptions to all obligations in the WTO goods agreements?

The legal framework for goods may be contrasted with the framework for services where there is no doubt that the PTA exception applies to all services obligations.[50] Applying the PTA exception in Article XXIV:5 of GATT 1994 to only some goods-related obligations might imply the existence of a hierarchy of norms among the goods obligations, with some being subject to the exception but not others. However, it does not seem that the Members intended to establish such a hierarchy. Rather, the exception in Article XXIV:5 originally extended to all goods-related obligations – that is, to all obligations under GATT 1947. As negotiators gradually extended the number and scope of goods agreements, they did not expressly extend the exception in Article XXIV:5. In the absence of such express clarification, panels and the Appellate Body cannot apply the exception automatically to all goods-related obligations. Rather, they must strive to translate the ambiguous textual indications into a workable system of rights and obligations. The current climate of uncertainty, and possible dissatisfaction with the existing jurisprudence, may provide the necessary impetus for Members to reach a specific agreement on this question in the ongoing negotiations.

III. Eliminating restrictions on trade within the PTA: Article XXIV:8(a)(i) and (b)

A. Introduction

As already mentioned, Article XXIV:8 of GATT 1994 defines 'customs union' and 'free-trade area'. To benefit from the exception in Article XXIV:5, a PTA must meet one of these definitions. Both types of PTA are defined by the elimination of internal trade restrictions. For customs unions, this requirement is contained in Article XXIV:8(a)(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

50 GATS, Article V.

> the union or at least with respect to substantially all the trade in products originating in such territories . . .

For FTAs, the corresponding requirement is contained in Article XXIV:8(b):

> 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.

Thus, both customs unions and FTAs: (a) require the elimination of restrictions on 'substantially all the trade' between the PTA parties; (b) define the restrictions that must be eliminated as duties and 'other restrictive regulations of commerce' (ORRCs); and (c) expressly allow the maintenance of certain restrictions, 'where necessary', namely 'those permitted under Articles XI, XII, XIII, XIV, XV and XX' of GATT 1994.

Before turning to an examination of these three common elements, we point out a difference in these provisions regarding the origin of goods traded between PTA parties. In the case of customs unions, internal restrictions must be eliminated either on substantially all trade between the parties, or on substantially all trade in products originating in the parties. The first option is more trade-liberalising, because it entails the elimination of restrictions on trade in any goods, irrespective of where the goods originate. In contrast, the second option entails the elimination of trade restrictions only on goods originating within the customs union. In the case of FTAs, only the second of these options is available. That is, internal restrictions must be eliminated on substantially all trade 'in products originating' within the FTA.

B. Measuring 'substantially all the trade'

1. Members' views

The meaning of 'substantially all the trade' in Article XXIV:8 has given rise to much discussion over the years. To date, WTO Members have been unable to agree on the proportion of trade that amounts to 'substantially' all trade,[51] or how 'all the trade' within a PTA is to be measured.[52] However, two overlapping approaches have gained currency. First, a *qualitative* approach, which would require the elimination of restrictions with respect to every major sector of the economies of the PTA parties. Second, a *quantitative* approach, which relies on a statistical threshold, for example requiring the elimination of restrictions with respect to a predefined percentage of trade.

51 New Zealand has even suggested, in view of the many difficulties surrounding the word 'substantially', that the word should be 'removed' from Article XXIV:8: WTO Committee on Regional Trade Agreements, *Note on the Meetings of 16–18 and 20 February 1998*, WT/REG/M/16 (18 March 1998), para. 115.

52 WTO Committee on Regional Trade Agreements, *Coverage, Liberalization Process and Transitional Provisions in Regional Trade Agreements: Background Survey by the Secretariat*, WT/REG/W/46 (5 April 2002).

The qualitative approach is designed to prevent PTA parties from maintaining restrictions to protect important sectors from competition within the PTA. The rationale would seem to be that an exception to WTO rules should only be granted when the parties to a regional agreement have shown commitment to closer economic integration. If the parties exclude major economic sectors from liberalisation, that commitment is deemed lacking. If this approach were adopted, it would be likely to operate in conjunction with a quantitative criterion, and rules would be required to determine what constitutes a major economic sector.

Under the quantitative approach, one suggestion is that internal restrictions should be eliminated on 95 per cent of all Harmonised Commodity Description and Coding System (HS) tariff lines at the six digit level. Tariff lines can be used as a criterion to ensure that liberalisation covers all possible or potential trade between the PTA parties, because all goods fall within a tariff line. However, using tariff lines may give a misleading impression of the extent to which trade has been liberalised, for instance where actual trade flows between the PTA parties are concentrated in a few tariff lines. If restrictions on these few tariff lines were maintained, a large share of current trade could escape liberalisation.[53] Conversely, a large number of tariff lines may be devoted to a small amount of actual trade. For example, around a quarter of all HS tariff lines deal with agricultural products, which may account for only a small portion of actual trade.[54]

Trade flows provide an alternative to tariff lines in establishing the threshold of trade for which restrictions must be eliminated. Thus, for example, the elimination of internal restrictions could be required with respect to 95 per cent of all trade flows between the PTA parties. However, using trade flows as a criterion is also problematic. First, actual trade flows are distorted by trade restrictions and do not necessarily reflect the likely trade volumes if restrictions were eliminated.[55] Second, difficulties arise in applying this criterion. For example, a threshold of 95 per cent of all trade could be measured either as a proportion of aggregate trade flowing between the parties or as a proportion of each party's individual trade with the other. To take the simplest case, where there are only two PTA parties,[56] suppose that Country A exports to Country B are valued at US$95m, and Country B exports

53 For instance, the EC has pointed out that in agreements involving the Faroe Islands, 'well under 50 tariff lines accounted for about 80 per cent of the trade'. Norway, likewise, has observed that in a Faroe Islands–Norway Free Trade Agreement, all of the trade between the two parties was conducted under just ten tariff lines. WTO Committee on Regional Trade Agreements, *Note on the meetings of 16–18 and 20 February 1998*, WT/REG/M/16 (18 March 1998), paras. 118 and 125.

54 WTO Committee on Regional Trade Agreements, *Note on the Meetings of 23–24 September 1998*, WT/REG/M/19 (16 October 1998), para. 18.

55 See generally WTO Committee on Regional Trade Agreements, *Communication from Australia*, WT/REG/W/22 (30 January 1998) and Add.1 (24 April 1998). See also WTO Committee on Regional Trade Agreements, *Note on the meetings of 16–18 and 20 February 1998*, WT/REG/M/16 (18 March 1998), para. 112.

56 The situation becomes even more complicated for RTAs with three or more parties.

to Country A are valued at US$5m. Using an aggregate measure, the two countries would need to eliminate internal trade restrictions on 95 per cent of the total trade, valued at US$100m. The parties would have discretion as to which part of the total trade to liberalise,[57] and they could even agree simply that Country B would eliminate all restrictions on Country A imports. In contrast, using an individual measure, each country would have to eliminate trade restrictions on 95 per cent of the imports from the other country.

The question of how to calculate trade flows in applying a quantitative approach to 'substantially all the trade' could be of particular importance in the case of North–South agreements, where the parties may wish to liberalise trade unequally. Using an aggregate measure, developing countries might be able to benefit from the elimination of restrictions on a greater share of their exports to a developed country party. Alternatively, WTO Members might consider it preferable to prescribe individual measurement, in order to prevent one PTA party from forcing another, in a weaker bargaining position, to accept a lower degree of liberalisation.

In order to measure 'substantially all the trade' between FTA parties 'in products originating' in those parties under Article XXIV: 8(b), rules are required to determine whether goods 'originated' within the PTA. Such rules are also needed in connection with a customs union if the parties chose to eliminate restrictions not with respect to substantially all trade between them, but only with respect to substantially all trade in products originating in the parties' territories.

Rules of origin are used to decide in which country goods are produced and, therefore, in a PTA setting, whether they qualify for a tariff preference.[58] In FTAs, the parties often adopt special rules of origin to determine which goods qualify for preferential treatment in the PTA. The preferential rules may apply much stricter qualifying conditions than the rules of origin generally used in MFN trade.[59] Thus, goods that are deemed to originate in one PTA party under the general rules of origin may not be treated as originating in that party under preferential rules of origin. Such special rules of origin may, therefore, narrow the scope of trade that is liberalised within a PTA. This has led some Members to suggest that the measurement of 'substantially all the trade' should take into account preferential rules of origin. For example, 'all the trade' within a PTA in products originating in the PTA parties could be measured using MFN rules of origin, while the proportion that is liberalised could be measured using the preferential rules of origin applying within that PTA.[60]

57 See WTO Committee on Regional Trade Agreements, *Communication from Australia – Addendum*, WT/REG/W/22/Add.1 (24 April 1998).

58 The WTO imposes limited disciplines on rules of origin under the Agreement on Rules of Origin.

59 Preferential rules of origin are not subject to the general obligations in the Agreement on Rules of Origin, although they are subject to certain transparency requirements in the Common Declaration with Regard to Preferential Rules of Origin in Annex II of that Agreement.

60 See, e.g., WTO Committee on Regional Trade Agreements, *Note on the meetings of 6–7 and 10 July 1998*, WT/REG/M/18 (22 July 1998), para. 19.

2. Interpretation in dispute settlement

Although the Members have yet to agree on a meaning for the term 'substantially all the trade', panels or the Appellate Body may be called upon to interpret the term in dispute settlement. So, far, neither the Appellate Body nor any panel has provided a detailed interpretation of this notion. In *Turkey–Textiles*, the Appellate Body noted that 'substantially all the trade' is not the same as all the trade, but that it 'is something considerably more than merely *some* of the trade'.[61] Therefore, the relevant amount of trade falls somewhere between some and all trade among the PTA parties. Beyond this, the disputes provide little guidance. In order to prove that NAFTA complied with Article XXIV:8(b) in *US–Line Pipe Safeguards*, the US submitted evidence that NAFTA eliminated 'duties on 97 per cent of the Parties' tariff lines, representing more than 99 per cent of the trade among them in terms of volume'.[62] After reviewing the evidence, and without offering any views on the meaning of 'substantially all the trade', the panel held that the US had established a *prima facie* case that NAFTA met the definition of an FTA under Article XXIV:8 (b).[63] The Appellate Body took the view that it need not address this finding and declared it to be of no legal effect.[64]

It is perhaps unrealistic and inappropriate to expect that panels or the Appellate Body will develop a refined formula for identifying 'substantially all the trade'. For instance, it would be difficult for a panel to find a textual basis for a finding that a precise threshold of 90 per cent is never 'substantial' but that a precise threshold of 95 per cent always is. If the clarification of this notion is left to panels and the Appellate Body, it is more likely that they will develop a flexible test premised on the word 'substantial', which indicates that the elimination of internal restrictions must cover a very considerable proportion of the trade between the parties. The words 'all trade' will also be important, as they identify the broad base against which internal liberalisation is to be measured. In each case, panels are likely to reach a conclusion based on the specific facts at issue, probably taking account of the qualitative and quantitative factors discussed by the Members.

C. Eliminating 'duties and other restrictive regulations of commerce'

A second question arising from the definitions of customs unions and FTAs is which trade restrictions are to be eliminated. According to Article XXIV:8(a)(i) and (b), the parties to a customs union or an FTA must eliminate duties and ORRCs on substantially all the trade within the PTA. WTO Members have frequently discussed the words 'duties and other restrictive regulations of commerce', without reaching

61 Appellate Body Report, *Turkey–Textiles*, para. 48 (original emphasis).
62 Panel Report, *US–Line Pipe Safeguards*, para. 7.142. 63 Ibid., para. 7.144.
64 Appellate Body Report, *US–Line Pipe Safeguards*, paras. 198–9.

any agreement on their meaning. Similarly, no panel or Appellate Body reports to date have interpreted these words. While the words 'substantially all the trade' dictate how much trade must be liberalised within a PTA, the words 'duties and other restrictive regulations of commerce' describe the types of restriction to be eliminated. Evidently, elimination of a broader range of restrictive regulations will result in a higher level of liberalisation within the PTA, in accordance with the purpose of the exception in Article XXIV:5.

What seems important, in determining which regulations constitute ORRCs, is not the form of a regulation, but its effect on commerce. The requirement of elimination applies only to regulations that have a 'restrictive' effect on commerce, irrespective of whether the regulation imposes duties or takes some other form. Article XXIV:8 does not state expressly what kind of restrictive effect is intended. Virtually all regulations affecting goods have some kind of 'chilling' effect that restricts trade in those goods. This is equally true of border regulations, which chill imports, and marketplace regulations,[65] which chill trade in domestic and imported goods. It seems rather unlikely, though, that Article XXIV:8 was intended to encompass all regulations that have a restrictive effect on trade, however small. It is worth noting that the RTA Understanding refers to the 'elimination *between the constituent territories* of duties and other restrictive regulations of commerce' (emphasis added). This suggests that the regulations to be eliminated under Article XXIV:8 are those restricting the cross-border movement of goods between the PTA parties. The focus of internal liberalisation under Article XXIV:8 is, in other words, on restrictions that adversely affect imported or exported goods, with the goal being to create a market among the parties that is border free rather than regulation free.

So what types of restrictions are duties or ORRCs pursuant to Article XXIV:8? By definition, border restrictions apply solely to imports, imposing restrictions on the cross-border movement of goods, and they are certainly ORRCs. These include import bans, quantitative restrictions, and the many administrative rules regulating importation. Sanitary and phytosanitary (SPS) measures prohibiting the importation of goods would also be ORRCs. ORRCs are also likely to include marketplace regulations that adversely affect imported goods, as compared with domestic goods, but such regulations would likely be already proscribed by the WTO national treatment obligation.[66]

Much discussion among academics and WTO negotiators has focused on whether trade remedy measures are ORRCs. Measures adopted under Article VI (anti-dumping and countervailing measures) or XIX (safeguard measures) of GATT 1994 are not expressly identified in the bracketed phrase in Article XXIV:8, ('except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX'), which is discussed further below.[67] The exclusion of trade remedy measures from

65 Marketplace regulations regulate, for example, the distribution, transport, marketing or sale of goods.
66 GATT 1994, Article III. 67 See section III.D.2 below.

this phrase could mean that trade remedy measures are simply not ORRCs (in which case there was no need to include them in the brackets and they are not subject to the elimination requirement). However, it could also be that they are ORRCs and their exclusion from the brackets means there is no express right to maintain them (in which case they should be eliminated on substantially all the trade between the PTA parties).[68]

The text of Article XXIV:8 contains little support for excluding trade remedy measures from the measures that need to be eliminated, i.e., duties and ORRCs.[69] Anti-dumping and countervailing duties are described as 'duties' in Articles II and VI of GATT 1994, as well as in the Anti-Dumping Agreement and the SCM Agreement. These 'duties' are imposed, in addition to ordinary customs duties, on the importation of products. Moreover, the very purpose of these duties is to restrict imports of specific products. Under Article XIX of GATT 1994, safeguard measures involve the modification or withdrawal of a market access concession for imported goods. The purpose of safeguard measures is, therefore, also to restrict imports. The restriction on access takes the form of either a duty or a quantitative restriction. Again, there is little reason to suppose that safeguard measures are not ORRCs.[70]

D. Internal restrictions that may be maintained

1. Restrictions on an 'insubstantial' portion of trade

Under Article XXIV:8, the PTA parties need not eliminate all ORRCs; they must simply eliminate ORRCs on 'substantially all the trade' between the parties. On the remaining portion of trade, the parties are entitled to retain all ORRCs of any type (provided that they are not otherwise inconsistent with WTO rules), including trade remedy measures and other measures not listed in the brackets. But difficult questions remain.

If the PTA parties decide to retain the possibility of imposing trade remedy measures on each other, the PTA is likely to include a general authority for each party to impose such measures in specific cases in the future. This general authority, of itself, might be regarded as an ORRC on all the products that are potentially subject to trade remedy measures at a later stage. In this case, restrictions would be

68 WTO Negotiating Group on Rules, *Compendium of Issues Related to Regional Trade Agreements – Background Note by the Secretariat (Revision)*, TN/RL/W/8/Rev.1 (1 August 2002), para. 74.

69 Cf. Angela T. Gobbi Estrella and Gary N. Horlick, 'Mandatory Abolition of Anti-Dumping, Countervailing Duties and Safeguards in Customs Unions and Free-Trade Areas constituted between WTO Members: Revisiting a Long-Standing Discussion in Light of the Appellate Body's *Turkey–Textiles Ruling*' (2006) 40(5) *Journal of World Trade* 909–44.

70 The panel in *Argentina–Footwear Safeguards* assumed that safeguard measures are 'duties and other restrictive regulations of commerce' under Article XXIV:8: paras. 8.96–8.97. The Appellate Body reversed the panel's findings on Article XXIV: Appellate Body Report, *Argentina–Footwear Safeguards*, para. 110. However, this aspect of the panel's findings on Article XXIV was not examined by the Appellate Body nor specifically declared to be an erroneous interpretation of Article XXIV:8.

deemed to remain on all the products potentially subject to trade remedy measures. To comply with the requirement to eliminate restrictions on substantially all the trade, PTA parties would have to confine the general authority to a defined group of products representing no more than an insubstantial portion of trade.

Alternatively, it could be argued that the general authority does not, in fact, restrict commerce; it merely enables a potential future restriction, which might never be realised. On that view, the general authority is not an ORRC and need not be limited to particular products representing an insubstantial portion of trade. Rather, specific measures imposed pursuant to the general authority are ORRCs and must be limited to such a portion.[71] This approach is also problematic. It would leave undefined and uncertain the number and type of ORRCs that could be imposed within the PTA and, hence, the proportion of trade subject to ORRCs. As a result, the consistency of the PTA with the conditions of the exception in Article XXIV:5 of GATT 1994 would vary, depending on the number and extent of trade remedy measures imposed at any given time. It would be impossible to state definitively, based merely on the PTA itself, whether it was justified under the exception.

2. Other restrictions expressly permitted

Although Articles XXIV:8(a)(i) and (b) state that, in a customs union or an FTA, restrictive regulations of commerce must be eliminated on substantially all internal trade, both paragraphs create an exception to this requirement, 'where necessary', for 'those' ORRCs 'permitted under Articles XI, XII, XIII, XIV, XV and XX'.

Some WTO Members have suggested that the bracketed list of measures is illustrative only. In other words, measures apart from those 'permitted under Articles XI, XII, XIII, XIV, XV and XX', such as trade remedy measures, may also be implicitly included in the list and maintained within a PTA.[72] This argument has not won the support of all Members. In any case, since the bracketed list provides an exception to the general rule of elimination of ORRCs, it would normally be interpreted in a manner precluding the addition of other measures. This approach is consistent with the Appellate Body's statement in *Turkey–Textiles* that the bracketed phrase allows parties to maintain measures 'otherwise permitted under Articles XI through XV and under Article XX of the GATT 1994'.[73] While not a definitive ruling on this issue, this statement suggests that the Appellate Body would read the

71 This seems to be the approach suggested in Panel Report, *Argentina–Footwear Safeguards*, para. 8.97. See *ibid.*

72 WTO Negotiating Group on Rules, *Compendium of Issues Related to Regional Trade Agreements – Background Note by the Secretariat (Revision)*, TN/RL/W/8/Rev.1 (1 August 2002), para. 75. The WTO Secretariat has observed that '[t]he drafting history does not indicate why Articles XI–XV and XX were included in the list of exceptions while others, in particular Article XIX, were not included': WTO Committee on Regional Trade Agreements, *Systemic Issues Related to 'Other Regulations of Commerce': Background Note by the Secretariat (Revision)*, WT/REG/W/17/Rev.1 (5 February 1998), para. 6.

73 Appellate Body Report, *Turkey–Textiles*, para. 48.

bracketed phrase as containing an exclusive list of the ORRCs that may be maintained in a PTA.[74]

In *Turkey–Textiles*, the Appellate Body recognised that this exception to the general requirement of elimination of ORRCs offers 'some flexibility' to the parties to a customs union (and presumably also an FTA) to maintain certain types of ORRCs.[75] However, the Appellate Body cautioned that this flexibility is limited by the requirement that ORRCs be eliminated with respect to substantially all internal trade. In addition, the exception applies only 'where necessary', although the text provides no guidance as to when it is necessary to maintain restrictions. In *Turkey–Textiles*, the Appellate Body developed and applied a necessity test to the exception for PTAs in Article XXIV:5 of GATT 1994.[76] A similar test could also be applied to the bracketed phrase in Article XXIV:8. In that context, to the extent that the formation of a PTA would be prevented if an ORRC listed in that phrase were eliminated, it could be regarded as 'necessary' to maintain the ORRC.

An interesting and, as yet, unresolved question is whether products subject to ORRCs listed in the brackets are part of the 'substantial' or 'insubstantial' portion of trade. The question can be illustrated by example. Suppose a WTO Member maintains quantitative restrictions, under Article XII, on imports of all steel products from partner countries in a PTA. No duties or other restrictions are imposed on steel imports. In measuring whether ORRCs have been eliminated on substantially all the trade in the PTA, should steel products be counted as trade on which ORRCs have been eliminated (the substantial portion of trade) or as trade on which ORRCs have not been eliminated (the insubstantial portion of trade)?

The straightforward – and stricter – view is that trade in any product subject to an ORRC has not been liberalised, and the product cannot form part of the substantial portion of trade on which ORRCs have been eliminated. On this view, the substantial portion of trade is confined to products that are subject to no ORRCs at all; conversely, a product that is subject to any ORRC, including an ORRC listed in the brackets, must form part of the insubstantial portion of trade.[77]

This reading is, however, problematic. The list of ORRCs in brackets includes, among others, restrictions maintained pursuant to Article XX of GATT 1994. Article

74 It may be that certain measures permitted under Article XXI of GATT 1994 in connection with essential security interests are also permitted by Article XX, perhaps as necessary to protect human, animal or plant life or health, or even public morals.

75 Appellate Body Report, *Turkey–Textiles*, para. 48. The Appellate Body was examining a case involving a customs union and not an FTA. However, the text of Article XXIV:8 is the same in this regard for customs unions and FTAs.

76 See section II.C.2.(b) above.

77 It is not clear whether the advocates of this approach take the view that the only restrictive regulations that may be applied to any product are those mentioned in the brackets. Contrary to this view, we have suggested that the parties are free to retain any restrictive regulations they wish on products representing an insubstantial portion of trade because Article XXIV:8 requires only the elimination of restrictions on the substantial portion of trade.

XX provides a general exception to all GATT 1994 obligations. In certain circumstances, Article XX allows Members to promote governance priorities – such as public health and environmental protection – that conflict with WTO rules. WTO-consistent SPS measures are also covered by Article XX[78] and, in all likelihood, so are most WTO-consistent technical barriers to trade (TBTs). There is broad recognition in the WTO agreements, and among WTO Members, that Members should have discretion to pursue these other priorities, subject to the conditions governing the exceptions to WTO rules. However, if a product subject to health restrictions permitted by Article XX necessarily formed part of the insubstantial portion of trade on which ORRCs had not been eliminated, this would constrain WTO Members' right to pursue health objectives. In a customs union or an FTA, a WTO Member would be able to promote health only through internal restrictions on the 'insubstantial' group of products. As well as being questionable in terms of state sovereignty, this reading of Article XXIV:8 would be at odds with the text of Article XX. Article XX(b) states that 'nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures . . . necessary to protect human, animal or plant life or health'. If Article XXIV:8 of GATT 1994 meant that Article XX health measures could only be maintained on the insubstantial portion of trade, that interpretation would 'prevent' the adoption or enforcement of health measures on 'substantially all the trade', contrary to Article XX.

An alternative reading follows from the structure of Articles XXIV:8(a)(i) and (b). These two sub-paragraphs require that a PTA eliminate all ORRCs – except those bracketed – on substantially all trade. The bracketed exception is located immediately after the phrase 'duties and other restrictive regulations of commerce' and, together with this phrase, defines the universe of restrictions that must be eliminated with respect to substantially all trade. Thus, for products comprising substantially all trade, all ORRCs must be eliminated except those listed in the brackets. This reading, therefore, creates, three categories of product under Article XXIV:8:

- First, products that are not subject to ORRCs at all. These products form part of the 'substantial' portion of trade with respect to which all ORRCs have been eliminated.
- Second, products that are not subject to ORRCs, except for one or more of those listed in the brackets. These products also form part of the 'substantial' portion of trade with respect to which ORRCs, other than those listed in the brackets, have been eliminated.
- Third, products that are subject to ORRCs that are not listed in the brackets. These products must represent no more than an 'insubstantial' portion of trade,

78 See SPS Agreement, Article 2.4.

with respect to which ORRCs need not be eliminated. These products may also be subject to ORRCs listed in the brackets.

Under this reading, WTO Members would be entitled to maintain, 'where necessary', any of the ORRCs listed in the brackets with respect to any product. In addition, they would be entitled to maintain any ORRCs with respect to an insubstantial portion of trade. This reading of Article XXIV:8 would, therefore, avoid the problem of constraining Members from maintaining measures permitted under Article XX.

IV. Restrictions on the external trade of the PTA

A. Introduction

As we have seen in the previous section of this chapter, Article XXIV:8 of GATT 1994 imposes certain conditions on the restrictions imposed by PTA parties on trade within the PTA. In addition, as we shall see in the following sections, Article XXIV of GATT 1994 imposes two conditions on the restrictions applied by PTA parties in the external trade of the PTA.

First, under Article XXIV:8(a)(ii), the definition of a customs union requires each of the parties to the union to apply 'substantially the same duties and other regulations of commerce to the trade of territories not included in the union'.[79] This condition applies only to customs unions and not to FTAs.

Second, under Articles XXIV:5(a) and (b), a PTA will not qualify for the PTA exception under Article XXIV:5 if, broadly speaking, the 'duties and other regulations of commerce' imposed by the PTA parties on other WTO Members are higher or more restrictive than before the PTA was formed. The precise character of this condition differs for customs unions and FTAs. For customs unions, the condition is framed as follows under Article XXIV:5(a):

> [T]he duties and other regulations of commerce imposed at the institution of [a customs union] in respect of trade with [WTO Members] not parties to such union ... shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union ...

For FTAs, the condition is contained in Article XXIV:5(b):

> [T]he duties and other regulations of commerce maintained in each [of] the constituent territories and applicable at the formation of [an FTA] to the trade of [WTO Members] not included in such area ... shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the same constituent territories prior to the formation of the free-trade area ...

79 This requirement is expressly subject to Article XXIV:9, which relates to preferences in respect of import duties or charges as described in GATT 1994, Article I:2.

Sub-paragraphs 5(a), 5(b), and 8(a)(ii) of Articles XXIV all impose conditions on the 'duties and other regulations of commerce' imposed by PTA parties on external trade. We examine the meaning of these words before turning to the specific requirements of the different provisions.

B. The meaning of 'duties and other regulations of commerce'

1. Structure and context of the relevant provisions

In our view, it makes sense to interpret the words 'duties and other regulations of commerce' consistently in sub-paragraphs 5(a), 5(b), and 8(a)(ii) of Articles XXIV, mindful of the different context in which they appear.

The words 'duties and other regulations of commerce' in sub-paragraphs 5(a), 5(b), and 8(a)(ii) of Articles XXIV are reminiscent of the words 'duties and other restrictive regulations of commerce' in sub-paragraphs 8(a)(i) and 8(b) of Article XXIV, examined earlier in the context of the conditions imposed on internal trade restrictions. The key difference is that the word 'restrictive' is absent in the context of external trade. However, although this is not formally part of the definition of 'other regulations of commerce' (ORCs), sub-paragraphs 5(a) and 5(b) of Article XXIV are concerned with the 'restrictiveness' of ORCs.

Sub-paragraphs 5(a) and 8(a)(ii) form a coherent pair, both dealing with customs unions. Under sub-paragraph 8(a)(ii), the parties to a customs union must 'substantially' harmonise duties and ORCs applied to the trade of countries that are not party to the PTA (whether or not they are WTO Members); sub-paragraph 5(a) requires that the newly harmonised ORCs, plus any remaining un-harmonised ORCs, applied in respect of trade with WTO Members that are not party to the PTA, be no more restrictive than the ORCs previously applied in respect of such trade. Thus, the ORCs described in sub-paragraph 5(a) (i.e., ORCs applied to WTO Members) form a subset of the ORCs that must be harmonised under sub-paragraph 8(a)(ii) (i.e., all ORCS). Sub-paragraph 5(b) relates to FTAs and, like sub-paragraph 5(a), it addresses ORCs applied in respect of trade with WTO Members that are not party to the PTA. In the remainder of the discussion in this section of the meaning of 'duties and other regulations of commerce', we use the words 'external trade' or 'trade with third countries' as a convenient way of referring to the trade of countries that are not party to the PTA (in the context of Article XXIV:8(a)(ii)) and to trade with WTO Members that are not party to the PTA (in the context of Article XXIV:5(a) and (b)).

2. Examples of regulations of commerce

PTA parties could impose various measures that could potentially constitute ORCs, including:

- border measures regulating either the import of goods from third countries or the export of goods to third countries; and

- marketplace measures that may be applicable: solely to goods of third countries; to goods of both third countries and PTA parties; or solely to goods of PTA parties.

(a) Border measures It seems clear, and relatively uncontroversial, that the ORCs relevant to sub-paragraphs 5(a), 5(b), and 8(a)(ii) of Article XXIV include border measures applied to imports from third countries, as these measures are certainly imposed on, or applied to, external trade. These measures include customs duties and similar charges, import prohibitions, quantitative restrictions, and administrative rules regulating importation. Administrative rules might include rules of origin used to distinguish between imports of goods originating in a PTA party and those originating in a third country, and prohibition of imports from third countries that do not comply with certain SPS or TBT standards. Moreover, these measures are ORCs whether they are applied individually by one PTA party or, in the case of a customs union, by all parties.

Border measures that restrict exports from PTA parties to third countries are more problematic. During the Uruguay Round, one proposal was that the words 'duties and other regulations of commerce' should be interpreted to cover 'all border measures taken in connection with importation or exportation which have a differential impact on imported products as compared to domestic products'.[80] This proposal was rejected due to, among other things, the inclusion of the word 'exportation'. This might suggest that the negotiators did not agree that ORCs included export measures.

A further difficulty with interpreting ORCs as including border measures on exports is that such measures are generally applied by PTA parties to their own goods when destined for third-country markets[81] and therefore cannot be described as being applicable or applied 'to the trade *of*' third countries within the meaning of Articles XXIV:5(b) and 8(a)(ii). However, in the context of customs unions, Article XXIV:5(a) refers to measures 'imposed . . . in respect of trade *with*' third countries. This language might be broad enough to encompass export measures. This could mean that, on the one hand, export measures are not relevant to the determination under Article XXIV:8(a)(ii) of whether the parties to a customs union apply substantially the same ORCs to other countries, nor to the determination under Article XXIV:5(b) of whether the parties to an FTA impose higher or more restrictive ORCs on other Members; but, on the other hand, export measures are relevant to the determination under Article XXIV:5(a) of whether the parties to a *customs union* impose higher or more restrictive ORCs on other Members. It is unclear whether the drafters intended this distinction.

80 WTO Committee on Regional Trade Agreements, see above n. 72, para. 10.

81 Export measures may also restrict the re-exportation of (processed) goods imported from third countries.

(b) Marketplace measures During the Uruguay Round, a second proposal was for 'duties and other regulations of commerce' to be interpreted as covering 'all duties and charges and measures imposed on or in connection with importation or exportation'.[82] This proposal was also rejected, primarily because of differing opinions as to whether ORCs include internal measures such as sales taxes and price controls. In the end, no agreement was reached on an authoritative interpretation of 'duties and other regulations of commerce', and no explicit guidance was included as to whether these words cover internal or 'marketplace' measures.

The Appellate Body has read Article XXIV:8(a)(ii) as requiring the parties to a customs union to adopt 'a common external trade regime'.[83] In other words, it appears to be assumed that parties are not obliged by Article XXIV:8(a)(ii) to harmonise internal marketplace measures (in addition to eliminating internal restrictions on trade under Article XXIV:8(a)(i)). This approach is supported by the context and purpose of Article XXIV:8(a)(ii). Read together with the chapeau of Article XXIV:8, sub-paragraph 8(a)(ii) states that a 'customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that ... substantially the same duties and other regulations of commerce are applied ... to the trade of territories not included in the union'. The use of the word 'customs' in the chapeau indicates that the provision focuses on border measures. Moreover, it would be rather intrusive if WTO rules required parties to apply 'substantially the same' marketplace measures on goods, whether such a requirement was limited to goods from third countries or extended to goods from within the PTA. Such a rule would be particularly broad, given that Article XXIV:8(a)(ii) is not limited to 'restrictive' regulations of commerce, and it would also not necessarily further the purpose of maximising the liberalising effects of the PTA on trade between PTA parties and minimising the trade restrictive effects on other WTO Members.

The language of Articles XXIV:5(a) and (b) suggests that the ORCs that must not be 'higher or more restrictive' do not include marketplace measures. In relation to customs unions, as already noted, Article XXIV:5(a) refers to ORCs imposed 'in respect of trade with' other WTO Members. Thus, the focus is on trade between a PTA party and another Member, rather than on trade within the PTA party. In relation to FTAs, Article XXIV:5(b) refers to ORCs 'maintained in ... and applicable ... to the trade of' other WTO Members. This wording might more easily extend to marketplace measures. However, the use of the word 'trade' (as opposed to 'goods') may well signify that the focus is not on the treatment of goods of other Members within the PTA, but on the treatment of such goods at the border.

Some Members have argued that certain marketplace measures imposed by PTA parties solely on goods originating within the PTA might restrict external trade and

82 WTO Committee on Regional Trade Agreements, see above n. 72.

83 Appellate Body Report, *Turkey–Textiles*, para. 49.

therefore be relevant ORCs under these three sub-paragraphs.[84] Examples of such measures, drawn from existing PTAs, include the application of lower SPS or TBT standards[85] on internal PTA trade or the replacement of anti-dumping measures within the PTA with competition rules.[86] These harmonised rules apply solely to goods from PTA parties; the normal WTO rules apply to goods from third countries.[87]

It is difficult to know how to treat measures that apply solely to goods from PTA parties but may have a distortive effect on trade with third countries. ORCs are described as measures 'imposed ... in respect of' (Article XXIV:5(a)), 'applicable ... to' (Article XXIV:5(b)), or 'applied ... to' (Article XXIV:8(a)(ii)) the relevant trade. The verbs 'impose' and 'apply' suggest that relevant ORCs are measures that directly regulate trade with third countries and not measures that merely have an indirect effect on trade with third countries. This perhaps indicates that marketplace measures 'imposed' only on goods from PTA parties are not ORCs and, therefore, do not need to be harmonised in customs unions (under Article XXIV:8(ii)) or included in determining the level of restrictions on external trade in any PTA (under Articles XXIV:5(a) and (b)). Moreover, these harmonised rules arise from internal liberalisation within the PTA, which some have argued means that they should not be regarded as barriers to trade with third countries.[88] However, it is difficult to reconcile this with the twin purpose of the PTA exception in Article XXIV:5, given that these harmonised rules may well distort or restrict trade from third countries.

C. Substantially the same external restrictions in customs unions: GATT Article XXIV:8(a)(ii)

Article XXIV:8(a)(ii) requires the parties to a customs union to apply 'substantially the same duties and other regulations of commerce ... to the trade of territories not included in the union'. This requirement has been described as creating 'a

84 WTO Committee on Regional Trade Agreements, *Note on the Meetings of 6–7 and 10 July 1998*, WT/REG/M/18 (22 July 1998), paras. 40–6.

85 The application of two different SPS or TBT regimes – one for internal trade and another for external trade – may mean that the external regime is inconsistent with the SPS or TBT Agreement. For instance, if more stringent rules are applied externally than internally, that could well indicate that the external rules are more trade-restrictive than is necessary or that different restrictions are being applied in similar circumstances. See SPS Agreement, Articles 5.5, 5.6 and 6.1; and TBT Agreement, Article 2.2.

86 See WTO Committee on Regional Trade Agreements, *Inventory of Non-Tariff Provisions in Regional Trade Agreements: Background Note by the Secretariat*, WT/REG/W/26 (5 May 1998).

87 Canada has argued that preferential rules of origin cannot be ORCs because they are directed to the internal trade of the RTA and not the external trade (WTO Committee on Regional Trade Agreements, *Note on the Meetings of 6–7 and 10 July 1998*, WT/REG/M/18 (22 July 1998), para. 28). However, preferential rules of origin apply equally to all goods to determine their origin, even though the result will be preferential treatment for goods treated as originating in the RTA.

88 See WTO Committee on Regional Trade Agreements, *Note on the Meetings of 3–5 November 1997*, WT/REG/M/14 (24 November 1997), para. 8.

common external trade regime' or 'a common commercial policy'.[89] To achieve this, the parties must harmonise their respective external trade rules regulating trade with third countries; but to what extent must these restrictions be harmonised?

Discussions among Members have not focused on the meaning of 'substantially the same'. However, in the event of agreement on the meaning of 'substantially all the trade', the criteria adopted might also apply, *mutatis mutandis*, to the term 'substantially the same'. In dispute settlement, in *Turkey–Textiles*, the panel indicated that Article XXIV:8(a)(ii) describes 'a situation where constituent members have "comparable" trade regulations having similar effects with respect to trade with third countries'.[90] The Appellate Body rejected this interpretation,[91] suggesting that the word 'substantially' means 'something closely approximating "sameness" '.[92] Nevertheless, it stated that parties have 'a certain degree of flexibility' to retain individual restrictions on external trade.[93] They are not required to harmonise all external trade restrictions or to adopt an identical external trade regime.[94] Despite these statements by the Appellate Body, certain questions remain as to how to determine whether the parties to any particular customs union apply substantially the same duties and ORCs to other countries. Adopting a case-by-case approach, relevant factors could include: the number of ORCs that are fully or partially harmonised, as compared with the number of un-harmonised ORCs; the degree of partial harmonisation; and the products and value of trade affected by these different restrictions.

In order to harmonise external ORCs upon the formation of a customs union, a party to the union may need to increase a specific duty beyond the bound rate specified in its Schedule of Concessions under Article II of GATT 1994. In that event, Article XXIV:6 requires the party to enter into negotiations with affected Members following the procedure set forth in Article XXVIII of GATT 1994. Essentially, these negotiations are directed towards modification or withdrawal of concessions by affected Members[95] in order to 'maintain a general level of reciprocal and mutually advantageous concessions not less favourable to trade than that provided for in [GATT 1994] prior to such negotiations'.[96] Following the enlargement of the European Communities (EC) from fifteen to twenty-five Member States on 1 May 2004, negotiations of this kind commenced. The EC recently extended the deadline for affected Members to withdraw concessions as a result of the withdrawal of concessions by certain new EC member States in connection with the enlargement.[97]

89 Appellate Body Report, *Turkey–Textiles*, paras. 49 and 50; Panel Report, *Turkey–Textiles*, para. 9.148.
90 Panel Report, *Turkey–Textiles*, para. 9.151. 91 Appellate Body Report, *Turkey–Textiles*, para. 50.
92 *Ibid.* 93 *Ibid.* 94 *Ibid.*, para. 49. 95 GATT 1994, Article XXVIII:1. 96 *Ibid.*, Article XXVIII:2.
97 WTO Council for Trade in Goods, *Communication from the European Communities: Article XXIV:6 Negotiations; Enlargement of the European Union*, G/L/695 (30 September 2004).

D. External restrictions not higher: Article XXIV:5

1. Customs unions: Article XXIV:5(a)

Article XXIV:5(a) of GATT 1994 states that the duties and other regulations of commerce imposed 'at the institution of' a customs union in respect of trade with other WTO Members 'shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union'. This provision therefore requires a comparison of the ORCs imposed before and after the institution of the customs union. Before forming the union, each party applies its own ORCs on trade with other Members. After forming the union, the parties largely replace these individual trade regimes with a common external trade regime. In keeping with the purpose of the PTA exception, the requisite comparison aims to ensure that the new external trade regime of the union does not raise barriers to trade with other Members.

First, the comparison requires an assessment of 'the general incidence of the duties and other regulations of commerce applicable in the constituent territories prior to the formation of' the customs union. The term 'general incidence' suggests a focus on the cumulative or combined effect of all ORCs imposed by the PTA parties rather than the specific effects of any individual ORC or the ORCs imposed by one PTA party. In any case, it would be difficult to compare specific ORCs before and after formation of the customs union because they are likely to be replaced by different ORCs under the new common external trade regime.

Second, the comparison requires an assessment of the 'duties and other regulations of commerce imposed at the institution of' the customs union. This includes all harmonised ORCs, as well as any un-harmonised ORCs that the parties to the union continue to apply on an individual basis. Such ORCs are not to be 'on the whole . . . higher or more restrictive' than before. The words 'on the whole', like the words 'general incidence', demonstrate that the comparison is based on the overall, cumulative impact of the ORCs, not on specific ORCs. As a result, certain specific ORCs imposed by one or more PTA parties may be more burdensome than before, while others may be less burdensome. However, if the ORCs 'as a whole' are more burdensome than before, the customs union cannot benefit from the PTA exception in Article XXIV:5.

The RTA Understanding provides a methodology for determining the cumulative impact of ORCs before and after the formation of the customs union, based on 'an overall assessment of weighted average tariff rates and of customs duties collected'. Paragraph 2 of the RTA Understanding states:

> This assessment shall be based on import statistics for a previous representative period to be supplied by the customs union, on a tariff-line basis and in values and quantities, broken down by WTO country of origin. The Secretariat shall compute the weighted average tariff rates and customs duties collected in accordance with the methodology used in the assessment of tariff offers in the

> Uruguay Round of Multilateral Trade Negotiations. For this purpose, the duties and charges to be taken into consideration shall be the applied rates of duty.

As regards ORCs other than duties and charges, the RTA Understanding is less explicit. Paragraph 2 recognises that for the 'overall assessment' of ORCs 'for which quantification and aggregation are difficult, the examination of individual measures, regulations, products covered and trade flows affected may be required'. This general guidance falls short of a methodology and leaves open precisely how to assess the impact of these ORCs. This process may be difficult because, unlike duties and charges, these restrictions do not take the form of a fixed amount or percentage that is applied to specific products.

2. Free-trade areas: Article XXIV:5(b)

Like Article XXIV:5(a), sub-paragraph 5(b) calls for a comparison between two sets of ORCs: those 'existing' prior to the formation of the FTA, and those 'applicable' at the formation of the FTA. For customs unions, we saw that the comparison under Article XXIV:5(a) is between the 'general incidence' of all ORCs applied before and after the formation of the union. For FTAs, Article XXIV:5(b) calls for a comparison between the ORCs applied after the formation of the FTA and the 'corresponding' ORCs applied before formation. The use of the word 'corresponding' suggests that specific ORCs should be compared as they applied before and after the formation of the FTA.

This view is consistent with the nature of economic integration in FTAs. As with parties to customs unions, FTA parties must eliminate most 'duties and other restrictive regulations of commerce' on substantially all internal trade. However, as stated above, FTA parties have no obligation to adopt common rules for external trade, and parties to an FTA typically continue to impose their own external trade regimes.[98] Therefore, Article XXIV:5(b) prevents an FTA party from using the formation of an FTA as an opportunity to increase the burden of any individual ORC it imposes on external trade. In Article XXIV, such an increase in burden is essentially deemed unnecessary to the formation of an FTA and is inconsistent with the purpose of Article XXIV of minimising the restrictive effects of PTAs on external trade.

Article XXIV:6 envisages increases in specific bound rates upon the formation of a customs union and provides a procedure for negotiating a 'compensatory adjustment' for the affected Member. In contrast, no provision in Article XXIV envisages any increase in specific duties upon the formation of an FTA. This supports the view that a WTO Member may not make any ORC more burdensome upon the formation of an FTA. Nevertheless, other provisions of GATT 1994 or

98 There may be situations where the formation of an FTA does result in modification to the external trade regimes of the parties. For instance, the parties to an FTA may harmonise certain internal restrictions, such as SPS measures, and in consequence modify the corresponding external restrictions.

other covered agreements could conceivably provide a justification for the introduction of new restrictions by FTA parties. For instance, if the parties to an FTA decide to harmonise the SPS/TBT framework within the PTA and, in the process, one or more of the parties introduces new SPS measures or TBTs, the parties could justify the new restrictions under the SPS Agreement or the TBT Agreement, even if these restrictions would normally be regarded as relevant ORCs under Article XXIV:5(b). The introduction on the formation of an FTA of a new ORC that is justified by other WTO provisions should not prevent the FTA concerned from benefiting from the PTA exception under Article XXIV:5 – WTO rules entitle the Member to adopt the ORC whether or not it joins the PTA.

V. The GATS exception for PTAs: Article V[99]

Article V of the GATS is the GATS equivalent of Article XXIV of the GATT. It does not make a distinction between FTAs and CUs, although the PTAs that it contemplates appear closest to GATT FTAs. Its provisions are similar to the GATT's[100] and it also has been the subject of only very limited consideration by WTO dispute settlement bodies.[101]

A. Eliminating restrictions on trade within the PTA

The first substantive requirement for a PTA in the GATS is substantial sectoral coverage and the elimination of substantially all discrimination. Article V:1 of the GATS states:

> This Agreement shall not prevent any of its Members from being a party to or entering into an agreement liberalising trade in services between or among the parties to such an agreement, provided that such an agreement:
>
> (a) has substantial sectoral coverage; and
> (b) provides for the absence or elimination of substantially all discrimination, in the sense of Article XVII, between or among the parties, in the sectors covered under subparagraph (a), through:
> (i) elimination of existing discriminatory measures, and/or

99 See generally, Christopher Findlay, Sherry Stephenson and Francisco J. Prieto, 'Services in Regional Trading Arrangements', in Patrick F.J. Macrory, Arthur E. Appleton and Michael G. Plummer (eds.), *The World Trade Organization: Legal, Economic and Political Analysis* (New York: Springer, 2005), Vol. 1, pp. 293–312.

100 Cf., e.g., GATS, Article V.5; and GATT, Article XXIV.6.

101 It has only been considered in Panel Report, *Canada–Automotive Industry*, paras. 10.265–10.272. In that case the Panel simply found that the measures at issue could not be considered part of NAFTA provisions on liberalisation of trade in services since they were only part of a 'specific exemption'. Further the measure's import duty exemption (i) was accorded to only a small number of US firms on a selective basis; and (ii) excluded other firms in another party to the economic integration agreement (Mexico). The Panel held that this was inconsistent with GATS Article V:1(b).

> (ii) prohibition of new or more discriminatory measures, either at the entry into force of that agreement or on the basis of a reasonable timeframe, except for measures permitted under Articles XI, XII, XIV and XIV*bis*.

Footnote 1 to Article V:1 of the GATS states that the term substantial sector coverage is to be 'understood in terms of number of sectors, volume of trade affected and modes of supply. In order to meet this condition, agreements should not provide for the *a priori* exclusion of any mode of supply'. The 'substantial sectoral coverage' requirement is suggestive of the 'substantially all trade' requirement of Article XXIV of the GATT. Unfortunately, as we saw above, there is no agreement about the meaning of this requirement so we cannot use it to shed light on its context in the GATS.[102]

B. Restrictions on the external trade of the PTA

The second substantive requirement is a prohibition from erecting new trade barriers against those outside the PTA. Article V:4 of the GATS states:

> Any agreement referred to in [Art V.1] shall be designed to facilitate trade between the parties to the agreement and shall not in respect of any Member outside the agreement raise the overall level of barriers to trade in services within the respective sectors or subsectors compared to the level applicable prior to such an agreement.

However, Article V:5 of the GATS makes it clear that compensation must be negotiated where commitments are to be modified:

> If, in the conclusion, enlargement or any significant modification of any agreement under [Art V.1], a Member intends to withdraw or modify a specific commitment inconsistently with the terms and conditions set out in its Schedule, it shall provide at least 90 days advance notice of such modification or withdrawal and the procedure set forth in paragraphs 2, 3 and 4 of Article XXI shall apply.

VI. The likelihood of legal challenge

One might imagine that, given the uncertainties identified above and the enormous number of FTAs concluded or being negotiated, FTAs are at substantial risk of challenge. Certainly FTAs can be challenged, either through the Committee on Regional Trade Agreements (CRTA) or through the dispute settlement mechanism. However, neither mechanism looks likely to begin effectively enforcing the rules.

102 See above section III.

A. Committee on Regional Trade Agreements

WTO Members have a duty to notify the WTO of their decision to enter into FTAs.[103] These notifications are received by the Committee on Regional Trade Agreements (CRTA).[104] The CRTA is required to, among other things:

> (a) carry out the examination of agreements in accordance with the procedures and terms of reference adopted by ... and thereafter present its report to the relevant body for appropriate action;[105]

The CRTA has the power to determine that an FTA is inconsistent with the rules. It may:

> make such reports and recommendations to Members as they may deem appropriate.

However, the CRTA has never made a decision that an FTA was inconsistent with the rules. Indeed, the reports that the CRTA makes on the FTAs it reviews are adopted notwithstanding the often divergent views on their consistency with the rules.[106] The only consensus that has been achieved on an FTA's consistency with the rules was the 1993 customs union between the Czech Republic and the Slovak Republic after the breakup of Czechoslovakia. Given that 211 notifications have been made, the sustained lack of serious enforcement is disturbing.

B. Dispute settlement

While WTO tribunals clearly have the competence to determine claims of the inconsistency of a PTA with the WTO Agreements,[107] a legal challenge is unlikely for a number of reasons. One is that Members may consider that WTO tribunals will

103 GATT, Article XXIV:7(a). The language in this Article suggests that it is a prospective obligation, but for most of its history, notifications to the CRTA have been made after the establishment of the PTA. WTO Members have recently agreed to a new transparency mechanism which provides for early announcement of any RTA and notification to the WTO (much of the mechanism arguably reflects existing obligations): JOB(06)/59/Rev.5.

104 The CRTA was established by a decision of the General Council on 7 February 1996: WTO Doc WT/L/127.

105 WTO Doc WT/L/127.

106 Mitsuo Matsushita, Thomas J. Schoenbaum and Petros C. Mavroidis, *The World Trade Organization: Law, Practice, and Policy*, 2nd edn (Oxford: Oxford University Press, 2006), p. 560.

107 PTA Understanding, Article 12: 'The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding may be invoked with respect to any matters arising from the application of those provisions of Article XXIV relating to customs unions, free-trade areas or interim agreements leading to the formation of a customs union or a free-trade area'. See also Lorand Bartels, 'WTO Dispute Settlement Practice on Article XXIV of the GATT', in Federico Ortino and Ernst-Ulrich Petersmann (eds.), *The WTO Dispute Settlement System 1995–2003* (The Hague: Kluwer Law International, 2004), pp. 263–73, at p. 268.

avoid determining the ambiguities identified above and therefore not wish to engage in the costly process of bringing a dispute. Given:

> the uncertainty surrounding the precise legal frontiers between consistency and inconsistency with the multilateral rules, apart from exceptional cases, it is unlikely that a panel will find itself on firm legal ground to provide a definitive statement on the law itself. [For example, they might state] the burden of proof has not been met, or evidence provided has not been effectively refuted and request additional proof from the complainant.[108]

WTO tribunals are skilled at avoiding answering unnecessary questions and are likely to be able to avoid resolving some key questions where the WTO inconsistency of an FTA was at issue. A stronger reason is that, since all but one WTO Member is party to a FTA, and many FTAs could be WTO-inconsistent, a situation of 'co-operative equilibrium' has developed, where to avoid challenge, Members do not challenge other Members FTAs.[109]

VII. Conclusion

In a global trading system, where PTAs have become a central tool of trade policy, and where they are growing rapidly in number and complexity, the exceptions in Article XXIV:5 of GATT 1994 and Article V of GATS play a crucial role in ensuring coherence between multilateral and regional trade policy. We have noted that these exceptions seeks to ensure that PTAs work to the benefit of the global trading system by promoting a net increase in trade liberalisation. Yet questions remain on almost every issue of importance concerning this exception.[110] Without answers to these questions, the value of Article XXIV and Article V in shaping regional trade policy is diminished. Moreover, the risk that PTAs work to undermine trade liberalisation at the multilateral level increases. This chapter has explored some of the questions surrounding Article XXIV and Article V, evaluating possible options, always keeping in mind the underlying purpose of the PTA exception. We have examined the views expressed by Members, panels, and the Appellate Body, as well as the text of WTO agreements. We have also drawn on the way PTAs work in practice. The conclusion must be that Article XXIV and Article V are mired in doubt. Until the WTO makes further progress in this area, the WTO-consistency of most PTAs will be uncertain and Members will have difficulty determining the best way of structuring PTAs in a WTO-consistent fashion.

108 Matsushita *et al.*, above n. 106, at p. 585. 109 *Ibid.*, at p. 587.

110 For example, does the exception extend to GATT-inconsistencies arising from the elimination of internal trade restrictions only if these inconsistencies were necessary to the formation of the RTA? Does it justify a departure from the obligation under the Agreement on Safeguards to impose safeguards on all imports of the relevant product from all sources? How should 'substantially all the trade' between the RTA parties be measured in assessing whether internal trade restrictions have been sufficiently reduced? Do the parties to a customs union have to harmonise not only border measures but also marketplace measures applied to goods of other Members?

6

PTAs and public international law

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I. Introduction

From the first report of the Appellate Body of the World Trade Organisation (WTO) in 1996[1] to Joost Pauwelyn's seminal work in 2003,[2] commentators and practitioners alike have been grappling with the thorny relationship between the WTO and public international law.[3] More recently, problems in interpreting and applying WTO provisions in the light of customary international law and non-WTO treaties[4] have come to reflect a concern regarding 'fragmentation' of international law more generally.[5] One reason for this potential fragmentation lies in the disparate dispute settlement mechanisms under various international legal systems,[6] including preferential trade agreements (PTAs).[7]

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1 Appellate Body Report, *US–Gasoline*, p. 17: 'the *General Agreement* is not to be read in clinical isolation from public international law'.

2 Joost Pauwelyn, *Conflict of Norms in Public International Law: How WTO Law Relates to Other Rules of International Law* (Cambridge: Cambridge University Press, 2003).

3 See also, e.g., Lorand Bartels, 'Applicable Law in WTO Dispute Settlement Proceedings' (2001) 35(3) *Journal of World Trade* 499–519; Michael Lennard, 'Navigating by the Stars: Interpreting the WTO Agreements' (2002) 5(1) *Journal of International Economic Law* 17–89; Gabrielle Marceau, 'WTO Dispute Settlement and Human Rights' (2002) 13(4) *European Journal of International Law* 753–814; Joel P. Trachtman, 'The Jurisdiction of the World Trade Organization' (2004) 98 *American Society of International Law Proceedings* 139–42; and Joel P. Trachtman, 'Jurisdiction in WTO Dispute Settlement', in Rufus Yerxa and Bruce Wilson (eds.), *Key Issues in WTO Dispute Settlement: The First Ten Years* (Cambridge: Cambridge University Press, 2005), pp. 132–43.

4 See, e.g., Appellate Body Report, *EC–Tariff Preferences*, para. 163; and Appellate Body Report, *EC–Sugar Subsidies*, paras. 310 and 312.

5 See, e.g., International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, Report of the Study Group (finalised by Martti Koskenniemi), UN Doc. A/CN.4/L.682 (4 April 2006); and Campbell McLachlan, 'The Principle of Systemic Integration and Article 31(3)(c) of the Vienna Convention' (2005) 54 *International & Comparative Law Quarterly* 279–320.

6 See, e.g., Joost Pauwelyn, 'Adding Sweeteners to Softwood Lumber: The WTO–NAFTA 'Spaghetti Bowl' is Cooking' (2006) 9(1) *Journal of International Economic Law* 197–206; and Yuval Shany, *The Competing Jurisdictions of International Courts and Tribunals* (Oxford: Oxford University Press, 2003).

7 We use the term 'preferential trade agreements' to refer to bilateral and regional agreements between States or customs territories that focus at least in part on liberalising trade between the parties, as distinct from

As negotiations in the Doha Round sputter,[8] and PTAs proliferate,[9] the relationship between PTAs and other institutions and aspects of public international law becomes all the more crucial. States evaluating the benefits of PTAs must be fully aware of the broader international context into which they are born and the implications of international law as each PTA develops. Moreover, existing PTA members may seek additional certainty about their PTA rights and obligations and the likely outcome in the event of a dispute relating to other areas of international law. More broadly, an investigation into the relationship between public international law and PTAs provides an additional case study of the perceived problem of fragmentation of international law.

In this chapter, we focus on two primary sources of public international law, namely treaties and customary international law. We also take into account two other sources of public international law, namely general principles of law and judicial decisions and leading commentary. All four sources are included in Article 38(1) of the Statute of the International Court of Justice (ICJ Statute), which is often recognised as providing an informal list of the sources of international law.[10]

Below, we examine three significant areas in which public international law interacts with PTAs: first, how various forms of public international law affect the interpretation of PTA provisions; second, the related issue of how PTAs contribute to customary international law and the extent to which customary international law applies to PTAs; and, finally, how to resolve conflicts between PTAs and other treaties. This final section examines both substantive conflicts and problems arising from overlapping jurisdictions of PTA tribunals and other international tribunals. This survey illustrates the complex web of links between PTAs and public international law and the readiness of PTA tribunals, particularly under the North American Free Trade Agreement[11] (NAFTA), to draw on other sources of international law in interpreting PTA provisions and otherwise determining PTA disputes. At the same time, no clear answers emerge about

the multilateral system established under the WTO. 'PTAs' therefore include free-trade areas and customs unions within the meaning of Article XXIV of GATT 1994.

8 See Minutes of the General Council meeting held on 27–28 July 2006, WT/GC/M/103, paras. 1–53; and WTO, 'Talks Suspended. 'Today there are only losers'', *News Item*, 24 July 2006.

9 See, e.g., Report by the Consultative Board to the Director-General, 'The Future of the WTO: Addressing Institutional Challenges in the New Millennium', Geneva, 2004, para. 76; and World Bank, *Global Economic Prospects 2005: Trade, Regionalism, and Development* (Washington, DC: World Bank, 2005), at pp. 28–30.

10 See, e.g., Martti Koskenniemi, 'Introduction', in Martti Koskenniemi (ed.), *Sources of International Law* (Aldershot: Ashgate, 2000), p. xi; Gerald G. Fitzmaurice, 'Some Problems Regarding the Formal Sources of International Law' (1958) *Symbolae Verzijl* 153–76, at 173; and Robert Y. Jennings, 'What is International Law and How Do We Tell It When We See It?' (1981) 37 *Schweitzerisches Jahrbuch für Internationales Recht* 59–88, at 61.

11 (1993) 32 ILM 289 and (1993) 32 ILM 605.

how best to deal with the likelihood of ever increasing conflicts between PTAs and other treaties.

II. Interpreting PTA provisions

In exploring how public international law influences the interpretation of PTA provisions, we first consider the role of the Vienna Convention on the Law of Treaties[12] (Vienna Convention), before moving on to the relevance of WTO law.

A. Impact of the Vienna Convention on the Law of Treaties

The Vienna Convention applies to 'treaties between States',[13] where a 'treaty' is defined as 'an international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation'.[14] This would naturally include PTAs between any of the 108 parties of the Vienna Convention,[15] unless they were concluded before that convention's entry into force in 1980.[16]

At least some parts of the Vienna Convention are widely accepted as codifying customary international law or having attained the status of customary international law.[17] Articles 31 and 32 on the interpretation of treaties, in particular, are frequently regarded as declaring or reflecting customary international law.[18] This means that the rules of interpretation in these provisions apply to all PTAs between States, whether or not those States are party to the Vienna Convention. This conclusion is fairly uncontroversial, just as few would argue that the WTO agreements should be interpreted other than by reference to Articles 31 and 32 of the Vienna Convention.[19]

In any case, although a PTA could conceivably dictate alternative rules for interpretation, the more common scenario would be that the PTA explicitly or

12 Done at Vienna 23 May 1969, in force 27 January 1980, 1155 UNTS 331; (1969) 8 ILM 679, UKTS (1980) 58.

13 Vienna Convention, Article 1. Accordingly, the Vienna Convention does not apply to treaties between States and international organisations or between international organisations: Ian Sinclair, *The Vienna Convention on the Law of Treaties*, 2nd edn (Manchester: Manchester University Press, 1984), at pp. 6–7. The Vienna Convention is adapted to international organisations by the Vienna Convention on the Law of Treaties Between States and International Organisations or Between International Organisations, opened for signature 21 March 1986, not yet in force, (1986) 25 ILM 543.

14 Vienna Convention, Article 2(1)(a).

15 UN, *Multilateral Treaties Deposited with the Secretary-General*, ST/LEG/SER/E/–, available at http://untreaty.un.org.

16 Vienna Convention, Article 4.

17 We discuss customary international law further below in section III.

18 See, e.g., *Case Concerning the Territorial Dispute (Libyan Arab Jamahiriya* v. *Chad) (Merits)* [1994] ICJ Rep. 6, pp. 21–2; Sinclair, above n. 13, at p. 19 (regarding Vienna Convention, Articles 30–3); Pauwelyn, above n. 2, at p. 245. See also *Gabckovo-Nagymaros Project (Hungary* v. *Slovakia) (Merits)* (*Gabckovo-Nagymaros Project*) [1997] ICJ Rep. 7 at p. 38 (regarding Vienna Convention, Articles 60–2).

19 See, e.g., Appellate Body Report, *US–Gasoline*, pp. 16–17; and DSU, Article 3.2.

implicitly confirms that the Vienna Convention rules apply. For example, Article 21.9(2) of the Australia–United States Free Trade Agreement (AUSFTA) provides:

> The panel shall consider this Agreement in accordance with applicable rules of interpretation under international law as reflected in Articles 31 and 32 of the *Vienna Convention on the Law of Treaties* (1969).[20]

Similarly, Article 102(2) of NAFTA provides that '[t]he Parties shall interpret and apply the provisions of this Agreement in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law', which are read to include Articles 31 and 32 of the Vienna Convention.[21]

Articles 31 and 32 of the Vienna Convention themselves provide an example of public international law (in this case, interpretative rules amounting to customary international law) influencing PTAs. Thus, the primary customary international law rule for interpreting treaties also applies to PTAs: 'A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose'.[22]

In turn, various forms of public international law may affect the meaning of various terms in Articles 31 and 32 and how they should be applied. For example, Article 31(3) of the Vienna Convention states that, in interpreting a treaty:

> There shall be taken into account, together with the context:
>
> (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
> (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
> (c) any relevant rules of international law applicable in the relations between the parties.

The words 'subsequent practice' have taken on a specific meaning in public international law,[23] and a correct interpretation in accordance with Article 31(3) should have regard to that meaning.

More importantly, Article 31(3)(c) of the Vienna Convention provides a concrete basis for examining non-interpretative rules of public international law in interpreting PTA provisions. In particular, other treaties to which the PTA members are party should be considered. For example, the NAFTA Arbitral Tribunal in *SD Myers* v. *Government of Canada* examined the Canada–USA Transboundary

20 See also NAFTA, Article 102(2).

21 See, e.g., NAFTA Ch 20 Panel Report, *Tariffs Applied by Canada to Certain U.S.-Origin Agricultural Products*, CDA-95-2008-01 (2 December 1996), paras. 118–19; and NAFTA Ch 11 Arbitral Tribunal, *SD Myers Inc* v. *Government of Canada* ('*Myers v. Canada*') (Partial Award of 13 November 2000), para. 200.

22 Vienna Convention, Article 31(1).

23 See, e.g., Arnold D. McNair, *The Law of Treaties* (Oxford: Clarendon Press, 1961), Chapter XXIV; Sinclair, above n. 13, at pp. 135–8; and Appellate Body Report, *Japan–Alcoholic Beverages*, paras. 12–13.

Agreement on Hazardous Waste in interpreting NAFTA provisions in an arbitration between the Government of Canada and a United States (US) investor.[24] Most commentators would agree that the WTO agreements contain references to non-WTO 'rules of international law'.[25] Pursuant to Article 31(3)(c), these rules must therefore be taken into account, where relevant, in interpreting a PTA between any of the WTO's 150 Members.

B. Relevance of WTO law

This leads to the question of the significance of WTO 'jurisprudence' in clarifying the WTO rules and, in turn, in interpreting PTA provisions. WTO case law itself, in the form of Panel or Appellate Body Reports adopted by the Dispute Settlement Body (DSB),[26] does not necessarily amount to or create rules of international law within the meaning of Article 31(3)(c), given that Panels, the Appellate Body and the DSB must not 'add to or diminish the rights and obligations provided in the covered agreements'.[27] It may nevertheless comprise 'judicial decisions' providing a 'subsidiary means for the determination of rules of law'.[28] Locknie Hsu even suggests that WTO provisions and cases may 'evolve into customary international law'[29] and on that basis be relevant sources of international law in interpreting PTAs. At the least, even though the WTO's Ministerial Conference and General Council 'have the exclusive authority to adopt interpretations' of the WTO agreements,[30] the reasoning and conclusions in adopted Panel and Appellate Body Reports may shed light on the correct interpretation of particular WTO provisions, which may be relevant in interpreting related PTA provisions.

24 *Myers* v. *Canada*, paras. 205–8.

25 See, e.g., Joost Pauwelyn, 'The Jurisdiction of the World Trade Organization' (2004) 98 *American Society of International Law Proceedings* 135–8, at 136; Gabrielle Marceau, 'Conflicts of Norms and Conflicts of Jurisdictions: The Relationship between the WTO Agreement and MEAs and Other Treaties' (2001) 35(6) *Journal of World Trade* 1081–131, at 1081; and Trachtman, 'The Jurisdiction of the World Trade Organization', above n. 3, at 139 (referring to 'a separation between WTO law and *other* international law' (emphasis added)).

26 For general information about the WTO dispute settlement system, see WTO, *A Handbook on the WTO Dispute Settlement System* (Cambridge: Cambridge University Press, 2004); David Palmeter and Petros C. Mavroidis, *Dispute Settlement in the World Trade Organization: Practice and Procedure*, 2nd edn (The Hague: Kluwer Law International, 2004); Bryan Mercurio, Yang Guohua and Li Yongjie, *WTO Dispute Settlement Understanding: A Detailed Interpretation* (The Hague: Kluwer Law International, 2005); and Giorgio Sacerdoti, Alan Yanovich and Jan Bohanes (eds.), *The WTO at Ten: The Contribution of the Dispute Settlement System* (Cambridge: Cambridge University Press, 2006).

27 DSU, Articles 3.2 and 19.2.

28 ICJ Statute, Article 38(1)(d). As Brownlie notes, 'the practical significance of the label ''subsidiary means'' in Article 38(1)(d) is not to be exaggerated': Ian Brownlie, *Principles of Public International Law*, 6th edn (Oxford: Oxford University Press, 2003). See below n. 98 and corresponding text.

29 Locknie Hsu, 'Applicability of WTO Law in Regional Trade Agreements: Identifying the Links', in Lorand Bartels and Federico Ortino (eds.), *Regional Trade Agreements and the WTO Legal System* (Oxford: Oxford University Press, 2006), pp. 525–52, at p. 532.

30 WTO Agreement, Article IX:2.

This conclusion is particularly apt where the PTA provision in question incorporates a WTO provision by reference or replicates the wording of the WTO provision, both of which are common techniques.[31] An example of a PTA incorporating a WTO provision by reference appears in Article 301(1) of NAFTA:

> Each Party shall accord national treatment to the goods of another Party in accordance with Article III of the *General Agreement on Tariffs and Trade* (GATT), including its interpretative notes, and to this end Article III of the GATT and its interpretative notes, or any equivalent provision of a successor agreement to which all Parties are party, are incorporated into and made part of this Agreement.

An example of a PTA replicating the wording of a WTO provision[32] appears in Article 809 of the Thailand–Australia Free Trade Agreement, which is very similar to Article XVI of the WTO's General Agreement on Trade in Services (GATS).

The relevance of WTO law in interpreting these and other PTA provisions[33] is evidenced by a number of decisions by PTA tribunals. For instance, examining a NAFTA exception provision that 'closely track[ed] the GATT Article XX language', an Arbitral Panel established under NAFTA Chapter 20 found that 'the GATT/WTO jurisprudence proves helpful in determining what ''necessary'' means'.[34] The NAFTA *Myers* Arbitral Tribunal referred to WTO case law on 'like products' in interpreting the words 'like circumstances' in Article 1102 of NAFTA[35] (although a subsequent tribunal criticised this approach given the different language used in the two treaties).[36]

Incidentally, citation by WTO Panels or the Appellate Body of PTA tribunal decisions as legal authority in interpreting WTO law is much rarer,[37] although Todd Weiler has argued that:

> should NAFTA tribunal jurisprudence in the fields of services and investment regulation continue to outstrip that of WTO panels, it would not seem too

31 On the different ways in which PTA provisions may invoke WTO law, see Hsu, above n. 29, at p. 542.

32 See also AUSFTA, Article 17.9(3), duplicating TRIPS Agreement, Article 30.

33 Conversely, incorporation of WTO provisions in PTAs may have implications for the compulsory nature of the WTO dispute settlement system, given that the same issue may be litigated under a PTA instead of the WTO. This relates to the problem of overlapping WTO/PTA jurisdiction, as discussed further below, section IVB.

34 NAFTA Ch 20 Panel Report, *In the Matter of Cross-Border Trucking Services*, USA-MEX-98-2008-01 (6 February 2001), paras. 260 and 262.

35 *Myers* v. *Canada*, paras. 243–6. For further discussion of the use of WTO law by NAFTA panels and tribunals, see Hsu, above n. 29, at pp. 543–9.

36 NAFTA Ch 11 Arbitral Tribunal, *Methanex Corporation* v. *United States of America* (Award of 9 August 2005), Part IV, Chapter B, paras. 29–37.

37 Cf., e.g., Appellate Body Report, *EC–Chicken Classification*, paras. 310–45. See also Isabelle Van Damme, 'What Role is there for Regional International Law in the Interpretation of the WTO Agreements?', in Bartels and Ortino, above n. 29, pp. 553–75, at pp. 569–71, on the use by WTO Panels and the Appellate Body of PTAs (as opposed to PTA jurisprudence) in interpreting WTO law.

> much to ask that NAFTA awards be considered by WTO panels in the adoption of an inductive approach to as-of-yet 'untested' GATS obligations.[38]

Weiler made this statement in 2003, before the release of several significant WTO cases on services (not that these embraced PTA tribunal jurisprudence either).[39]

III. FTAs and customary international law

As already mentioned,[40] Articles 31 and 32 of the Vienna Convention reflect customary international law on treaty interpretation and therefore represent one way in which customary international law affects PTAs. Moreover, Article 31(3)(c) provides an avenue for various aspects of public international law (including customary international law) to influence the interpretation of PTAs. In this section, we explore two additional issues regarding the relationship between PTAs and customary international law. To begin with, how might PTAs contribute to or influence customary international law? Conversely, how might customary international law affect the operation of PTAs other than in an interpretative sense? We address these intersecting questions in turn.

A. Contribution of PTAs to customary international law

Customary international law is an independent source of international law, as reflected in Article 38(1)(b) of the ICJ Statute, which refers to 'international custom, as evidence of a general practice accepted as law'.[41] In accordance with this description, customary international law is essentially created through the two elements of 'State practice' and '*opinio juris*'[42] (i.e., belief among the relevant States that this practice accords with a binding norm). More particularly:

> Not only must the acts concerned amount to a settled practice, but they must also be such, or be carried out in such a way, as to be evidence of a belief that this practice is rendered obligatory by the existence of a rule of law requiring it. . . . The States concerned must therefore feel that they are conforming to what amounts to a legal obligation.[43]

38 Todd Weiler, 'NAFTA Article 1105 and the Principles of International Economic Law' (2003) 42 (1) *Columbia Journal of Transnational Law* 35–85, at 73.

39 See, in particular, Appellate Body Report, *US–Gambling*; and Panel Report, *Mexico –Telecoms.*

40 See above section IIA.

41 For further discussion of customary international law, see Michael Byers, *Custom, Power and the Power of Rules* (Cambridge: Cambridge University Press, 1999); and Kristen Walker and Andrew D. Mitchell, 'A Stronger Role for Customary International Law in Domestic Law?', in Hilary Charlesworth, Madelaine Chiam, Devika Hovell and George Williams (eds.), *The Fluid State* (Sydney: Federation Press, 2005), pp. 110–35, at pp. 112–25.

42 See, e.g., *North Sea Continental Shelf (Federal Republic of Germany* v. *Denmark; Federal Republic of Germany* v. *Netherlands) (Merits)* ('*North Sea Continental Shelf*') [1969] ICJ Rep. 3, at p. 41.

43 *North Sea Continental Shelf*, p. 44.

In 1990, before the creation of the WTO, Stephen Zamora canvassed the possibility of 'customary international economic law', suggesting that international economic law (including in the form of multilateral and bilateral treaties) could contribute to, or provide, evidence of both State practice and *opinio juris*.[44]

Let us consider an example of how this might occur. Under customary international law, a State is responsible for a 'denial of justice' where its courts or tribunals fail to accord a minimum standard of procedural or (more rarely) substantive fairness to aliens in the administration of justice.[45] (Importantly, this 'minimum standard' may relate to the way the State treats its own nationals, but it operates independently of and supplements the 'national treatment' rule common in WTO agreements and PTAs.)[46] This customary rule could be relevant in interpreting PTA provisions,[47] or it could apply independently to the conduct of PTA parties just as other customary rules may do, as discussed below. At the same time, the development of the rule in PTAs and PTA jurisprudence could affect the content or status of the customary rule. This is particularly likely given that PTAs frequently incorporate some form of the doctrine of denial of justice in their provisions, and that disputes concerning the treatment of aliens, including in the courts, often arise in the context of PTAs.

For instance, Article 1105(1) of NAFTA provides:

> Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.

The reference to international law in this provision highlights the dynamic relationship between NAFTA and other aspects of public international law. The mere inclusion of Article 1105(1) in NAFTA could provide some evidence of state practice and *opinio juris* in connection with the doctrine of denial of justice in customary international law. The NAFTA Free Trade Commission's interpretation of Article 1105(1) supports this suggestion, stating that '[t]he concepts of ''fair and equitable treatment'' and ''full protection and security'' do not require treatment in addition to or beyond that which is required by the customary international law

44 Stephen Zamora, 'Is There Customary International Economic Law?' (1990) 32 *German Yearbook of International Law* 9–42, at 18–23.

45 See, e.g., *Case Concerning Elettronica Sicula SpA (ELSI) (United States of America* v. *Italy) (Merits)* ('*Elettronica Sicula*') [1989] ICJ Rep. 15, pp. 66–7; Louis B. Sohn and Richard R. Baxter, 'Responsibility of States for Injuries to the Economic Interests of Aliens' (1961) 55 *American Journal of International Law* 545–84; Robert Y. Jennings and Arthur Watts (eds.), *Oppenheim's International Law*, 9th edn (London: Longman, 1992), Vol. I, at pp. 543–4; Jan Paulsson, *Denial of Justice in International Law* (Cambridge: Cambridge University Press, 2005); and Andrew D. Mitchell, 'Due Process in WTO Disputes', in Yerxa and Wilson, above n. 3, pp. 144–60, at pp. 148–9.

46 Giorgio Sacerdoti, 'Bilateral Treaties and Multilateral Instruments on Investment Protection' (1997) 269 *Hague Academy, Recueil des Cours* 251–460, at 342.

47 In relation to the doctrine of denial of justice in interpreting investment treaty provisions, see Weiler, above n. 38, at 77 and 79–81.

minimum standard of treatment of aliens'.[48] Furthermore, NAFTA jurisprudence on Article 1105(1) could influence the meaning of denial of justice beyond the scope of NAFTA.

In *Loewen Group Inc and Raymond L Loewen* v. *United States of America*, Canadian investors challenged, *inter alia*, a Mississippi State Court decision in a commercial dispute with local business, on grounds including that:

> the trial court, by the way in which it conducted the trial, in particular by its conduct of the *voir dire* and its irregular reformation of the initial jury verdict for $260,000,000, [and] by permitting extensive nationality-based, racial and class-based testimony and counsel comments, violated Article 1105 of NAFTA . . . [49]

The Arbitral Tribunal determined that the conduct of the trial amounted to a 'miscarriage of justice amounting to a manifest injustice as that expression is understood in international law'.[50] However, due to the failure to appeal the State Court decision (as discussed further below) and subsequent developments affecting its jurisdiction, the Arbitral Tribunal ultimately dismissed Loewen's claims.[51] Its discussion of denial of justice could nevertheless clarify the meaning of this doctrine under international law, not as a binding direction (particularly given the outcome of the case) but as a reflection of the understanding of the NAFTA parties regarding the content of customary international law (potentially as evidence of *opinio juris*)[52] and perhaps as a guide to the development of that law. The following statements could play this kind of role:

> [W]e take it to be the responsibility of the State under international law and, consequently, of the courts of a State, to provide a fair trial of a case to which a foreign investor is a party. It is the responsibility of the courts of a State to ensure that litigation is free from discrimination against a foreign litigant and that the foreign litigant should not become the victim of sectional or local prejudice.[53] . . .

48 As cited in and endorsed by *The Loewen Group, Inc. and Raymond L. Loewen* v. *United States of America* ('*Loewen* v. *US*'), ICSID Case No. ARB(AF)/98/3, (Award of 26 June 2003), paras. 125–6 and 128. The Free Trade Commission's interpretation contrasts with the earlier decision in NAFTA Ch 11 Arbitral Tribunal, *Pope & Talbot Inc* v. *Government of Canada* (Award of 10 April 2001), paras. 111–18, which held that the 'fair and equitable treatment' standard was separate from and supplementary to the customary international law standard.

49 *Loewen* v. *US*, para. 39. 50 *Ibid*., para. 54. 51 *Ibid*., para. 240.

52 Here we emphasise that these decisions could provide *evidence* of States' beliefs and intentions to establish the existence or content of customary international law. We do not mean that the decisions would themselves constitute *opinio juris* or customary international law. As noted elsewhere in this chapter, judicial decisions may constitute a 'subsidiary means' for determining rules of international law: see above n. 28 and below n. 98 and corresponding text.

53 *Loewen* v. *US*, para. 123.

> A decision which is in breach of municipal law and is discriminatory against the foreign litigant amounts to manifest injustice according to international law.[54]

Other international tribunals have indeed referred to NAFTA rules and jurisprudence in interpreting other international treaties and determining the content of international law rules such as the minimum standard of treatment of aliens. For example, in *Tecnicas Medioambientales Tecmed SA* v. *United Mexican States*, an Arbitral Tribunal was established within the framework of the International Centre for Settlement of Investment Disputes (ICSID) to hear a dispute concerning a bilateral investment treaty between Spain and Mexico.[55] The tribunal cited as authority the NAFTA decisions in *Myers* and *Mondev International Ltd* v. *United States of America* in determining that 'the commitment of fair and equitable treatment' under the investment treaty was 'an expression and part of the *bona fide* principle recognized in international law, although bad faith from the State is not required for its violation'.[56]

More recently, in *CMS Gas Transmission Company* v. *Argentine Republic*,[57] another ICSID Arbitral Tribunal considered a dispute arising under a bilateral investment treaty between the US and Argentina.[58] Article II(2)(a) of the treaty provided that '[i]nvestment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that required by international law'.[59] Referring to the NAFTA Free Trade Commission's interpretation of Article 1105(1) of the NAFTA,[60] the Arbitral Tribunal in *CMS Gas* concluded that the 'standard of fair and equitable treatment' under the investment treaty was 'not different from the international law minimum standard and its evolution under customary law'.[61]

The *CMS Gas* case also demonstrates how PTA tribunal decisions may affect state practice. The Arbitral Tribunal noted that the NAFTA ruling in *Pope & Talbot Inc* v. *Government of Canada*[62] that 'the standard of fair and equitable treatment is separate and more expansive than that of customary international law'[63] prompted the Free Trade Commission's contrary interpretation[64] as well as clarifications in other treaties,[65] such as the United States–Chile Free Trade Agreement. Article 10.4.2 of that PTA provides additional guidelines regarding the obligations

54 *Ibid*., para. 135. 55 See the Spain–Mexico BIT.

56 *Tecnicas Medioambientales Tecmed SA* v. *United Mexican States*, ICSID Case No. ARB(AF)/00/2 (Award of 29 May 2003), para. 153 (footnote omitted), (citing *Myers* v. *Canada*, para. 134 and NAFTA Ch 11 Arbitral Tribunal, *Mondev International Ltd* v. *United States of America* ('*Mondev International v. US*'), ICSID Case No. ARB(AF)/99/2 (Award of 11 October 2002), para. 116).

57 *CMS Gas Transmission Company* v. *Argentine Republic* ('*CMS Gas v. Argentina*'), ICSID Case No. ARB/01/8 (Award of 12 May 2005).

58 See the United States–Argentina BIT. 59 As cited in *CMS Gas* v. *Argentina*, para. 266.

60 *CMS Gas* v. *Argentina*, para. 283. See above n. 48 and corresponding text.

61 *CMS Gas* v. *Argentina*, para. 284. 62 See above n. 48 and corresponding text.

63 *CMS Gas* v. *Argentina*, para. 282. 64 See above n. 48 and corresponding text.

65 *CMS Gas* v. *Argentina*, para. 282.

in Article 10.4.1, stating, '[f]or greater certainty', that '[t]he concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by' the standard applicable under customary international law. A similar qualification appears in the AUSFTA, which requires treatment of covered investments 'in accordance with the customary international law minimum standard of treatment of aliens, including fair and equitable treatment and full protection and security'.[66]

The increasingly important role of NAFTA and other PTA tribunals in public international law may concern some commentators, who argue that they are not 'equipped to hear questions of international law that are normally submitted to the' International Court of Justice (ICJ).[67] On the other hand, the process of 'dialectic review' pursuant to NAFTA Chapter 11 may be especially valuable in the 'development of international norms of due process' and the 'refinement of existing norms'.[68] Interestingly, the Arbitral Tribunal in *Loewen* pointed out that Chapter 11 itself 'represents a progressive development in international law whereby the individual investor may make a claim on its own behalf and submit the claim to international arbitration'.[69]

B. Non-interpretative impact of customary international law on PTAs

We turn now to the related question of how customary international law constrains or otherwise affects the operation of PTAs, in addition to its common influence in dictating rules of interpretation. Specifically, we consider the extent to which customary international law may impact on PTAs in the absence of a PTA provision that expressly incorporates or refers to a specific rule or principle of international law (such as the minimum standard of treatment of aliens).

Some PTA provisions may suggest that all aspects of customary international law (as well as other aspects of international law, such as treaties, as discussed further below) apply not merely in interpreting PTA provisions but more broadly in resolving PTA disputes. For instance, Article 1131 of NAFTA, the corollary of Article 102(2) mentioned above,[70] provides in relation to state-investor disputes under Chapter 11:

> Governing law
>
> 1. A Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law.

66 AUSFTA, Article 11.5(1) (see also Article 11.5(2)).

67 Ari Afilalo, 'Towards a Common Law of International Investment: How NAFTA Chapter 11 Panels Should Solve Their Legitimacy Crisis' (2004) 17 *Georgetown International Environmental Law Review* 51–96, at 84.

68 Robert B. Ahdieh, 'Between Dialogue and Decree: International Review of National Courts' (2004) 79(6) *New York University Law Review* 2029–163, at 2124–5.

69 *Loewen* v. *US*, para. 223. 70 See above section IIA.

The reference to 'applicable rules of international law' arguably encompasses all procedural or substantive rules of international law, as opposed to purely interpretative rules such as those found in Articles 31 and 32 of the Vienna Convention. Conversely, one might contend that Article 1131 has no impact on the Tribunal's applicable law; it simply confirms or restates out of an abundance of caution what would be the case anyway. In other words, Article 1131 acknowledges that, pursuant to international law, certain rules not spelled out in NAFTA will apply to Chapter 11 disputes. Assuming that this interpretation is correct, or that we are discussing a PTA that contains no equivalent to Article 1131, we are faced with the question of whether or which customary international law rules would apply.

In the WTO context, few would dispute that Panels and the Appellate Body have jurisdiction to hear only claims under WTO law, as opposed to claims under any other body of domestic or international law.[71] Similarly, most PTAs that include dispute settlement provisions make clear the types of claims that the relevant tribunals may hear: typically those concerning the interpretation or application of the PTA in question.[72] A separate, more controversial question[73] in the context of both the WTO and PTAs is the extent to which customary international law forms part of the applicable or governing law in resolving disputes.

On one view, put simply, each PTA is 'born into' public international law and therefore customary international law applies to it and the resolution of disputes under it to the extent that the PTA does not otherwise provide. This is the view espoused by Pauwelyn in relation to the WTO.[74] Joel Trachtman forcefully expresses the opposing position:

> It is important . . . to recognize the distinction between the law that applies to the conduct of states and the law that is applicable within WTO dispute settlement. [Pauwelyn] argues that because states are subject to the full range of their conventional and customary international legal obligations unless they contract out of them, WTO dispute settlement must apply all international legal obligations unless they are specifically precluded from application . . . This logic is fundamentally incorrect: it is a non sequitur. The opposite is true. International legal tribunals are authorized only to (1) hear cases and (2) apply law pursuant to their specific, positive mandates. They are not implicitly

71 See, e.g., Pauwelyn, above n. 25, at 135; Trachtman, 'The Jurisdiction of the World Trade Organization', above n. 3, at 139; and Debra P. Steger, 'The Jurisdiction of the World Trade Organization' (2004) 98 *American Society of International Law Proceedings* 142–6, at 143.

72 See, e.g., Thailand–Australia PTA, Article 21.2. On 'non-violation' claims, as allowed under this provision and certain other PTAs as well as Article XXIII:1(b) of GATT 1994 and Article XXIII:3 of GATS, see Locknie Hsu, 'Non-violation Complaints – World Trade Organization Issues and Recent Free Trade Agreements' (2005) 39(2) *Journal of World Trade* 205–37.

73 International Law Commission, above n. 5, para. 45. 74 Pauwelyn, above n. 2, at pp. 460–1 and 466–7.

> courts of general jurisdiction, either as to the cases they can hear *or* as to the law they can apply.[75]

Although this debate has so far taken place largely in the context of the WTO, the same issues arise in relation to PTAs and are equally difficult to resolve. Nevertheless, PTA provisions and case law provide some indication of how PTAs in practice deal with their relationship with customary international law. In addition, at the outset, it is important to recognise that PTAs can neither 'contract out of' nor avoid by omission certain rules of international law, namely *jus cogens* norms.

Article 53 of the Vienna Convention defines a *jus cogens* norm or 'a peremptory norm of general international law' as 'a norm accepted and recognized by the international community of States as a whole as a norm from which no derogation is permitted and which can be modified only by a subsequent norm of general international law having the same character'.[76] Under the same provision, '[a] treaty is void if, at the time of its conclusion, it conflicts with a peremptory norm of general international law'. Similarly, Article 64 of the Vienna Convention provides that '[i]f a new peremptory norm of general international law emerges, any existing treaty which is in conflict with that norm becomes void and terminates'. These pronouncements as to *jus cogens* norms being above all others in the hierarchy of public international law apply not merely to States parties to the Vienna Convention, as '[t]he concept of *jus cogens* operates as a concept superior to both customary international law and treaty'.[77] Arguably, the implications for a treaty that conflicts with a *jus cogens* norm as set out in the Vienna Convention represent customary international law and are therefore also binding on all States.[78]

Norms generally recognised as having the character of *jus cogens* include, for instance, genocide,[79] crimes against humanity, war crimes,[80] and 'the prohibition of the use of force expressed in Article 2, paragraph 4, of the Charter of the United Nations'.[81]

75 Joel Trachtman, 'Book Review. Conflict of Norms in Public International Law: How WTO Law Relates to Other Rules of International Law by Joost Pauwelyn' (2004) 98 *American Journal of International Law* 855–60, at 857–8 (emphasis in original).

76 See *Legality of the Threat or Use of Nuclear Weapons (Advisory Opinion)* [1996] ICJ Rep. 226, p. 258, referring to Vienna Convention, Article 53, as defining *jus cogens*.

77 *Application of the Convention on the Prevention and Punishment of the Crime of Genocide (Bosnia and Herzegovina* v. *Serbia and Montenegro) (Order on Provisional Measures)* [1993] ICJ Rep. 325, p. 440 (Separate Opinion of Judge Lauterpacht).

78 See Sinclair, above n. 13, pp. 17–18.

79 *Reservations to the Convention on the Prevention and Punishment of Genocide (Advisory Opinion)* [1951] ICJ Rep. 15, p. 23.

80 *Application of the Convention on the Prevention and Punishment of the Crime of Genocide (Bosnia and Herzegovina* v. *Serbia and Montenegro)*, p. 440 (Separate Opinion of Judge Lauterpacht); M. Cherif Bassiouni, 'International Crimes: *Jus Cogens* and *Obligatio Erga Omnes*' (1996) 59(4) *Law and Contemporary Problems* 63–74, at 68; and *Restatement (3rd) of the Law: The Foreign Relations Law of the United States* (1987), vol. 2, § 702, pp. 161–2.

81 *Case Concerning Military and Paramilitary Activities in and against Nicaragua (Nicaragua* v. *United States of America) (Merits)* [1986] ICJ Rep. 14, pp. 100–1.

Therefore, peremptory norms may have minimal impact on PTAs in practice, given that few PTAs would ever be likely to conflict with these kinds of norms.

Aside from these non-derogable norms, several customary international law norms may apply to PTAs and PTA dispute settlement, either because the PTA does not specify that they are inapplicable (taking the Pauwelyn approach) or because the PTA designates them or customary international law more generally as part of the applicable law (taking the Trachtman approach). We now provide two examples of such other norms and how they might arise in a PTA dispute: the international norms on state responsibility, and international rules regarding exhaustion of local remedies.

In the *Myers* case, the NAFTA Arbitral Tribunal held that a Canadian ban on certain exports to the US violated Canada's NAFTA obligations and that Canada therefore must pay compensation to the US investor Myers for the injury caused to its investment in Canada.[82] The Arbitral Tribunal therefore needed to consider the 'principles on which compensation should be awarded'.[83] Noting that it had to decide the matter, pursuant to Article 1131, in accordance with NAFTA 'and applicable international law', the Arbitral Tribunal first considered the NAFTA provisions on compensation but found no relevant guidelines. It therefore turned to international law for guidance.[84] Referring to[85] the *Factory at Chorzów* decision by the Permanent Court of International Justice[86] and to the (then draft) *Articles on Responsibility of States for internationally wrongful acts* of the International Law Commission (ILC Articles on State Responsibility),[87] it concluded that the approach to calculating compensation should 'reflect the general principle of international law that compensation should undo the material harm inflicted by a breach of an international obligation'.[88] Thus, the Arbitral Tribunal applied an aspect of the international law rules on state responsibility either as a norm of customary law or as a general principle of law (as discussed further below).

The international rule on exhaustion of local remedies is widely accepted as having attained the status of customary international law.[89] In the context of a PTA

82 *Myers* v. *Canada*, para. 301. 83 *Ibid.*, Chapter XI. 84 *Ibid.*, paras. 304–10.

85 *Ibid.*, paras. 311–12.

86 *Case Concerning the Factory at Chorzów (Claim For Indemnity) (Merits)* [1928] PCIJ (Ser. A) No. 17, pp. 4 and 47.

87 See UN General Assembly Resolution, *Responsibility of States for Internationally Wrongful Acts*, A/RES/56/83 (28 January 2002) Annex, Article 36; and James Crawford, *The International Law Commission's Articles on State Responsibility: Introduction, Text and Commentaries* (Cambridge: Cambridge University Press, 2002).

88 *Myers* v. *Canada*, para. 315.

89 See, e.g., the sources cited in Chittharanjan F. Amerasinghe, *Local Remedies in International Law*, 2nd edn (Cambridge: Cambridge University Press, 2004), at pp. 3–4. See also Bernardo Sepúlveda Amor, 'International Law and National Sovereignty: The NAFTA and the Claims of the Mexican Jurisdiction' (1997) 19 *Houston Journal of International Law* 565–94, at 583–8. On the relationship between the rule on exhaustion of local remedies and 'denial of justice' (discussed above, section IIIA), see Amerasinghe, above, at pp. 84–106.

dispute, the question may arise whether the rule applies to preclude an alien investor from resorting to a PTA tribunal to challenge a measure of a PTA party before exhausting remedies available within the domestic system of that party. The ICJ in *Case Concerning Elettronica Sicula SpA (ELSI) (United States of America* v. *Italy)* suggested that the rule will apply to a treaty unless the treaty otherwise provides:

> The Chamber has no doubt that the parties to a treaty can therein either agree that the local remedies rule shall not apply to claims based on alleged breaches of that treaty; or confirm that it shall apply. Yet the Chamber finds itself unable to accept that an important principle of customary international law should be held to have been tacitly dispensed with, in the absence of any words making clear an intention to do so.[90]

In the specific context of PTAs, NAFTA again provides useful evidence of the application of the customary international law norm regarding the exhaustion of local remedies.

As mentioned earlier, even if the Arbitral Tribunal in *Loewen* had determined that it had jurisdiction, it would not have provided a remedy to the foreign investor (despite its finding of manifest injustice) because the investor had not, for example, appealed the offending court's decision to the US Supreme Court. Significantly, the Arbitral Tribunal distinguished between the procedural rule that 'requires a party complaining of a breach of international law by a State to exhaust the local remedies in that State before the party can raise the complaint at the level of international law'[91] and the substantive 'requirement that a decision of a lower court be challenged through the judicial process before the State is responsible for a breach of international law constituted by judicial decision'.[92] It reviewed a range of sources including the ILC Articles on State Responsibility,[93] decisions of the United States–Mexican Claims Tribunal and the Iran–United States Claims Tribunal,[94] and the work of several jurists,[95] and it stated, 'No instance has been drawn to our attention in which an international tribunal has held a State responsible for a breach of international law constituted by a lower court decision when there was available an effective and adequate appeal within the State's legal system'.[96] The Arbitral Tribunal relied on other international tribunals in exploring the scope of the obligation to pursue local remedies.[97]

Article 38(1)(d) of the ICJ Statute includes as an additional source of international law to which the ICJ should have regard in resolving disputes 'judicial decisions and the teachings of the most highly qualified publicists of the various

90 *Elettronica Sicula*, p. 42. 91 *Loewen* v. *US*, para. 149. 92 *Ibid.*, para. 156.
93 *Ibid.*, para. 149. 94 *Ibid.*, paras. 151 and 155. 95 *Ibid.*, paras. 150 and 152–3.
96 *Ibid.*, para. 154. On whether a 'reasonably available' alternative remedy in fact existed, see Noah Rubins, '*Loewen v. United States*: The Burial of an Investor-State Arbitration Claim' (2005) 21(1) *Arbitration International* 1–36, at 17–23.
97 *Loewen* v. *US*, paras. 165–6.

nations, as subsidiary means for the determination of rules of law'.[98] Thus, in relying on these various sources, the Arbitral Tribunal in *Loewen* was applying international law, not merely as a means to interpret NAFTA provisions, but as a non-interpretative rule of law. Ultimately, it concluded that 'Loewen failed to pursue its domestic remedies, notably the Supreme Court option and that, in consequence, Loewen has not shown a violation of customary international law and a violation of NAFTA for which Respondent is responsible'.[99]

While applauding the desirability of the rule on exhaustion of local remedies, William Dodge contends that the *Loewen* decision conflicts with Article 1121 and other NAFTA decisions on the issue.[100] Article 1121 of NAFTA sets out the 'conditions precedent to submission of a claim to arbitration' by an investor under Chapter 11. One of the conditions is that the investor:

> waive their right to initiate or continue before any administrative tribunal or court under the law of any Party ... any proceedings with respect to the [challenged] measure ... except for proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages, before an administrative tribunal or court under the law of the disputing Party.

Dodge contends that Article 1121 waives the international law rule on exhaustion of local remedies;[101] on that view, it is inappropriate for a NAFTA tribunal to rely on the rule.

Perhaps the reason for the apparent conflict that Dodge perceives lies in the distinction that the Arbitral Tribunal in *Loewen* drew between the procedural local remedies rule (which bars international jurisdiction in the absence of exhaustion of local remedies) and the substantive rule that States are not responsible for errors of their courts unless those errors have been appealed to the court of last resort. Arguably, the *Loewen* Arbitral Tribunal applied the second of these rules, whereas Article 1121 and other NAFTA tribunal decisions address the first.[102] In this context it is easier to understand the *Loewen* Arbitral Tribunal's conclusion that Article 1121 does not waive or modify the 'duty to pursue local remedies', at least where the

98 This provision is expressed as subject to Article 59 of the ICJ Statute, which states: 'The decision of the Court has no binding force except between the parties and in respect of that particular case'.

99 *Loewen* v. *US*, para. 217.

100 William S. Dodge, '*Loewen Group, Inc. v. United States*, and *Mondev International Ltd. v United States*' (2004) 98(1) *American Journal of International Law* 155–63, at 161–3 (referring to, *inter alia*, *Mondev International* v. *US*; and NAFTA Ch 11 Arbitral Tribunal, *Metalclad Corporation* v. *United Mexican States*, ICSID Case No. ARB(AF)/97/1 (Award of 30 August 2000)).

101 William S. Dodge, 'Investor-State Dispute Settlement between Developed Countries: Reflections on the Australia-United States Free Trade Agreement' (2006) 39(1) *Vanderbilt Journal of Transnational Law* 1–38, at 3; cf. *Loewen* v. *US*, para. 161 (referring to Professor Greenwood QC and the late Sir Robert Jennings).

102 See Rubins, above n. 96, at 16. Dodge's response to this explanation of *Loewen* is here: Dodge, above n. 100, at 162.

alleged international wrong is a judicial act:[103] 'It would be strange indeed if sub silentio the international rule were to be swept away'.[104]

Before turning to the issue of conflicts between PTAs and other treaties, we wish to make certain additional observations regarding the relationship between PTAs and 'general principles of law', which form a separate source of international law according to Article 38(1)(c) of the ICJ Statute. That provision directs the ICJ to apply 'the general principles of law recognized by civilized nations'. This is a complex area of international law that is explored elsewhere.[105] For the purpose of this chapter, it is worth noting that general principles of law may apply to PTAs and PTA disputes just as customary international law may do. To some extent these principles may overlap with customary international law, but as certain general principles may find no corollary in customary international law we should not forget this source of international law.

One important example of a general principle of law (as well as possibly a part of customary international law) that may be significant in a PTA dispute is the principle of good faith.[106] Indeed, Weiler describes good faith as a substantive principle of international economic law.[107] The scope and content of this principle is unclear, but some PTA provisions incorporate some form of it. For example, the AUSFTA requires parties, in the event of a dispute, to 'enter into consultations in good faith',[108] echoing the WTO's Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU).[109] Depending on one's understanding of the applicable law in PTA disputes,[110] this and other aspects of the principle of good faith may operate independently of any PTA provision.

In the *Pope & Talbot* case, the NAFTA Arbitral Tribunal rejected Canada's claim that the US investor was estopped from bringing a challenge under NAFTA Chapter 11, because the elements of estoppel recognised under international law were not made out.[111] Although estoppel did not lie in this case, in ruling on Canada's claim with reference to international law, the Arbitral Tribunal applied one particularisation of the principle of good faith. The principle of good faith may also require parties to a PTA to perform the PTA in good faith (*pacta sunt servanda*, as reflected

103 *Loewen* v. *US*, para. 164. 104 *Ibid.*, para. 162.

105 See generally Bin Cheng, *General Principles of Law as applied by International Courts and Tribunals* (London: Stevens & Sons, 1953); and Andrew D. Mitchell, *Legal Principles in WTO Disputes* (Cambridge: Cambridge University Press, 2008).

106 *Certain Norwegian Loans (France* v. *Norway) (Jurisdiction)* [1957] ICJ Rep. 9, p. 53. See also Cheng, above n. 105, at pp. 105–60; John O'Connor, *Good Faith in International Law* (Aldershot: Ashgate, 1991); and Andrew D. Mitchell, 'Good Faith in WTO Dispute Settlement' (2006) 7 *Melbourne Journal of International Law* 339–71, at 341–51.

107 Weiler, above n. 38, at 77. 108 AUSFTA, Article 21.5(1). 109 DSU, Article 4.3.

110 See section IIIB.

111 NAFTA Ch 11 Arbitral Tribunal, *Pope & Talbot Inc* v. *Government of Canada* (Interim Award of 26 June 2000), paras. 111–12.

in Article 26 of the Vienna Convention),[112] and exercise their rights under the PTA in good faith (in accordance with the doctrine of *abus de droit*).[113]

From these examples concerning state responsibility, the local remedies rule, and good faith, we can see that the practice of PTA tribunals (or at least those within NAFTA) is to apply substantive and procedural aspects of customary international law and general principles of law in resolving disputes. Where the PTA expressly overrides such international law norms (other than *jus cogens* norms), the PTA will typically prevail. However, resolving conflicts between PTAs and other treaties is more complex.

IV. Resolving conflicts between PTAs and other treaties

We now explore the possibility of conflicts between PTAs and other treaties, recalling that Article 38(1)(a) of the ICJ Statute includes as a potential source of international law 'international conventions, whether general or particular, establishing rules expressly recognized by the contesting states'.

A. Substantive conflicts

Because of the expanding content of PTAs and their broadening geographical coverage, they are increasingly likely to include rights or obligations that conflict with those under other bilateral or multilateral treaties, including the WTO agreements, other PTAs, and conventions on issues from human rights and the environment to development and consular immunities. The possibility of these conflicts raises issues similar to those discussed above in relation to PTAs and customary international law.[114] In particular, for the purpose of resolving disputes within the framework of a PTA, if the applicable law includes public international law (either because the PTA does not specifically exclude public international law or because the PTA specifically incorporates it, depending on one's point of view), the PTA tribunal will need to decide whether the relevant PTA rule or the conflicting non-PTA rule should prevail. This will of course depend on the circumstances, but several common considerations and guidelines will apply to the decision, as we explain below. If the non-PTA rule is to prevail, this may mean it provides a defence to a PTA violation, independent of any PTA provision providing for this defence.

The rules on treaty interpretation as discussed above,[115] including Article 31(3) of the Vienna Convention, may assist in avoiding conflicts between PTAs and other

112 See also, e.g., *North Atlantic Coast Fisheries Arbitration (United States* v. *Great Britain)* (1910) 11 RIAA 167, p. 186; *Gabčíkovo-Nagymaros Project*, p. 79; and Arnold D. McNair, *The Law of Treaties* (Oxford: Clarendon Press, 1961), at p. 540.

113 See generally G.D.S. Taylor, 'The Content of the Rule against Abuse of Rights in International Law' (1972–73) 46 *British Yearbook of International Law* 323–52.

114 See section IIIB. 115 See section IIA.

treaties. If a conflict does arise and cannot be avoided through interpretation, we must look to the PTA or conflicting treaty to see if any specific provision indicates how to resolve it. Article 30(2) of the Vienna Convention provides: 'When a treaty specifies that it is subject to, or that it is not to be considered as incompatible with, an earlier or later treaty, the provisions of that other treaty prevail'. Accordingly, the impact of a conflict rule may depend on its content and the timing and nature of the conflicting treaty.

One example of a PTA conflict rule that is likely to fall within Article 30(3) of the Vienna Convention and therefore be effective in resolving conflicts with certain other treaties is Article 20.3(3) of the Korea–Chile Free Trade Agreement, which states:

> Nothing in this Agreement shall affect the rights and obligations of either Party under any tax convention. In the event of any inconsistency between this Agreement and any such convention, that convention shall prevail to the extent of the inconsistency.

In contrast, Article 103 of NAFTA sets out its 'relation to other agreements' as follows:

1. The Parties affirm their existing rights and obligations with respect to each other under the General Agreement on Tariffs and Trade and other agreements to which such Parties are party.
2. In the event of any inconsistency between this Agreement and such other agreements, this Agreement shall prevail to the extent of the inconsistency, except as otherwise provided in this Agreement.

This provision does the reverse of what Article 30(2) of the Vienna Convention contemplates. However, it is consistent with the *lex posterior* rule reflected in Article 30(4)(a) of the Vienna Convention, as discussed further below, and it would be effective at public international law to ensure that NAFTA prevails over GATT 1994 and other previous agreements, at least as between the NAFTA parties.

In addition to the general conflict rule in Article 103, NAFTA contains a specific conflict rule regarding three multilateral environmental agreements (MEAs). Article 104 provides for obligations under the Convention on International Trade in Endangered Species of Wild Fauna and Flora,[116] the Montreal Protocol on Substances that Deplete the Ozone Layer,[117] and (upon its entry into force for the three NAFTA parties) the Basel Convention on the Control of Transboundary Movements of Hazardous Waste and Their Disposal ('Basel Convention')[118] to prevail to the extent of any inconsistency with NAFTA, subject to the condition that

116 Adopted 3 March 1973, in force 1 July 1975, 993 UNTS 243; (1973) 12 ILM 1085.
117 Adopted 16 September 1987, in force 1 January 1989, 1522 UNTS 3.
118 Adopted 22 March 1989, in force 5 May 1992, 1673 UNTS 57. At the time of writing, this convention has entered into force for Canada and Mexico, but the US is not yet a party.

'where a Party has a choice among equally effective and reasonably available means of complying with such obligations, the Party chooses the alternative that is the least inconsistent' with the provisions of NAFTA.[119] The *Myers* Arbitral Tribunal referred to this provision when Canada raised the Basel Convention as a defence to a NAFTA violation. As the Basel Convention had not (and still has not) entered into force for the US, Articles 103 and 104 of NAFTA meant that Canada's claim failed.[120]

FTAs may also contain provisions that are not explicit conflict rules but that provide exceptions for certain policy objectives or particular kinds of measures that may be promoted under other treaties (equivalent to, say, Article XX of GATT 1994 in the WTO context). The United States–Singapore Free Trade Agreement, for example, provides an exception for 'environmental measures necessary to protect human, animal, or plant life or health',[121] which could include measures undertaken pursuant to MEAs.

Article XXIV of GATT 1994 provides an example of a corresponding exception in another treaty that might conflict with a PTA (the WTO treaty). A PTA that meets the stringent requirements of this exception for 'customs unions and free-trade areas' would not conflict with WTO law, or at least not with GATT 1994. The same applies to the arguably less stringent requirements of Articles V and V*bis* of GATS,[122] as regards a conflict with GATS. Unfortunately, the limited jurisprudence to date sheds little light on the meaning of these exceptions,[123] which are contested and by their terms ambiguous,[124] if not inherently flawed.[125] Although this uncertainty may create a practical disincentive for one WTO Member to challenge another's compliance with Article XXIV of GATT 1994 (particularly in view of the proliferation of PTAs across the WTO Membership), it means that Article XXIV does not provide a lasting, predictable solution to resolving conflicts between PTAs and WTO law.[126]

119 Article 104 also extends to certain bilateral environmental agreements listed in NAFTA Annex 104.1.

120 *Myers* v. *Canada*, paras. 214–15. 121 Articles 13.4(1)(b) and (2).

122 Bernard Hoekman, 'Tentative First Steps: An Assessment of the Uruguay Round Agreement on Services', World Bank Policy Research Working Paper No. 1455 (May 1995), at p. 8.

123 Sungjoon Cho, 'Breaking the Barrier between Regionalism and Multilateralism: A New Perspective on Trade Regionalism' (2001) 42(2) *Harvard International Law Journal* 419–66, at 421 and 437–50. See also Joel P. Trachtman, 'Toward Open Recognition? Standardization and Regional Integration under Article XXIV of GATT' (2003) 6(2) *Journal of International Economic Law* 459–92, at 473–7 and 481–9.

124 On the many difficult issues surrounding the exception in Article XXIV of GATT 1994, see generally Nicolas Lockhart and Andrew D. Mitchell, 'Regional Trade Agreements under GATT 1994: An Exception and its Limits', in Andrew D. Mitchell (ed.), *Challenges and Prospects for the WTO* (London: Cameron May, 2005), at p. 217. See also James H. Mathis, *Regional Trade Agreements in the GATT/WTO: Article XXIV and the Internal Trade Requirement* (The Hague: TMC Asser Press, 2002); and Joel P. Trachtman, 'International Trade: Regionalism', in Andrew T. Guzman and Alan O. Sykes (eds.), *Research Handbook in International Economic Law* (Cheltenham, UK: Edward Elgar, 2007), pp. 160–74.

125 Sungjoon Cho, above n. 123, at 450–2.

126 For an example of how Article XXIV of GATT 1994 might apply to a challenged measure in practice, see Lorand Bartels, 'The Legality of the EC Mutual Recognition Clause under WTO Law' (2005) 8(3) *Journal of International Economic Law* 691–720.

Although Lorand Bartels argues that Articles 3.2 and 19.2 of the DSU operate as conflict rules in WTO dispute settlement[127] (which could operate to resolve conflicts with PTAs), they do not do so explicitly, and no consensus exists on any such rules. Language more clearly amounting to a conflict rule is found in non-trade treaties such as the Cartagena Protocol on Biosafety to the Convention on Biological Diversity,[128] the preamble of which states:

> *Recognizing* that trade and environment agreements should be mutually supportive with a view to achieving sustainable development,
>
> *Emphasizing* that this Protocol shall not be interpreted as implying a change in the rights and obligations of a Party under any existing international agreements,
>
> *Understanding* that the above recital is not intended to subordinate this Protocol to other international agreements . . .

These kinds of statements (which are followed in other treaties such as the draft Convention on the Protection and Promotion of the Diversity of Cultural Expressions adopted by the United Nations Educational, Scientific and Cultural Organization in 2005)[129] promote the positive notion of mutual supportiveness and allow some flexibility, while preventing the suggestion of any deliberate or blatant breach of WTO or PTA law. However, they may be ultimately too contradictory or unhelpful to resolve conflicts as they arise.

Especially where a PTA and another treaty 'relating to the same subject matter'[130] do not make clear how to resolve a substantive conflict between them (or where they conflict as to the proper way of doing so), the *lex posterior* rule as set out in Article 30 of the Vienna Convention comes into play:[131]

> 3. When all the parties to the earlier treaty are parties also to the later treaty but the earlier treaty is not terminated or suspended in operation under article 59, the earlier treaty applies only to the extent that its provisions are compatible with those of the later treaty.
> 4. When the parties to the later treaty do not include all the parties to the earlier one:
> (a) as between States Parties to both treaties the same rule applies as in paragraph 3;
> (b) as between a State party to both treaties and a State party to only one of the treaties, the treaty to which both States are parties governs their mutual rights and obligations.

127 Bartels, above n. 3, at 507.

128 Adopted 29 January 2000, in force 11 September 2003, (2000) 39 ILM 1027.

129 Adopted 20 October 2005, in force 18 March 2007, CLT-2005/CONVENTION DIVERSITE-CULT REV (20 October 2005), Article 20.

130 Vienna Convention, Article 30(1). See International Law Commission, above n. 5, paras. 253–6.

131 We leave to one side the possibility that the whole or part of a PTA might be 'illegal' by virtue of Articles 41 or 58 of the Vienna Convention, in which case a PTA conflict rule could not save it. See Pauwelyn, above n. 2, at pp. 302–15.

In general, problematic PTA conflicts would involve Article 30(4), namely because the PTA conflicts with an earlier multilateral treaty that includes the PTA parties as well as non-PTA parties.[132] In a dispute between PTA parties (or one party and an investor of another) the PTA would generally prevail in accordance with Article 30(3) of the Vienna Convention. However, in a dispute between a PTA party and a non-PTA party (say, before the ICJ or a WTO Panel), Article 30(4) provides that the earlier multilateral treaty would prevail. Accordingly, as a matter of international law, the PTA party would be obliged to comply with all its obligations under that earlier treaty with respect to non-PTA parties.

What if none of these rules – in the PTA, the conflicting treaty, or the Vienna Convention – is able to resolve a particular conflict? Essentially, no hierarchy exists between treaties, unless a *jus cogens* norm[133] or Article 103 of the Charter of the United Nations[134] is involved.[135] The principle of *lex specialis derogat legi generali* may assist, although its precise content and status at international law remain uncertain.[136] Therefore, the results in any given instance are difficult to foresee.

B. Overlapping disputes

All international tribunals may face difficulties in reconciling their role with the operation of existing domestic court systems, particularly where a given dispute is litigated at both domestic and international levels, either simultaneously or in sequence. Some PTAs mitigate this problem by precluding resort to domestic dispute resolution in some circumstances. For example, Article 21.15 of the AUSFTA provides: 'Neither Party may provide for a right of action under its domestic law against the other Party on the ground that a measure of the other Party is inconsistent with this Agreement'.[137] However, a growing problem for PTAs and international tribunals more generally is the potential for conflict between dispute resolution forums at the international level, with given circumstances giving rise to

132 Of course, the dating of a multilateral treaty such as the WTO agreements may be difficult. Is the date of the WTO agreements 15 April 1994 (signing), 1 January 2005 (entry into force), 11 January 2007 (most recent accession), or some other date, given that negotiations on revising the agreements have occurred almost continuously since they entered into force? For further discussion, see Pauwelyn, above n. 2, at pp. 372–84.

133 See section IIIB.

134 Article 103 states: 'In the event of a conflict between the obligations of the Members of the United Nations under the present Charter and their obligations under any other international agreement, their obligations under the present Charter shall prevail'. Article 30(1) of the Vienna Convention provides that the usual rules in Article 30 regarding successive treaties are subject to Article 103 of the UN Charter.

135 Ignaz Seidl-Hohenveldern, 'Hierarchy of Treaties', in Jan Klabbers and René Lefeber (eds.), *Essays on the Law of Treaties: A Collection of Essays in Honour of Bert Vierdag* (The Hague: Martinus Nijhoff, 1998), pp. 7–18, at pp. 7–9 ; and International Law Commission, above n. 5, paras. 324–79.

136 See International Law Commission, above n. 5, paras. 56–122; and Pauwelyn, above n. 2, at pp. 385–409.

137 See also NAFTA, Articles 1121(1)(b) and (2)(b).

potential claims under more than one treaty. This includes potential conflicts not only between rulings of the WTO's DSB and those of PTA tribunals, but also between rulings of one PTA tribunal and another, and between PTA tribunals and other specialised or general tribunals operating within public or private international law.

To combat this problem, many PTAs with dispute settlement mechanisms therefore include a 'choice of forum' clause. Article 21.4 of the AUSFTA thus states:

> 1. Where a dispute regarding any matter arises under this Agreement and under another trade agreement to which both Parties are party, including the WTO Agreement, the complaining Party may select the forum in which to settle the dispute.
> 2. Once the complaining Party has requested a panel under an agreement referred to in paragraph 1, the forum selected shall be used to the exclusion of the others.

A similar but more elaborate provision exists in NAFTA to prevent a complaining party from pursuing a remedy under both NAFTA Chapter 20 and the WTO dispute settlement system.[138] However, although these provisions may be effective within the PTA dispute settlement system, their impact outside that system may depend on the application of the VCLT rules as discussed above. In other words, a PTA party might bring a dispute first to a PTA tribunal and then to a different tribunal, despite the existence of a choice of forum clause preventing such action. Moreover, the complaining party might find the second tribunal amenable to hearing the dispute despite the existence of that clause.[139]

That conflicts between PTA tribunals and other international tribunals are more than mere possibilities is demonstrated by several recent WTO cases.[140] In particular, in *Mexico–Taxes on Soft Drinks*,[141] Mexico asked a WTO Panel to decline jurisdiction in order to enable the parties to resolve their dispute within NAFTA.[142] The Panel refused, and the Appellate Body upheld this decision.[143] However, the circumstances of the case were unusual, in that the dispute before the WTO was

138 Article 2005 of NAFTA. Regarding factors for parties to consider in deciding whether to use NAFTA or WTO dispute settlement, see generally Rafael Leal-Arcas, 'Choice of Jurisdiction in International Trade Disputes: Going Regional or Global?' (2007) 16 (1) *Minnesota Journal of International Law* 1–59.

139 Kwak and Marceau reach a similar conclusion: Kyung Kwak and Gabrielle Marceau, 'Overlaps and Conflicts of Jurisdiction between the World Trade Organization and Regional Trade Agreements' (2003) 41 *Canadian Yearbook of International Law* 83–152, at 106–7.

140 See, e.g., the cases discussed in Greg Anderson, 'Can Someone Please Settle This Dispute? Canadian Softwood Lumber and the Dispute Settlement Mechanisms of the NAFTA and the WTO' (2006) *World Economy* 585–610; Kwak and Marceau, above n. 139, at 91–5; and Gabrielle Marceau, 'NAFTA and WTO Dispute Settlement Rules: A Thematic Comparison' (1997) 31(2) *Journal of World Trade* 25–81, at 75–80.

141 Appellate Body Report, *Mexico–Taxes on Soft Drinks*; and Panel Report, *Mexico–Taxes on Soft Drinks*.

142 Panel Report, *Mexico–Taxes on Soft Drinks*, paras. 3.2, 7.11 and 7.12.

143 *Ibid.*, paras. 7.1, 7.18 and 9.1; and Appellate Body Report, *Mexico–Taxes on Soft Drinks*, paras. 57 and 85(a).

brought by the US against certain Mexican tax measures on soft drinks and other beverages, whereas the dispute that Mexico wanted heard before NAFTA would have been brought by Mexico against certain US measures limiting market access for Mexican cane sugar.[144] In addition, the US was stalling the NAFTA dispute by preventing panellist selection (indeed, this may have been part of Mexico's justification for imposing the measures that allegedly violated WTO law).[145] Hence, the NAFTA choice of forum clause did not apply to prevent the matter from proceeding before a WTO Panel.

The result might have differed had Mexico or the US called on the WTO Panel to enforce or apply the NAFTA choice of forum clause by declining jurisdiction or accepting that it lacked jurisdiction. In other words, had Mexico requested a NAFTA panel to resolve the dispute under NAFTA and then subsequently requested the establishment of a WTO panel to resolve the same dispute under WTO law, the WTO panel might have concluded that the choice of forum clause in Article 2005 of the NAFTA prevented it from adjudicating the dispute. Perhaps this is what the Appellate Body had in mind when it stated: 'we express no view as to whether there may be other circumstances in which legal impediments could exist that would preclude a panel from ruling on the merits of the claims that are before it'.[146] An express choice of forum clause preventing resort to both the WTO and a PTA panel might be one such 'legal impediment'. According to Pauwelyn, a WTO Panel faced with such a clause would have to conclude that it lacked jurisdiction to hear a dispute brought in violation of it (i.e., in violation of the agreement already reached between the disputing parties about how to resolve their trade disputes).[147] On the other hand, Kyung Kwak and Gabrielle Marceau contend that '[i]t is doubtful whether this type of provision would suffice to allow a WTO panel to refuse to hear the matter in situations where the dispute settlement process of the free trade agreement has been triggered'.[148]

Other doctrines might also prevent a PTA tribunal or other international tribunal from hearing a dispute that overlapped with another tribunal, thereby avoiding contradictory rulings. This is a complex area that Yuval Shany has ably covered elsewhere.[149] Nevertheless, it is worth briefly examining some of the

144 Panel Report, *Mexico–Taxes on Soft Drinks*, para. 7.14.

145 *Ibid*., paras 8.170 and 8.200; Pauwelyn, above n. 6, at 198.

146 Appellate Body Report, *Mexico–Taxes on Soft Drinks*, para. 54. See also Panel Report, *Mexico–Taxes on Soft Drinks*, para. 7.13.

147 Joost Pauwelyn, 'How to Win a World Trade Organization Dispute Based on Non-World Trade Organization Law: Questions of Jurisdiction and Merits' (2003) 37(6) *Journal of World Trade* 997–1030, at 1013.

148 Kwak and Marceau, above n. 139, at 90–1.

149 Yuval Shany, above n. 6. See also Vaughan Lowe, 'Overlapping Jurisdiction in International Tribunals' (1999) 20 *Australian Yearbook of International Law* 191–204.

considerations to which PTA tribunals might have regard in the face of a potential conflict with another tribunal. First, in recognition of the principle of judicial comity (even though this may not have the force of international law),[150] a PTA tribunal might defer or decline to commence proceedings while another tribunal was hearing the same or a closely related dispute. On the same basis, a PTA tribunal might refuse to adjudicate a matter that another tribunal had already resolved. This kind of response would express respect for the other tribunal and discourage forum-shopping by disputing parties, while also potentially reducing the chances of substantive conflicts between treaties (e.g., due to interpretations without regard to other treaties).

More legally forceful principles could also govern a PTA tribunal's response in these circumstances. In particular, *res judicata*, recognised as part of customary international law or as a 'general principle of law' within the meaning of Article 38(1)(c) of the ICJ Statute,[151] could prevent a PTA tribunal from hearing a dispute that had already been resolved by another tribunal. This could occur where the disputes before the two tribunals involved the same parties and issues[152] (on one view, therefore, *res judicata* cannot apply where the two tribunals apply different law, e.g., the law of the WTO agreements vs the law of the relevant PTA).[153] Similarly, even in the absence of a choice of forum clause, a PTA tribunal might hold that a complainant was estopped from bringing before it a claim of a PTA violation had it already brought essentially the same claim to another forum.[154]

One difficulty that a PTA tribunal might perceive in determining whether it lacked jurisdiction due to a pre-existing proceeding would be that it might need to analyse non-PTA laws to answer that question. This difficulty is reflected in the WTO context in *Mexico–Taxes on Soft Drinks*, where the Appellate Body emphasised, 'We see no basis in the DSU for panels and the Appellate Body to adjudicate non-WTO disputes'.[155] However, a PTA tribunal would not need to decide anything as a matter of non-PTA law in order to determine whether the doctrines of *res judicata* or estoppel applied or to decide whether and how to give effect to a choice of forum clause. Although it might need to consider non-PTA law to assess the similarity between the issues and claims before the two tribunals, it would not thereby be resolving a non-PTA dispute. The meaning of the non-PTA

150 Shany, above n. 6, at p. 262. See also Pauwelyn, above n. 6, at 202.

151 Cheng, above n. 105, at p. 336; and Shany, above n. 6, at pp. 245–6.

152 Shany, above n. 6, at pp. 24–5; and Pauwelyn, above n. 6, at 200.

153 Kwak and Marceau, above n. 139, at 103.

154 Cf. NAFTA Ch 19 Panel Decision, *In the Matter of Certain Top-Mount Electric Refrigerators, Electric Household Dishwashers, and Gas or Electric Laundry Dryers*, CDA-USA-2000-1904-03 (15 April 2002), pp. 25–6. For further discussion of *res judicata*, issue estoppel and collateral estoppel in the context of WTO v. PTA disputes, see Pauwelyn, above n. 147, at 1017–19.

155 Appellate Body Report, *Mexico–Taxes on Soft Drinks*, para. 56.

law would be a question of fact, just as international tribunals frequently evaluate domestic laws as questions of fact.[156]

V. Conclusion

Some aspects of the relationship between PTAs and public international law are much clearer than others. For example, few would question that the interpretative rules contained in the Vienna Convention guide the interpretation of PTA provisions unless the PTA provides otherwise. Through these interpretative rules, and specifically Article 31(3)(c) of the Vienna Convention, treaty law, customary international law and general principles of law may affect the meaning and development of PTAs. This includes, in particular, WTO rules and jurisprudence, which may shed light on PTA provisions, especially where the PTA provisions mirror those in the WTO agreements.

The relationship between PTAs and customary international law beyond the interpretative context is murkier, as is the existence and content of customary international law itself. Nevertheless, an examination of past PTA disputes, particularly under NAFTA, demonstrates that PTAs have the potential to contribute to customary international law. In addition, customary international law may apply to PTAs in a procedural and substantive rather than purely interpretative manner. Examples of this are found in the recognition of *jus cogens* norms, the international norms on state responsibility, and the international rule regarding exhaustion of local remedies.

The trickiest issues surrounding the overlap between PTAs and public international law arise where a PTA conflicts with another treaty, either because of conflicting norms between the two treaties or because of dispute settlement systems that are capable of hearing the same dispute. The potential for conflicts is growing as the number and breadth of PTAs grow, and further complications can be expected as individual PTA dispute settlement systems become more active or developed. Public international law offers some methods for dealing with treaty conflicts and intersecting jurisdictions, while the judicial experience of decision makers on tribunals may also assist. As to the extent to which PTA tribunals will make use of principles such as judicial comity, *res judicata* and *lex specialis derogat legi generali* to avoid or resolve conflicts, we can only wait and see.

156 See Tania Voon and Alan Yanovich, 'The Facts Aside: The Limitation of WTO Appeals to Issues of Law' (2006) 40(2) *Journal of World Trade* 239–58, at 251–2.

PART IV

Legal aspects of PTAs: A comparative analysis

7

Agriculture

TIMOTHY E. JOSLING

I. Introduction

Agricultural trade is regarded as a sub-category of trade in goods for the purposes of bilateral, regional and multilateral trade agreements. But in virtually all such agreements, it is subject to special treatment. This treatment in bilateral and regional trade agreements can range from exclusion from the schedule of tariff reductions to import restrictions by quota over a transition period, and often includes specific safeguards and new institutions such as committees to which problems can be referred. In multilateral agreements specific treatment for agricultural products has also been the rule: exceptions for primary products were included in the General Agreements on Tariffs and Trade (GATT 1947) and an Agreement on Agriculture was negotiated in the Uruguay Round that perpetuates the special treatment of the sector.

The reason for such exceptional treatment lies in the sensitive nature of agricultural imports. Most governments share a concern for the security of their country's food supply and the level and stability of the income of their rural sector. This concern has translated itself in importing countries into caution about relying on imports for basic foodstuffs and a conviction that protection from overseas competition is necessary for the health of the rural economy. Those countries with export potential in the agriculture sector have long decried such sentiments, arguing that they can provide a regular supply of foodstuffs at lower prices and that supporting inefficient domestic production is not a sound basis for development. But, as one might expect in a sector where governments still have considerable control over markets, negotiations to open up trade in farm products have tended to proceed at the pace of the most reluctant importers.

Within the past two decades, this cautious attitude towards trade in farm goods has begun to give way to a more confident approach that sees imports as complementary to domestic production and exports as a natural extension of domestic markets. Consumers are becoming used to the greater choice of foodstuffs that comes with trade, and producers are setting their sights increasingly on foreign markets for new sources of revenue. Developed countries still have 'sensitive' sectors that, for political reasons, need to be sheltered, from both local and global competition. Developing countries, too, are concerned about opening up markets

and putting their own producers' livelihoods at risk. But even in these cases regional and bilateral trade agreements are slowly constraining the ability of governments to maintain a high level of protection for agricultural producers.

For the purposes of this chapter, a distinction will be made between Regional Trade Agreements (RTAs) and Bilateral Trade Agreements (BTAs).[1] Regional Trade Agreements involve more than two countries and are generally concluded among countries in the same geographical region. Such RTAs share a number of characteristics that make them of interest in the area of agriculture. They are reciprocal, involving trade liberalisation by all parties, though some have different treatment for low-income partner countries. This reciprocal nature implies that agricultural sectors are inevitably brought into the complex trade-offs that are needed in a regional negotiation. Indeed, RTAs often have an underlying rationale of increasing regional cohesion and political integration, making the treatment of the agricultural sector of interest beyond the commercial advantage. Food security can be enhanced and economic stability improved by co-ordination of food policies and marketing infrastructure. Export patterns are often similar, limiting the immediate impact of regional liberalisation on agricultural trade flows, but trade possibilities are enhanced by proximity to markets. Of the two types of RTAs, those that involve a common external tariff (Customs Unions) and those where the members retain their existing external tariffs (Free Trade Agreements), agricultural problems tend to be easier to solve in the latter. External protection can remain the province of domestic authorities. But in Free Trade Agreements (FTAs), rules-of-origin are necessary to prevent excessive trade deflection. As agricultural products are often undifferentiated, making such rules of origin enforceable or effective is not always easy.

Bilateral Trade Agreements include those between two countries that may or may not be in the same region. These BTAs also usually include reciprocal obligations, though often phased to avoid problems in one or other party. Such bilaterals commonly are aimed directly at expanding trade between the countries concerned, though sometimes have a political rationale in addition. Agriculture poses both problems and opportunities in BTAs. Relations between the bilateral partners are often asymmetric, with smaller countries seeking assured access into larger markets, while the larger country is likely to be able to shelter sensitive import-competing sectors and to impose an agreement that favours its export interests. Thus BTAs

1 Also of relevance to agricultural trade are Preferential Trade Agreements (PTAs) that involve asymmetric obligations. These usually grant non-reciprocal market access into the preference-giving country. Commonly such preferences are granted by developed countries seeking to assist certain developing countries to expand or maintain their exports. However, such access is often constrained when sensitive domestic industries (such as agriculture) are involved. Generalised preference schemes offered by industrial countries to most developing countries (GSPs) and the asymmetric treatment of Least Developed Countries within the WTO and by some developed countries are also forms of PTA. Agricultural trade is often constrained under these schemes. However, this chapter only discusses reciprocal free-trade agreements (RTAs and BTAs).

involving a country that is a significant agricultural exporter will inevitably have provisions for improved market access for those goods.[2]

An examination of the treatment of agriculture in regional and bilateral trade agreements (RTAs and BTAs) suggests certain patterns. It is likely to be easier for agriculture to be fully included in an RTA if the parties to the agreement have similar production costs (whether high or low). Regional trade partners are more likely to have similar climatic and soil constraints and thus have similar production patterns, though disparate policies and production structures can lead to different cost structures among neighbours.[3] This gives the incentive for some degree of co-ordination within the region to take advantage of specialisation and scale opportunities and to avoid conflicts. For those regional groups with sufficient political cohesion, there is a tendency to develop common polices for agriculture (including a common level of tariff protection), but many such common policies lack operational significance. Bilateral trade pacts, by contrast, do not appear to venture down the path of common policies for agriculture. Production patterns are likely to be different, leading to greater possible gains from trade and less possibility of sheltering high cost production within the bilateral (trade diversion).

One of the issues in evaluating trade agreements for their consistency with WTO rules (specifically with Article XXIV of GATT 1994) is their product coverage. Article XXIV requires 'substantially all trade' to be covered, and the level of preference to be 100 per cent. Though there has as yet been no agreement on the interpretation of 'substantially all trade', agriculture is the sector most often excluded or treated differently. A simple measure of the difference between the inclusion of agriculture and manufacturing tariff lines in discriminatory trade agreements is given by the relative margin of preference (RMP) ratio. The striking difference in the sectoral coverage as given by this measure is shown in Figure 7.1, drawn from a WTO Secretariat presentation on RTAs.[4] Manufactures are far more likely to benefit from tariff reductions in RTAs than are agricultural goods. On the other hand, the prospect of competing exporters challenging the exclusion of agriculture in an RTA is remote: they benefit from the exclusion. And exporters within the RTA have implicitly agreed to the exclusion, and would be reluctant to make a challenge against a partner in respect of mutually agreed decisions.

How have sensitive sectors of agriculture been protected from competition from regional and bilateral partners? A review of the various ways that agriculture has been treated shows that this is most often done by quantitative restrictions on imports. On some occasions the sensitive sector is excluded altogether. More

2 BTAs are usually in the form of free-trade agreements rather than customs unions. One party (or both parties) to a BTA can itself (themselves) be an RTA.

3 The original six countries of the EEC differed in their costs, but were able to offset this by adopting a high level of protection that was geared to the least efficient.

4 Roberto V. Fiorentino, 'Regional Trade Agreements and the WTO: Theory and Practice of WTO Provisions on RTAs', Presentation given to Workshop, Rome, 10–14 October 2005.

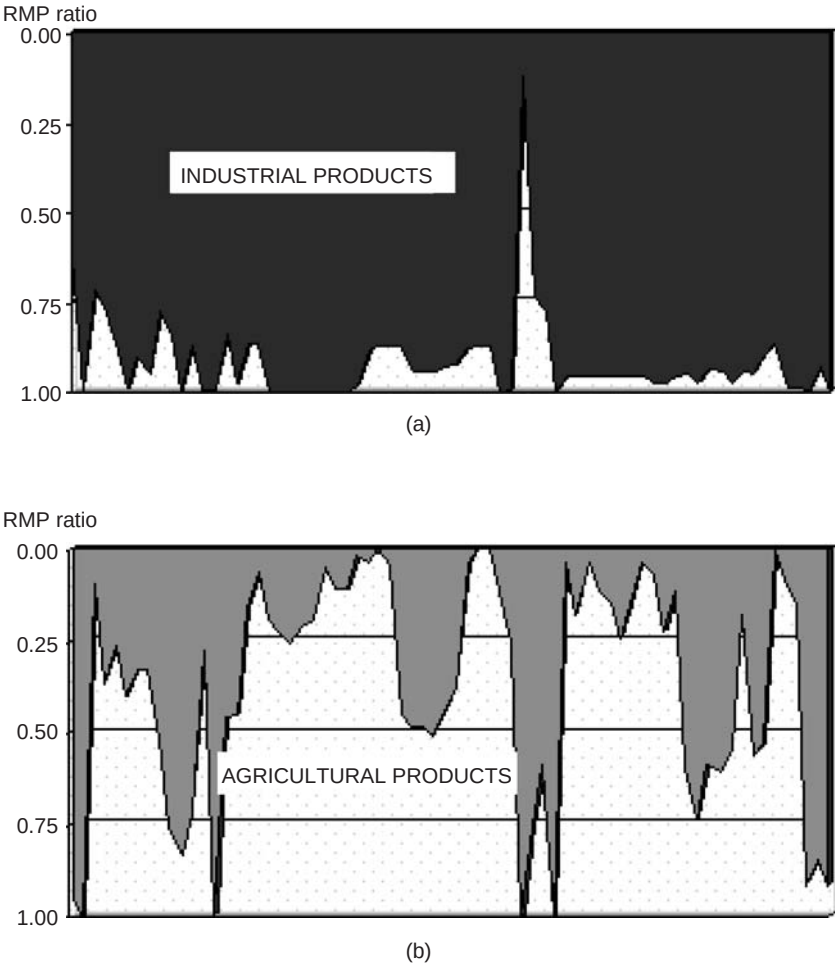

Figure 7.1 Comparison of the Depth of Liberalisation of industrial versus agricultural products

frequently, the tariff on imports from partners is reduced more slowly than that for other goods.[5] This chapter explores how the issue of agricultural trade is addressed in regional and bilateral trade agreements. The first section looks at regional trade agreements, grouping them by continent. The second section discusses bilaterals, particularly those being negotiated by the European Union (EU) and the United States (US). A third section looks at the prospects for future regional trade

5 Typically, the tariff schedule of each partner is divided into categories (A, B, C, etc.) corresponding to different reduction paths.

agreements and networks among such agreements in regard to the inclusion of agricultural trade.

II. Agriculture as an issue in Regional Trade Agreements

This brief survey focuses on RTAs that have emerged since the 1950s in the major trading regions of the world, Western Europe, the Americas, Africa and Asia. It does not try to be comprehensive: instead it illustrates the range of ways that agricultural trade has been incorporated in regional trade agreements.[6]

A. Agriculture in the RTAs of Western Europe

One of the first regional trade agreements of the modern era was the economic union between Belgium and Luxembourg (BLEU) that came into effect in 1922.[7] This pact integrated the smaller Luxembourg economy into the larger Belgian market and included bilateral free trade, the adoption of the Belgian external tariff, the use of the Belgian franc in Luxembourg and the development of common institutions. Agriculture was a problem area for the formation of the Union, as Luxembourg feared direct competition from Belgian farmers.[8] Special payments were made to Luxembourg farmers to compensate for the reduction of prices and later that country was allowed to re-impose quantitative limits on farm imports from Belgium.

The agricultural problems of the BLEU were exacerbated when the Netherlands entered the Union in 1948. The Benelux Union faced the problem that Dutch agriculture was more efficient than that of its partners. As a result, import restrictions were allowed within the Benelux market as an exception to free internal trade and the three countries essentially ran their own agricultural policies. The Netherlands continued to argue for the full inclusion of agriculture into the free trade zone, and it was eventually agreed that by 1962 the three countries should have a common policy and agricultural goods would circulate freely between

6 One region not discussed below is the Middle East. This does not imply that there has been no activity in this region. For example, in February 1997, the Arab League launched a free-trade programme, known as the Greater Arab Free-Trade Area (GAFTA), in which member states were asked to come up with specific commitments regarding elimination of tariffs, non-tariff measures and rules of origin. In the area of agriculture, the programme offered members the opportunity to suspend tariff reductions on some produce during the peak harvest seasons. Each GAFTA country was allowed to submit ten produce items for tariff suspension. So far, ten GAFTA countries have submitted a list of thirty fruits and vegetables. The exclusion of certain agricultural products during the crop/harvest seasons for the full transitory period of ten years will however substantially limit the trade creation effect.

7 The nineteenth century had been a period of extensive regional trade agreements, in the absence of any multilateral framework for trade rules. Most of these agreements were shattered by the events leading up to World War I.

8 Michael Tracy, *Government and Agriculture in Western Europe*, 3rd edn (Hemel Hempstead: Harvester Wheatsheaf, 1989), at p. 243.

Belgium and Holland, though the Luxembourg market was still protected. A fund was set up for adaptation of agriculture in the region, in essence to help Belgian and Luxembourg agriculture compete with the Dutch producers.[9] But events overtook this experiment in economic integration, as the three Benelux countries joined the European Economic Community (EEC) in 1957, and their agricultural policies were subsumed in the Common Agricultural Policy (CAP) of the EEC.

1. The EEC/EC/EU

The countries of continental Western Europe experimented in the 1950s with deep political and economic integration. In the context of rapid reconstruction of the war-torn economies, this regional integration played a strong role in the recovery of the European economies, and led directly to the formation of the EEC. Decisions made at that time with respect to the treatment of agriculture have had a lasting effect on Western Europe and on the world trading system.

The lessons of the Benelux Union were fresh in the minds of the architects of the EEC. The Spaak Report of 1956, which formed the basis for the Treaty of Rome that set up the EEC in the following year, emphasised the necessity to include agriculture in the common market. This was intended both to gain the advantage from the rationalisation of Western European farming and to make the EEC acceptable to the agricultural exporting countries (France, the Netherlands and Italy) in exchange for allowing German industrial products access into their markets. The Treaty established the principle of free movement for farm goods within the internal market but mandated 'market organisations' at the EEC level, at the insistence of the French, to manage the competition. The price for free internal trade was adequate external protection against third country imports (known as 'Community Preference').

The formation of the EEC in 1957 set the scene for the integration of Western European agricultural markets. A common market organisation (CMO) was developed for each of the main commodities. Administered prices were related to a 'target' price level for each commodity. Imports were only allowed in at 'threshold' price, calculated on the basis of the target price and transport costs, and excess production would be taken off the market at 'intervention' prices again fixed relative to the target price.[10] Prices were to be set each year by the Council of Ministers on the proposal from the European Commission.

The CAP was a major part of the EEC, and in fact was one of the few active 'common' policies (as opposed to the more passive removal of internal barriers to trade). The CAP dominated the work of the Commission, the spending of the common budget and the foreign trade policy of the emerging EU for its first three

9 *Ibid.*, at p. 245.

10 This terminology was used for the cereal market regime: some differences in instruments and nomenclature were introduced in the other commodity marketing organisations.

decades. Later, the CAP became a 'safe haven' against the forces of globalisation, but by the 1990s it proved increasingly difficult to sustain this isolation.

European integration has developed by 'widening' the EU to encompass new members as well as 'deepening' to embrace new functions. In the act of widening the same trend toward a fuller incorporation of agriculture is noticeable as in other regions, though progress is vastly complicated by the existence of the CAP. The countries of Central and Eastern Europe included agriculture fully in the Baltic Free Trade Area (BFTA) and in a more limited way in the Central European Free Trade Area (CEFTA), both intended as precursors to EU membership by the countries concerned. The Europe Agreements that aimed for free trade between the Central and Eastern European countries and the EU also included agriculture, initially with quantitative limits on products that threatened the operation of the CAP. Even these restrictions were relaxed as the process of integration developed. These countries became members of the EU, in May 2004, and they fell within the orbit of the CAP and thus their agricultural sectors will be essentially absorbed into that of the EU.

2. EFTA

The role that agricultural trade played in the architecture of post-war European integration is shown by the contrast between the EEC and the European Free Trade Association (EFTA), concluded in 1960 by seven of the countries that had opted out of the EEC. The position of the UK as a large importer of agricultural products from the British Commonwealth conflicted with the desire of the Six to expand internal trade behind tariff walls. Other countries (Sweden, Finland, Austria and Switzerland) had high-cost farming sectors as a result of climate or topography and did not wish to compete directly with Dutch or French producers. So the EFTA countries chose to exclude agriculture (and fisheries) from the free-trade provisions. Each country was able to maintain its own agricultural policy, through its tariff provisions and domestic support.[11]

The decision to leave agriculture (and fisheries) out of the EFTA agreement led to the exclusion of the sector from the terms of the European Economic Area (EEA), the set of bilaterals that the EU negotiated with the EFTA members as a way of keeping them close, in terms of economic regulation and price levels, with the EU. The EEA allowed free trade in manufactured goods and co-operation in regulatory issues: in effect it extended the previous bilaterals to include several aspects of trade that had been incorporated in the 1992 Single Market. Though some quotas on agricultural goods were expanded, there was no progress toward the incorporation of the rural sector in economic integration such as would be stimulated by enlargement. The EFTA countries still did not have a say in EU decisions, and thus were unable to influence regulations that would apply to them. The political stance

11 A side agreement guaranteed access for Denmark to the British market for pigmeat products and limited quantities of dairy goods.

of neutrality that had prevented several EFTA countries from having too close a tie with the EU countries became of less importance with the end of the Cold War. So, before the ink was dry on the EEA, Sweden made the decision to apply for full membership, and three other EFTA countries followed suit.

B. Agriculture in the RTAs of the Americas

1. LAFTA

Agriculture played a lesser role in the development of regional trade agreements in Latin America. The sector was largely excluded from the Latin American Free Trade Area (LAFTA) that was formed in 1960 and covered most of the subcontinent.[12] LAFTA, though in some respects following the European model, chose a quite different integration strategy. Rather than agreeing that all tariffs and trade barriers on internal LAFTA trade would be abolished, subject to a negotiated 'negative list', the decision was taken to offer a 'positive list' of sectors that would benefit from free trade. Not surprisingly, agricultural products were virtually absent from the list of sectors to be liberalised. Countries with export interests in farm products were not able to persuade their trade partners to open up their markets. Manufactured trade expanded in the region for the first few years, before also succumbing to the reluctance of countries to open their borders.

The nature of economic development in South America has tended to emphasise trade across the water rather than by land. Old colonial trade patterns linked port cities with European destinations. Development of internal transportation emphasised the movement of goods to the ports. The stimulus for the LAFTA came from the prevailing economic view of the early 1960s, as articulated by the Economic Commission for Latin America (ECLA) under the intellectual guidance of Raul Prebisch. This view held that trade with the industrial countries of Europe and North America was on increasingly disadvantageous terms, as prices for agricultural exports fell relative to the manufactured imports. It followed that industrialisation through import substitution was the key to economic development. Regional trade agreements fit into this pattern of development by promising the realisation of some economies of scale in the development of protected industries, through their location in one or more trade partners.

The timetable for liberalisation of trade in LAFTA slipped, and countries withheld offers to liberalise the sectors which were most sensitive. Agriculture was singled out as a sector which was not appropriate for liberalisation. The attitude towards agriculture reflected the generally prevailing development paradigm for the region. Import substitution in areas of manufacture was seen as the main thrust of trade policy, along with attempts to raise and stabilise the prices of raw materials on world

12 The seven original signatories were: Argentina, Brazil, Chile, Mexico, Paraguay and Peru and Uruguay. Colombia and Ecuador joined in 1961, followed by Bolivia and Venezuela.

markets. Regional import substitution was thus the aim of free-trade areas. Agriculture remained an exportable good, usually controlled by para-statal institutions and often taxed for revenue purposes. Intra-regional agricultural trade did not fit easily into this paradigm. Perhaps as a result of a misreading of the experience of the European Communities (EC), the inspiration for much of the economic integration in the 1960s, agriculture was not considered an essential part of a free-trade area.[13]

Andean Pact The Andean Pact (AP) arose from dissatisfaction with the workings of the LAFTA. There was a general feeling that the largest part of the benefit of the LAFTA had fallen to the largest countries, namely Argentina, Brazil and Mexico. The smaller economies were not receiving the benefits of industrial development, as both political weight and economic market size tended to pull these new industries to the big three countries. In addition, the poorer countries felt that making offers of tariff reductions in favour of the larger and richer nations would be exposing their own nascent industries to dangerous competition. As a result, Chile, Columbia, Bolivia, Ecuador, and Peru set up another trade group in 1969, known as the Andean Pact, which they felt was more suited to their own economic conditions. Attempts were made to avoid incompatibilities between the Andean Pact and LAFTA, but the effect was a mortal blow to the place of LAFTA in regional economic policy.

The Cartagena Agreement (1969), which established the Andean Pact, stated that the objectives of the AP should extend 'beyond' trade liberalisation to promote capital-intensive projects and to facilitate regional economic planning. Trade among the countries of the Andean Pact was to be free of all customs duties. The process of liberalisation was to be 'automatic and irrevocable' and include all products. Total liberalisation was initially set for the end of 1980 'at the latest', though this was extended for three years by the Lima Protocol of 1976.[14] A Common External Tariff was also to be agreed. Venezuela joined the AP in 1973.

Free trade among the AP countries was supposed to include agricultural products. However, in practice, the governments of the region chose not to allow agricultural goods to be traded freely. One of the first acts of the Andean Pact Commission was to enter a list of exceptions to free trade, including meat, dairy products, fruit, vegetables, cereals, rice, seeds, tobacco, hides and skins, timber, wool, and cotton. Most countries in the region had centralised purchasing and marketing structures for the basic agricultural products. Rigid price controls had been the norm, and countries were reluctant to allow regional trade to undermine the control of the

13 It was sometimes stated in discussions of Latin American integration that the EC had excluded agriculture from free internal trade (see, for instance, Sidney Dell, *A Latin America Common Market?* (New York: Oxford University Press, 1966); in fact, there was no exemption from the free movement of goods internally in the case of agriculture, as mentioned above.

14 Beverly M. Carl, *Economic Integration Among Developing Countries: Law and Policy* (New York: Praeger, 1986), at p. 227.

domestic market. Agriculture in most of the AP countries was adversely influenced by restrictive government polices, including export taxes and the effect of overvalued exchange rates. Investment was therefore discouraged in the domestic sector, whether for export or local consumption. Foreign foodstuffs, particularly from the US were often underpriced as a result of macroeconomic policies. Some agro-industrial activities were sponsored under the Andean Multinational Enterprise scheme.

The Andean Pact recovered some of its momentum in the 1980s, and developed, among other activities, a Common Agricultural Policy. The Presidents of the AP countries, meeting in La Paz, Bolivia in November 1990, indicated that the Andean Common Agricultural Policy would include the following elements: the equalising of conditions for competition in sub-regional markets; a stronger boost for joint development programmes; the adoption of sole stands in international forums; a common system for the treatment of food donations; the harmonisation of export incentives and policies and of mechanisms for stabilising the cost of imports from third countries; the progressive elimination of elements leading to price distortions; the consolidation of the free trade zone; and the strengthening of health activities. Such plans were by no means without substance. An Andean Pact price band, to stabilise domestic prices, was introduced, though not all countries adopted it. In effect, the AP (now the Andean Community) has become a vehicle for trade policy between Colombia and Ecuador and Venezuela: Bolivia and Peru have been increasingly impacted by the economies of the Mercado Commun del Sur (MERCOSUR) and eventually chose to become associate members of that group, along with Chile.[15]

2. MERCOSUR

The most significant step in recent years towards trade integration in the region has been the creation of MERCOSUR (the Common Market of the Southern Cone), in 1991. MERCOSUR negotiations were initiated in the mid-1980s by Argentina and Brazil, building upon an earlier agreement between those two countries. The four original members were Argentina, Brazil, Paraguay and Uruguay. This pact is one of the new 1980s variety of trade agreements that emphasised free internal trade over the *dirigiste* planning of the internal market, and emphasises the need for a low common external level of protection to prevent the cosseting of uncompetitive domestic industries.

The objectives of MERCOSUR are the acceleration of economic growth in the region by establishing free trade within its borders, and by co-ordinating economic policies for further integration. The Treaty of Asuncion aimed for the elimination of both tariff and non-tariff internal trade barriers by 1994, and

15 More recently, Venezuela became associated with MERCOSUR, but the economic provisions do not yet apply to that country.

the adoption of a Common External Tariff. The free internal market was delayed, but now covers 90 per cent of intra-bloc trade: the common tariff was agreed in 1994 and came into operation in 1995. The common tariff was set between zero and 20 per cent for most goods. A list of exceptions to the free internal trade has been drawn up, and some of these have yet to be removed. Some harmonisation of standards has already taken place, and discussions are under way on investment protection, anti-dumping and intellectual property rights. Though eventually envisioned, the free movement of labour and capital has not yet been achieved.

Among the countries of the MERCOSUR, agricultural trade is nominally free. Indeed, agricultural products are widely traded among the member States, notably from Argentina to the other countries. MERCOSUR has relatively few provisions that apply specifically to agriculture. Two reasons are likely to account for this relatively liberal treatment of agriculture. First, MERCOSUR includes major exporters of temperate agricultural products, each of whom would like to strengthen their agricultural industry and promote regional exports. Secondly, as a result of sweeping structural reforms, the countries concerned have eliminated many of the state marketing monopolies that previously controlled trade.[16] This, together with the reduction of subsidies and support prices, has allowed a fuller incorporation of agriculture within MERCOSUR than in many other RTAs.

Internal trade within the MERCOSUR bloc has always included agricultural products, and there was no real alternative to including agriculture in the provisions of the free trade treaty. Brazilian farmers were anxious about competing with the Argentinean producers, who have higher yields, lower costs and (in recent years) have been less taxed. Argentina had removed many agricultural programmes that would have interfered with free trade, including the National Grain Board, the National Meat Board and the sugar and tobacco boards. Brazil also removed the government monopoly on wheat marketing and trading, and cut producer subsidies in 1991, though Brazil retained many programmes for price regulation, and government storage. Uruguay still controls the import and export of wheat, but in general participates in regional agricultural trade. Paraguay, somewhat more remote from the coastal ports and transportation hubs, sells less of its products overseas, and is largely dependent on internal trade with MERCOSUR and Andean Pact countries.

Agriculture is thus a significant feature in intra-bloc agricultural trade in MERCOSUR, as contrasted with the situation in the Andean Pact. This gives it much more potential importance in trade policy developments in the region. But in addition, the fact that member countries are significant exporters to the rest of the

16 Argentina removed export taxes on agricultural goods, long a source of government revenue, in 1991. A small tax on oilseed exports remained, together with a fee to pay for research. Argentina has essentially liberalised imports of agricultural goods, though some export taxes have reappeared in recent years.

world complicates relationships with other trade blocs, such as the North American Free Trade Agreement (NAFTA) and the EU.

3. CUSFTA/NAFTA

As a first step in the direction of greater market integration in North America, Canada and the US signed an FTA in 1987 that took effect in January 1989. This agreement, the Canada–United States Free Trade Agreement (CUSFTA), liberalised trade between two countries of similar income levels who were already each the largest trading partner of each other. It was relatively easy to agree on a set of mutually agreeable steps to remove trade barriers.

Agriculture was included to the extent that it created no political problems. This meant essentially that Canada was able to exclude its supply-managed sectors, primarily dairy and poultry, which were managed largely by provincial marketing boards. Neither the US nor Canada wished to face the task of harmonising marketing systems for these products, and it was felt that the operation of the boards required control of all imports, including those from the US. As a result, the integration of these sectors was delayed. However, cereal trade did benefit from an agreement in the CUSFTA to allow imports from the other partner if the level of protection on the domestic market was not higher than that in the partner country. As a result of fluctuations in support levels over the first two years, trade barriers were essentially removed on grains moving across the border.

The request by Mexico to have a trade agreement with the US posed more significant problems for agriculture. In June 1990, Mexico initiated negotiations with the US, and in February 1991 these negotiations were expanded to include Canada. By August 1992, negotiations for a free trade area between the three countries were announced as completed. The agreement was subsequently ratified by the legislature in all three countries and went into operation on 1 January 1994.

Agricultural trade was evident in the motives for NAFTA negotiations. The US looked to gain market access in Mexico for grains and livestock products: Mexico wanted to be able to increase sales of fruits and vegetables in the US and reduce the chance that US trade barriers and health and safety standards would not be used to restrict such trade. On the other hand, Mexican growers of corn, in particular those in the low-productivity *ejido* sector, feared that US grain would sweep them out of business, and fruit and vegetable growers in Florida (and to a lesser extent, California) were concerned that their own sales into the US market would be undercut.

NAFTA set in progress the removal of all trade barriers to goods moving between countries in North America, and freed up trade in services except where sensitive regulatory issues precluded agreement. The time period for most sectors to achieve market integration was ten years, though the markets for some sensitive agricultural products were given fifteen years to adjust. NAFTA also sets up some common

institutions for settling disputes, and includes protocols on labour conditions and environmental legislation. A fund has been established to help Mexico improve environmental conditions, in particular in border regions.

Agriculture figured prominently in both the NAFTA negotiations and the debate over the ratification of the final agreement. As in the CUSFTA, it is one of a small number of sectors that is given the attention of a separate Chapter (Chapter Seven). The Chapter was structured to include a trilateral component, of relevance to all three countries and all agricultural commodities, and two separate bilateral trade agreements covering US–Mexico and Canada–Mexico agricultural trade. The general free-trade provisions of NAFTA (Market Access) apply to all trade, including agricultural trade, and the schedule of tariff reductions, along with the conversion of non-tariff barriers to tariffs, is contained in an Annex to that Chapter.[17] With few exceptions, all agricultural tariffs are subject to elimination on the schedules agreed in the NAFTA accord. The schedule of tariff reductions identifies categories of products subject to different rates of reduction.

As from the date of entry into force of the Treaty, no agricultural non-tariff barrier can remain unless specifically allowed by the GATT (under Article XI) or specifically included in the NAFTA text. Existing non-tariff barriers were converted into tariffs, as specified in the new tariff schedules, with tariff-rate quotas as agreed in the negotiations. Each country declared and was granted a set of exceptions to the provisions of the NAFTA.

The trilateral component of the agricultural agreement was relatively modest. It anticipated the existence of a GATT agreement in the Uruguay Round that was to cover the same areas of trade policy. It contains a statement on market access, that 'Parties shall work together to improve access to their respective markets through the reduction or elimination of import barriers to trade between them in agricultural goods', leaving the main action in this area to the bilaterals. Under Article 703.3, countries can invoke 'special' safeguards for selected (national) lists of commodities, representing the items judged to be most import-sensitive.

On domestic support, the NAFTA also contains the injunction to 'endeavor to work towards domestic support measures' that have minimal trade distorting effects, or that would be exempt under a future GATT agreement (the so-called 'green box' policy instruments). However, it recognises the right of Parties to change domestic support measures subject to GATT obligations. This light treatment of a contentious area enabled negotiators to say that they were not altering domestic policy.

On export subsidies, the text states that Parties 'share the objective of the multilateral elimination of export subsidies for agricultural goods' and promises

17 The Agriculture Chapter, however, has priority over the Agreement's 'general' Chapters where they affect the agricultural sector. If there is an inconsistency in tariff provisions between Chapter Three (Market Access) and Chapter Seven (Agriculture), the latter chapter prevails.

co-operation in the GATT to this end. However, the zeal for multilateral elimination of such policies does not extend to their internal use. Article 705.2 of the NAFTA merely holds it 'inappropriate' for a Party to grant export subsidies on sales to another Party unless the importing country is benefiting from export subsidies paid by other countries.[18] In other words, matching EU export subsidies in Mexico is allowable by the US and Canada, until such practices are stopped multilaterally. Indeed, if the exporting and importing parties agree to an export subsidy on intra-NAFTA trade, such a subsidy is allowed. This no doubt was included to take account of the considerable importance to the US of retaining the means to stay competitive with EC export subsidies in the Mexico market.

The trilateral agricultural agreement also set up some institutional mechanisms for administering the arrangements (a Committee on Agricultural Trade) and a new committee for dealing with private disputes (an Advisory Committee on Private Commercial Disputes regarding Agricultural Goods). The FTA Panel Review process is extended to include Mexico, adding procedures to be followed to address non-compliance or negation of a NAFTA Panel Ruling.

The trade aspects of NAFTA were included in three bilateral pacts and one trilateral agreement. The US–Canada bilateral pacts essentially continued the modest market opening in agricultural products that had been in the CUSFTA of 1986. An opening of the cereal trade across the Canadian border was ingeniously tied to the level of relative protection: neither side could maintain quantitative import restrictions if its own support level was higher than that of its neighbour.[19] Fluctuations in the level of support did in fact open up the grain trade, as both partners lost the right to protect their market in the first few years of the agreement. Attempts to integrate the US–Canada meat market proved less successful, and both pork and beef have been the subject of numerous bilateral disputes over the years. The sensitive sectors of dairy and poultry ('milk and feathers') were deliberately left off the table in the US–Canada talks, and so trade between US and Canada in these products remained restricted in the NAFTA.[20]

In sharp contrast to the cautious approach taken in the US–Canada bilateral, the US and Mexico decided on a bold initiative to move to a tariff- and quota-free market for all agricultural goods. Instead of permanent exceptions for sensitive products, long transition periods were agreed to put off for up to fifteen years the full impact of free access. For Mexico, the longest transition period was reserved for corn and beans, and for the US the sensitive products included citrus and tomatoes.

18 This is much softer language and treatment of export subsidies than was found in the CUSFTA where the use of export subsidies between the two countries was banned.

19 For this comparison the Producer Subsidy Equivalent (PSE) was used, though as it included direct payments, it was not the ideal measure of trade advantage.

20 Canada's bilateral agreement with Mexico mirrored that with the US: imports of dairy and poultry products were not included in the liberalisation schedules, but Canada gained access to the Mexican market at a rate similar to the US.

For sugar, the US and Mexico negotiated a complicated path toward free access into the US market by the end of fifteen years. Mexico retained its quota of 7,258 tons of raw sugar. If Mexico produced a surplus (at that time imports exceeded exports) a fixed amount of sugar, set at 25,000 tons, could enter the US duty free for each of the first six years. Thereafter, the quantity increases annually, jumping to 150,000 tons in the seventh year and rising by 10 per cent thereafter. If, however, Mexico should become a consistent net exporter of sugar, as actually happened, then the quantitative restrictions would eventually be removed altogether. The prospect of a single sugar market between the US and Mexico in 2008 is of concern to cane sugar producers in the US South and to other sugar producers throughout the States. Just as the Everything But Arms (EBA) agreement in the EU put pressure on the internal sugar regime (and the traditional preferred suppliers overseas) so the free importation of Mexican sugar could effectively erode the effectiveness of the high-price regime for sugar in the US.

Central America Five Central American countries agreed to form a free-trade area in June 1958, the Central American Free Trade Area. Two years later this was strengthened to become the Central American Common Market, under the General Treaty of Central American Economic Integration. The founding members were Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua.[21] Panama was admitted first as an observer and then attained the status of a full member in July 1991. The CACM flourished in the 1960s, floundered in the 1970s and practically disappeared in the 1980s. By 1970, the members had liberalised 94 % of intra-regional trade, and 80 % of external trade was subject to a common external tariff. After 1970, political problems among the members, as well as domestic strife within many of them, caused intra-bloc trade to decline.

The push toward regionalism has revived in Central America in recent years, as in other parts of Latin America. In 1990 the treaty was resuscitated and the decision was made to move to a common market by the end of 1992. The tariff rates on internal trade were to follow. A schedule was established of 5, 10, 15 and 20 % tariffs on different categories of inter-bloc imports. Most agricultural products traded within the CACM were to be free of duties by the end of 1991, with the rest being removed by June 1992.[22] Thus intra-bloc free-trade was finally to be extended to include agriculture.

As with the countries of the Andean Pact and MERCOSUR, the region of the CACM is on balance an exporter of agricultural products. Such exports declined slowly in the last decade although periodic booms in coffee prices interrupted this trend in 1994. Along with the reduction in exports of agricultural produce there has

21 Honduras left in 1967 and rejoined in 1991.

22 Augusto De la Torre and Margaret R. Kelly, *Regional Trade Agreements*, IMF Occasional Paper No. 93 (Washington, DC: IMF, 1992), at p. 7.

been a rise in imports of agricultural products, associated with the modest growth in the region. Fruit and vegetables constitute the major export items, along with sugar. Cereals and live animals are imported into the region.

There are however some significant differences between the situation in Central and South America. Central America is tied by trade links more closely to the US than are the countries to the south. The economies, being small, are relatively open: with trade amounting to 80 % of GDP in Costa Rica, 50 % in Honduras, El Salvador and Nicaragua, and 40 % in Guatemala. Well over 40 per cent of all trade is with the US. Twenty per cent of regional exports go to the EU, mainly coffee and bananas, and 11 per cent of imports come from Europe. Thus the security of trade pacts with the US and the EU has been a major aim of the region.

4. CARICOM

The Caribbean Common Market (CARICOM) was established by the Treaty of Chaguarmas in 1973, to replace the Caribbean Free Trade Area (CARIFTA) of 1968. The original membership of CARICOM included Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, and Trinidad and Tobago. Antigua and Barbuda, and the Bahamas joined in 1983, and the British Virgin Isles and the Turks and Caicos Islands became associated with CARICOM in 1990. Belize and Suriname also have become members. Within the CARICOM there exists another free-trade grouping, the Organization of East Caribbean States, (OECS) which includes seven of the smaller island members of CARICOM; Antigua, Dominica, Grenada, Montserrat, St Kitts, St Lucia and St Vincent. These countries established the East Caribbean Common Market in 1968, a prelude to the OECS Treaty of 1981. Recent developments in CARICOM have included the plans for a single internal market and a judicial body. Uneven country size and income levels have hampered the region in its quest for true integration but efforts continue in this direction.

The countries of the Caribbean region are among the most open of economies, and among the smallest in the hemisphere. Prior to gaining political independence and statehood these countries exported a limited range of traditional crops and imported not only manufactured products but significant proportions of their domestic food supply. The colonial legacy is still evident in the trade statistics today. Trade is heavily oriented towards the European market, in particular the UK. Trade with the US is large, but the volume of agricultural exports to that country is overshadowed by the imports of US temperate zone farm products. The US and the EC are the source of more than 55 per cent of CARICOM's imports and receive more than 60 per cent of its exports. There is a small but growing trade with Latin America, particularly as a destination for CARICOM's exports.

Agricultural commodity trade has traditionally been the life blood of the Caribbean economies. With few exceptions, agricultural trade has been critical to

the overall development of the economy. Agricultural exports provide more than 75 per cent of the foreign earnings for four of the Caribbean states and greater than 40 per cent for all but three of the states. The direction of agricultural export trade is strongly linked to the preferential trade agreements enjoyed by the region. In the case of the US these agreements come under the US Sugar Act and the Caribbean Basin Initiative (CBI). The former sets quotas on the amount of sugar that can be exported into the US market, while the latter eliminates import duties on a broad cross-section of imports from CBI countries. In the case of the EU the preferences are enshrined in the Lomé Convention (and now the Cotonou Agreement) under which the Caribbean exports sugar and bananas at preferential rates.

These preferential arrangements have been economically advantageous to the Caribbean. According to a World Bank study, 'in the period 1980–1986, preferential arrangements relating to sugar were worth an average of US$90m per year to Caribbean countries, and those relating to bananas an average of US$28 million per year'.[23] For bananas this benefit accrues mainly to the Commonwealth Caribbean. However, for sugar the benefits extend to the Dominican Republic, which in terms of both volume and value accounts for approximately 54 per cent of the region's sugar exports to the US.

The Caribbean Basin Economic Recovery Act, which gave substance to the CBI, was passed in the Congress of the United States in July 1983. The CBI is an integrated programme incorporating aid, trade and investment provisions promoting greater economic co-operation between the US and the Caribbean Basin countries (21 islands in the Caribbean and seven Central American countries). Trade expansion is considered a centrepiece of this agreement and is promoted through the elimination of US import duties on all but selected categories of imports from CBI countries. In August 1990, the CBI legislation was extended indefinitely.

C. Agriculture in Sub-Sahara African RTAs

Africa has a long history of RTAs, dating back to the desire to preserve some of the trade patterns among countries that had developed before independence. The goal of an African Economic Union has been espoused over the years. The reality, at least for agriculture, is that trade has not expanded along with the growth of RTAs. Trade patterns are still dominated by exports to the EU and by imports from European and American sources. Internal African food trade has been hampered by all manner of problems from political conflicts to inadequate roads. However, several trade agreements have emerged, not least as a result of the need to negotiate more effectively with outside institutions. Some of these are mentioned below.

23 World Bank, *Caribbean Region: Current Economic Situation, Regional Issues and Capital Flows, 1992* (Washington, DC: World Bank, 1993).

1. ECOWAS

West Africa had long experience in negotiating and operating free trade areas and customs unions among countries in the region. The first of these regional trade groupings stemmed from the early days of independence and followed the structures set up by the colonial authorities. Several francophone countries joined together to form in 1959 the West African Customs Union (UDAO/WACU) to preserve the customs union that had existed from before independence. Members of this group were Benin, Burkina Faso, Cote d'Ivoire, Mali, Mauritania, Niger and Senegal. They not only inherited a free-trade area but also benefited from a single currency tied to the French franc. The UDAO treaty called for common institutions and harmonisation of tax legislation, but proved to be too ambitious. The UDAO evolved in 1966 into the less demanding Customs Union of West African States (UDEAO/CUWAS). Trade at first rose rapidly within the UDEAO, but then fell back somewhat. Non-tariff barriers began to re-emerge, prompted by problems over the distribution of benefits within the region.[24] The UDEAO had virtually collapsed by 1972, when it was reorganised into the West African Economic Community (CEAO/WAEC). The CEAO enjoyed some success, but intra-bloc trade fell from 11.6 to 6.5 % of total (recorded) trade between 1983 and 1986. Non-tariff barriers re-emerged and the external tariff was never harmonised.

In 1975, the members of the CEAO joined with Nigeria and other English-speaking countries in the region to form ECOWAS. These included the three countries that had formed the Mano River Union (MRU) in 1973, Guinea, Liberia and Sierra Leone, as well as Gabon, the Gambia, Ghana, Guinea-Bissau, and Togo. This grouping of almost 200 million people aimed initially at liberalising the trade in agricultural and handicraft trade, to be followed later by manufactured trade liberalisation, the removal of non-tariff barriers and the establishment of a common tariff. The Economic Community of West African States(ECOWAS) also sought to promote 'harmonisation' of agricultural policies, including export price structures, and to curb (unofficial) trade in these commodities among member countries.

Agricultural trade is of paramount importance to the ECOWAS countries, but most of that trade is in tropical products for the European market. Intra-bloc trade in agricultural products is spasmodic, seasonal and often moves against the wishes of the authorities. Much of this illicit trade is an attempt to circumvent the normal marketing channels, usually run by parastatal marketing agencies. Some is 'normal' patterns of trade superimposed on 'artificial' national boundaries. Estimates of the extent of unrecorded trade reach as high as 30 per cent of recorded (total) trade, and would thus bring the level of intra-bloc trade up to that achieved for some other trade areas. Much of this unrecorded trade is in agricultural goods, responding to

24 For a discussion of the problems of these agreements, see Ulrich Hiemenz and Rolf J. Langhammer, *Regional Integration Among Developing Countries: Opportunities, Obstacles, and Options* (Teubingen, Germany: Westview Press, 1990).

seasonal production fluctuations, climatic advantage and arbitrage possibilities. Until this trade can be transformed into legal, sanctioned economic transactions, the ambivalence of authorities toward such activities will always impede liberalisation.

The ECOWAS treaty places particular emphasis on the need for policy co-operation in agriculture. Unlike many regional RTAs, the Lagos Treaty calls explicitly for a Common Agricultural Policy (Article 35). This policy is to co-ordinate the exploitation of natural resources in the area, as well as share research findings and harmonise internal and external agricultural policies. The ECOWAS Commission has produced a number of proposals and reports on the implementation of this policy, but as yet, little action has been taken.

2. CEEAC

In Central Africa, the Equatorial Customs Union (UDE/ECU) started in 1959, was replaced in 1966 by the Central African Customs and Economic Union (UDEAC/CACEU). The six members, the Republic of Cameroon, Central African Republic, the Republic of the Congo, Chad, Equatorial Guinea and Gabon, were francophone countries with relatively strong economies and the advantage of a history of monetary co-operation. The UDEAC aimed to set up a full customs union and set a timetable for the reduction of duties on regional trade. However, member states were allowed to introduce other barriers to intra-bloc trade. Intra-bloc trade stagnated, a victim of general slowdown in trade and reduction in income levels. More recently, an attempt has been made to expand and strengthen the agreement and encourage intra-bloc trade. This entailed the adoption of the Treaty establishing the Economic Community of Central African States, (CEEAC/ECCAS) in 1983. Besides the UDEAC countries, signatories included the members of the Economic Community of the Great Lakes Countries (CEPGL), the three former Belgian colonies of Burundi, Rwanda and Zaire, whose own free-trade area had been unsuccessful at generating internal trade flows, and the former Portuguese colony of São Tomé e Principe. CEEAC aimed for a free-trade area over a period of twelve years, with the final stage being the establishment of a customs union. As with other similar groupings, the timetable proved optimistic, and trade barriers still remain among the countries.

The CEEAC countries have experienced declining sales of agricultural produce over the years, while total merchandise exports have risen steadily. The countries concerned have somewhat similar agricultural conditions and production patterns. Expanded trade in the region is unlikely without a renewed effort to reduce the administrative and political impediments to market integration.

3. EAC, PTA, and SADC

Trade agreements are somewhat less numerous in Eastern and Southern Africa. In East Africa, the East African Community (EAC) was established in 1967 to take over from the colonial common market that had existed before independence. The EAC, with members Kenya, Tanzania and Uganda, also comprised a monetary union and

had a common tariff against third countries. The EAC finally broke up in 1977, unable to reconcile political differences between the members. More recently, two overlapping but rather different economic groupings have developed in southern and eastern Africa. In 1980, a number of states formed the Southern African Development Co-ordination Conference (SADCC), aimed at co-ordinating development in the region. Membership was primarily the States bordering South Africa, and had as an aim the reduction in dependence on transport facilities in that country. SADCC co-ordination extends to infrastructure, including transportation systems, and to agricultural research. It has proved attractive to donor organisations as a way of avoiding competing development strategies in the various member countries. The members created a new body, the Southern African Development Community (SADC), to extend operations more into trade matters.

More orthodox as a trade grouping, the Preferential Trade Area for Eastern and Southern African States (PTA) was set up in 1982 to promote liberalised trade, albeit with rules of origin which favour local manufacture. Members of the PTA include Burundi, Comoros, Djibouti, Ethiopia, Kenya, Lesotho, Malawi, Mauritius, Rwanda, Somalia, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe. The original plan called for a common market by 1992, but few parts of the liberalisation schedule have been adopted. A wide dispersal of incomes makes market opening difficult. The decision by the SADCC countries to extend their co-operation in the trade area put the two blocs in potential conflict. The PTA, after a slow start, has expanded in membership and scope. Renamed COMESA in 1994, it now includes among its members Libya and Egypt, as well nineteen other countries in the region.[25] However, the free-trade area only involves eleven of these countries, and ten of the COMESA members are also part of SADC.

Agricultural exports have been slipping in recent years, along with a general weakening of total merchandise exports. A sharp rise in agricultural imports over the past decade has eliminated the net exports from the region. Though one would not expect a high degree of intra-bloc agricultural trade in such a widely scattered region, opportunities undoubtedly exist for expanded commerce.

4. SACU

The South Africa Customs Union (SACU) has functioned for over 90 years among South Africa and the states in the immediate area. These presently include Botswana, Swaziland, Lesotho and Namibia. South Africa is the dominant economy, and the smaller states rely on that country for most of their trade. SACU is active in negotiating bilateral agreements, and this may have a positive impact on the development of the region as a whole. Agricultural trade is well integrated in the region, though each country still has autonomy in agricultural policy.

25 Two countries (Namibia and Swaziland) are members of the South African Customs Union (SACU). Tanzania has closer ties with the SADC countries, as well as a trade agreement with SACU.

D. Agriculture in the RTAs in Asia and the Pacific

1. ANZCERTA

The Closer Economic Relations Trade Agreement between Australia and New Zealand (ANZCERTA), came into effect in January 1983. It replaced an earlier agreement, the New Zealand–Australia Free Trade Agreement that had been introduced in 1966.[26] The first agreement had been somewhat limited in scope, covering a narrow range of manufactured products and trade in forest products.[27] The objectives of the ANZCERTA, besides broad co-operation in economic matters, included the removal of trade barriers between the two countries on an agreed timetable. Agriculture was to be included in the process of trade liberalisation, though some of the more difficult issues of parastatal marketing bodies were to be postponed.

A review of the working of the ANZCERTA in 1988 led to an acceleration of the process of liberalisation, and set the date of July 1990 for the removal of remaining tariff and non-tariff barriers. In addition, export subsidies on intra-bloc trade were to be removed, and many service sectors were included in the free-trade area. A further review was held in 1992, which added several new elements to the increasingly liberal economic relations between the two countries. The ANZCERTA takes the two countries further towards effective market integration than the NAFTA agreement in North America, though by no means as far as the EU.

One aspect of the ANZCERTA that is notable is the extent to which agricultural trade is now fully incorporated. The countries are major agricultural exporters. The product mix of exports is somewhat similar, reducing the scope for trans-Tasman trade, but there are natural trade flows based on climatic differences, such as sales of Australian wheat to New Zealand and exports of New Zealand dairy goods to Australia. These flows were hampered by tight restrictions on trade as a part of domestic marketing legislation. It took a bold political decision, coupled with a significant reduction in the power of the marketing agencies, to allow trade in agricultural products to flow freely.

2. ASEAN

The formation of ASEAN in 1967 was a manifestation of the desire to improve co-operation in a volatile region of the world. Such co-operation was more successful in the security than in the economic area. Though Singapore, in particular, had pushed for a free trade area, Indonesia was unwilling to travel as far in the direction of

26 There had been earlier, unsuccessful attempts to establish a free-trade area between Australia and New Zealand in the 1870s. New Zealand even considered joining the new Australian federation when it was formed in 1901. In the 1920s, the two countries granted each other mutual preferences as members of the British Empire: see Peter J. Lloyd, *The Future of CER: A Single Market for Australia and New Zealand*, Monograph No. 96 (Committee for Economic Development of Australia, Melbourne, and Institute for Policy Studies, Wellington, 1991), at p. 18.

27 *Ibid.*, at p. 12.

regional integration. At the Bali summit meeting in 1976 the leaders of the ASEAN nations expanded the scope of their co-operation to include regional tariff preferences (Preferential Tariff Arrangements), allowing intra-bloc imports to enter at a lower tariff rate, as well as promoting industrial development through ASEAN Industrial Projects and private firm co-operation on complementary ventures. The five founder members of ASEAN: Indonesia, Malaysia, the Philippines, Singapore and Thailand, were joined by Brunei in 1984 and more recently by Myanmar, Cambodia, Laos and Vietnam.

The lack of a commitment to free internal trade left ASEAN without a strong economic objective. The list of goods falling under the PTA expanded, but still covered only a small share of the members' total trade. Increases in intra-bloc trade have been small, due in part to the heavy reliance by countries on administered protection, and the continued opposition of local interests threatened with increased competition.[28]

With the renewed interest in regional trade liberalisation in recent years, an attempt has been made to turn ASEAN into a free-trade area along the lines of those in other regions. A plan for an ASEAN Free Trade Area (AFTA) was agreed by the six governments in 1992, with the objective of eventual free internal trade. Countries agreed to reduce tariffs on industrial goods and processed agricultural products on intra-ASEAN trade to a level of 0–5 per cent by 2008. The reductions are to be operationalised by establishing a Common Effective Preferential Tariff (CEPT) for each country that will be reduced on the basis of an agreed schedule. These tariffs are to be reduced to 20 per cent in the first eight years, with the remaining reductions coming in the final seven years of the transition. The reduction of non-tariff barriers to trade in manufactures is also mandated. However, expansion to include the four less developed economies has delayed realisation of the AFTA. Currently the target date for the completion of the free trade area is 2010 for the six more advanced members and 2015 for the remaining four. Though there has been an expansion in agricultural trade, many agricultural goods, foodstuffs and other primary products are still excluded from the planned liberalisation.[29]

Agricultural trade is important to the countries of ASEAN. The countries of the region account for 85 per cent of the world's rubber exports and 80 per cent of the palm oil trade, as well as significant quantities of copra and other raw materials. Agricultural trade within the region is less significant, though Singapore relies heavily on neighbouring countries for food supplies. Vulnerability to shortages of agricultural products on world markets has always been a concern of ASEAN countries. This aspect of agricultural trade was tackled in 1979, with the establishment of an emergency food stockpile, to which all would in principle contribute and from which each could withdraw in times of need. The initial

28 Dean A. DeRosa, *Regional Trade Arrangements among Developing Countries: The ASEAN Example*, Research Report 103 (Washington, DC: International Food Policy Research Institute, 1995), at p. 3.
29 *Ibid.*, at p. 4.

stockpile consisted of 50,000 tons of rice, a small but useful reserve in times of shortage.[30]

The ASEAN region is a net exporter of agricultural products, with rising agricultural exports keeping ahead of rising imports. ASEAN countries have been active members of the Cairns Group, the Group of 20 and the Group of 33. They can be expected to continue to push for further trade liberalisation at an international level, with an emphasis on maintaining policy flexibility at home. There is no doubt that increased trade among these countries would also be possible if agricultural liberalisation were to be fully included in the AFTA.

III. Agriculture as an issue in bilateral trade agreements

In contrast to the treatment of agriculture in RTAs, the way in which agriculture is treated in BTAs is a little more straightforward. RTAs grapple with the problem of the regional development of agriculture, balancing the benefits of rationalisation and efficiency against the interests of producers likely to be under pressure. Most BTAs have little interest in the development of regional agricultural competitiveness, but involve more the direct commercial exchange of goods, including agricultural products. The extent to which these BTAs include agriculture, then, is predominantly a matter of whether one or the other partner has specific commercial interests in such trade.

The nature of the agricultural component of BTAs can broadly be gauged by the policy of the largest of the trade partners: size of market allows considerable scope for setting parameters at an early stage in the talks. Thus there is a difference between BTAs negotiated with the EU and those with the US, and these are in turn different from those that involve China or Japan. The US has been persistent in arguing for the inclusion of agriculture in the BTAs that it has negotiated, and most of its negotiating partners have concurred, subject to safeguards and transition periods. However, the US has also been concerned to shelter some sensitive sectors, such as sugar, from open competition in BTAs. It has negotiated bilaterals with Chile, Central America, Colombia, Peru, Panama, Dominican Republic and Australia that give those countries preferred, though not free, access to US agricultural markets (see below). Negotiations with countries that are not major suppliers of agricultural goods, such as Morocco, Jordan, Singapore and Kuwait, have been easier to conclude and have only marginally impacted agricultural trade.

The EU has been more defensive, and is often under pressure by the negotiating partner to include agricultural products fully in the BTA. The EU gives limited access to sensitive agricultural products to the many countries that have signed such agreements, including the Mediterranean countries, the ACP, South Africa and Mexico, as described below. Negotiations with MERCOSUR, that have been put on

30 However useful this reserve is, it has rarely been used.

hold for the duration of the WTO Doha Round, were also approaching an agreement involving specific access to EU markets for grains, oilseeds and livestock products from South America.[31]

Japanese BTAs are even more cautious than those involving the EU with respect to entry of farm products. Negotiations on the bilateral with Mexico stalled for many months on the issue of imports of pig meat and oranges from Mexico. Eventually, the Japanese market was opened by a series of tariff rate quotas for beef, chicken and oranges and a reduction of tariffs for pig meat and orange juice. Japan has also negotiated a bilateral with Thailand, an efficient regional producer of rice and some other agricultural goods. Ratification of the bilateral is currently held up, as a result of political developments in Thailand, but most farm exports to Japan are covered by the agreement, albeit with transition periods: free trade in rice is not included. Japan has also agreed to lower trade barriers to many agricultural exports from the Philippines, under a BTA which came into effect in 2007, but the sensitive sectors of rice and sugar are not included in this agreement. An agreement between Japan and Chile is due to go into effect within a year, and will eventually allow imports of most of Chile's agricultural products. The Japanese BTA with Singapore was not hampered by issues of agricultural trade.

Korea has also negotiated a number of BTAs, often with the same countries as has Japan. Agriculture is even more of a sensitive issue in these agreements. Korean farmers have successfully argued that they cannot compete with imports. Thus, when Korea and ASEAN agreed an FTA in 2006, Thailand declined to sign the agreement, and has continued to argue for a significant tariff-rate quota (TRQ) for its rice exports to Korea. The bilateral with Chile has an emergency clause for agricultural products. Korea signed a bilateral with EFTA that went into effect in 2006 which excluded agricultural products. The bilateral with Singapore was similarly painless for agricultural interests. Discussions are underway with Canada, with the likelihood that there will be a long transition period agreed for agricultural products and some exclusions or limited TRQs. Negotiations with the US were concluded in April 2007, in time to be agreed under the US Trade Promotion Authority, and will again have strict limits on sensitive products and minimal liberalisation in rice. The discussion of an FTA with the EU was launched in early 2007, and the expectation is that agricultural sensitivities will be respected in this agreement.

China has also been active in negotiating bilateral trade pacts with countries in the region and beyond. Unlike Japan, China has considerable export potential in agricultural products. Tariffs on farm imports into China are in general lower than

31 This is made easier by the negotiation of tariff-rate quotas (TRQs) in the Uruguay Round that assured continued access for those countries with negotiated quotas. Allocation of TRQs allowed in WTO schedules to preferred partners is a main link between the multilateral and discriminatory trade regimes. These allocations appear contrary to the spirit of Article XIII of the GATT, which indicated that the distribution of quotas should be non-discriminatory and reflect market conditions.

in many other countries in the region. So, one condition of a trade agreement with China appears to be that agricultural trade is included. The negotiation of a partial FTA between China and ASEAN, designed to attain full free-trade status by 2010, included some agricultural goods among the 'early harvest' of July 2005. Indeed, agriculture is one of the 'Priority' sectors identified in that protocol. This followed an earlier partial FTA with Thailand, signed in 2004, that emphasised agricultural trade. Indeed, Thailand has recently experienced a surge in agricultural imports from China, leading to concerns about the impact of exchange rates and of the possibility of subsidies to Chinese export sectors. Negotiations with India, when they start, will be particularly difficult with respect to agriculture. Similar concerns with a rapid expansion of Chinese exports are being expressed by Indian farm interests.

India itself has become a desirable partner for a trade agreement. Besides the talks with China, India has been negotiating a BTA with ASEAN that could be signed in mid-2008. Agricultural sensitivities have been proved a problem, with both sides introducing 'negative lists' of goods to be excluded from liberalisation. An agreement to restrict the list to a maximum of 5 per cent of trade seems to have allowed the continuation of talks. But tropical products, particularly palm oil, rubber, coconuts, tea and pepper will feature prominently in remaining trade restrictions among these countries (as indeed they are within ASEAN). India began negotiations with Japan in 2007, and plans negotiations with the EU at a later stage.

The agricultural exporters that are the most active in seeking BTAs are Chile, Australia and New Zealand, with South Africa also showing an interest. However, the importer's sensitivities provide the parameters for the treatment of agriculture. Chile signed an FTA with EFTA in 2003 that omitted agricultural goods (Chapters HS1–24 of the tariff code), though it negotiated a 'complementary agreement on trade in agricultural goods' with each of the four current EFTA members that improved access marginally for Chile without any threat to domestic production in the importer. Australia has bilateral agreements with the US and is actively pursuing a BTA with Japan. Agriculture will also play an important role in the discussions with China that are expected to start within two years. New Zealand has not negotiated an agreement with the US but does have an FTA with Thailand that came into effect in 2005. New Zealand hopes to complete its own talks with China within a year, and though it has agreed to accept China's agricultural sensitivities it clearly expects extensive access to China's growing market for agricultural goods.

South Africa has made an effort to keep up with other exporters of temperate zone products in exploring BTAs that include agricultural goods. Once again, the results have differed depending on the sensitivities of the import markets. An FTA with the EU (mentioned below) was completed in 1999, and one with EFTA is under discussion. A trade agreement with MERCOSUR was signed in 2005, and plans are being made for talks with Kenya, Nigeria, China, Singapore, Korea and India. At a different level, India, Brazil and South Africa have floated the idea of a trilateral trade pact, perhaps along the lines of the trilateral between New Zealand, Chile and

Singapore (the 'Pacific Three'). Agriculture may not be the driving force behind such cross-regional agreements, but domestic support for such policies will require some inclusion of agricultural market access.[32]

Even where limits are put on the extent of the liberalisation of agricultural trade in these bilaterals, over time substantial amounts of agricultural trade face barriers that are less restrictive that MFN tariffs. Some of this trade is undoubtedly diverted from lower-cost suppliers, but trade creation is also likely to occur. Detailed empirical analyses of each agreement would be necessary to judge whether the BTAs as a whole are consistent with more liberal trade or mere trading of access into protected markets with little impact on resource allocation and expansion of consumer choice.

One result of the growth in BTAs is however clear: the agricultural marketplace is becoming a web of different rules governing access and safeguards. Multipart tariff schedules are becoming the norm, and rules of origin are themselves taking on increased significance. Although a detailed look at these issues in each of the bilaterals is clearly beyond the scope of this chapter, some further discussion of a selection of such agreements gives a view of the complexities that are emerging. The focus will be on the EU and the US bilaterals, as being not only the most numerous, but also the most significant, for other countries.

A. Treatment of agriculture in EU bilateral agreements

In the network of agreements involving the EU and non-members, agriculture is still treated as being largely outside the realm of unrestricted free trade. The Euro-Mediterranean agreements now being finalised between the EU and the countries of North Africa have so far avoided including unrestricted access for sensitive agricultural products, as does the customs union that was negotiated with Turkey. The negotiation of an FTA between the EU and South Africa was held up by the reluctance of the EU to grant improved access to goods that would have directly competed with those covered by the CAP. The agreement between the EU and Mexico was also difficult to negotiate, until Mexico abandoned its attempt to get easy access for a full range of agricultural products into the EU market.

Similarly, talks between MERCOSUR and the EU are finding it difficult to overcome the problems that improved access to the EU market would seem to pose for European agriculture. The Cotonou Agreement between the EU and the African, Caribbean and Pacific countries (ACP), that mandates the negotiation of a change in

32 Bilaterals are not confined to Asia, Europe and the Americas. Israel has complemented its FTAs with the US and the EU (see below) with pacts with Canada, EFTA, Romania, Bulgaria, Egypt, Jordan, Turkey, Mexico and MERCOSUR. The members of the Gulf Co-operation Council (GCC), separately or individually, are negotiating BTAs with Australia, China, MERCOSUR, Japan, Jordan, Turkey, New Zealand, India and the EU. Agriculture is not likely to be a major item on the agenda in these talks.

Table 1 *Bilateral trade agreements involving the EU*

Country/Agreement	Date/Status	Country/Agreement	Date/Status
EEA with EFTA countries (except Switzerland)	1992	Central America	Negotiations imminent
Cotonou Agreement with 78 African, Pacific and Caribbean countries (ACP)	2000	Andean Community	Negotiations imminent
Euro-Med	Agreements with most countries signed (except Syria and Libya)	India	Negotiations requested
South Africa	1999	Gulf Co-operation Council	Under negotiation
Western Balkans	Unilateral trade agreements with Albania, Serbia-Montenegro; FTAs with Croatia, Macedonia	EPA Pacific	Under negotiation
Mexico	2005	EPA Caribbean	Under negotiation
Chile	2006	EPA West Africa	Under negotiation
MERCOSUR	Negotiations well advanced	EPA Central Africa	Under negotiation
Korea	Negotiations suggested by Commission	EPA Southern Africa	Under negotiation
ASEAN	Negotiations suggested by Commission	EPA Eastern and Southern Africa	Under negotiation

Source: EU Commission, DG External Trade

the existing non-reciprocal agreements into full free-trade areas after eight years, will attempt to address agricultural trade issues, but these negotiations will also be hampered by inconsistency with the CAP. The trade agreement between the EU and the Least Developed Countries (called the Everything But Arms agreement) broke significant new ground in this respect, by providing duty- and quota-free access for agricultural goods, with only temporary derogations for the most sensitive commodities – rice, sugar and bananas.

1. Euro-Mediterranean partnership agreements

Traditionally, the EU has used the policy of trade preferences as a strategy of co-operation for development. Trade concessions have been granted by the EU on a unilateral basis to other countries. Now, Europe-Mediterranean agreements take further steps for trade liberalisation on a bilateral and reciprocal basis. Since the first Euro-Mediterranean Conference in November 1995, the EU and twelve Mediterranean countries have been engaged in negotiating Association Agreements (the Barcelona Process). The overall objective is to form, by 2010, one Euro-Mediterranean free-trade area from the separate agreements in place. The collapse of communism in Central and Eastern European countries (CEECs) and the conclusion of FTAs between these countries and the EU raised concerns that the Mediterranean Arab countries might be 'marginalised' in EU markets, as the competitive advantage that they used to enjoy in those markets would be eroded. To date, bilateral Association Agreements have been concluded with seven trade partners: Tunisia (1995), Israel (1995), Morocco (1996), Jordan (1997), the Palestinian Authority (1997), Algeria (2002) and Lebanon (2002).

Agriculture is a key sector in the debate between these trade partners as it is seen as necessary to establish a balance of commercial opportunities through the increase in both industrial and agricultural export from the region. However, trade in agriculture is subjected to weak liberalisation, within the present framework of the Association Agreements. No specific liberalisation roadmap has been defined for the agricultural sector as a whole. Only for certain products have specific concessions for liberalisation been determined.

The deferment of substantive negotiations of liberalisation of trade in agricultural products has been a constant feature of the Euro-Mediterranean partnership. This is largely explained by the political difficulties of reforming the EU's CAP and by the resistance on the part of European farmers who compete with non-EU member Mediterranean countries. The southern enlargement of the EC in the eighties redefined its relation with the Mediterranean partners. Spain, Greece and Portugal compete directly in agricultural products with the countries of North Africa, and these countries' political influence largely explains the limits to trade concessions through tariff quota and reference quantities.[33]

The other problem that needs to been considered by Mediterranean countries is a lack of diversification and competitiveness of their production structure. Several Mediterranean countries show a very similar product composition of exports. This is the case with Cyprus, Algeria, Spain, Israel and Morocco, all of them with an agriculture sector orientated to 'specialty products', mainly fresh fruit and nuts, olive oil and wine. The similarity of agricultural products makes supplies from non-member Mediterranean countries easily replaced by EU member countries, especially in the context of the enlargement of the EU to include Greece, Spain and Portugal as well as Malta and Cyprus.

33 Jose-Maria Garcia-Alvarez-Coque, 'Agricultural Trade and the Barcelona Process: Is Full Liberalization Possible?' (2002) 29(3) *European Review of Agricultural Economics* 399–422.

2. EPAs

The current negotiations between the EU and the countries of the ACP (the signatories to the Lomé and Cotonou Agreements) are proceeding in six regional talks. The EU is conversing with the ACP countries in the Caribbean region through CARICOM and their Regional Negotiating Mechanism. In the case of the African countries, negotiations are being channelled through four of the main regional agreements. ECOWAS, in collaboration with the West African Economic and Monetary Union (UEMOA/WAEMU), is the negotiating partner for sixteen West African states. Eight Central African states are negotiating through the Economic and Monetary Community of Central Africa (CEMAC) in conjunction with CEEAC with which it has plans to merge. Seven Southern African states are negotiating with the EU through SADC (though some of those states are not SADC members) and another fifteen are represented by COMESA, even though some of these countries do not participate in other COMESA activities.

B. Treatment of agriculture in US bilateral agreements

US policy towards regional and bilateral trade agreements changed dramatically in the mid-1980s. Long a champion of the multilateral system, and of non-discrimination, the U.S. has now become an active supporter of bilateral trade agreements as a complement to its commitment to the WTO and its membership of NAFTA. The US has completed, or is currently in the midst of, trade negotiations with thirty-one other countries aimed at creating about twenty-two separate FTAs.[34] The US strategy is to expand its commercial ties with countries for both economic and geopolitical reasons: the attraction to other countries is to secure preferred access to the large US market.[35]

The first of these recent FTAs was signed with Israel in 1985, as an expression of political and economic support for that country. The FTA with Canada followed in 1986, largely at the request of Canada, and was designed to consolidate existing sector agreements, encourage US investment north of the border and give Canadian firms some protection from aggressive use of trade remedy (anti-dumping and countervailing duty) provisions. But in 1990, Mexico requested similar conditions, to assure overseas investors of their access to the large US market. Canada opted to join the US and Mexico in the trilateral NAFTA which incorporated the earlier bilateral with Canada. An FTA with Jordan was agreed in 2001, again as a show of political support and economic assistance.

34 It is worth recalling that the US trade policy in the late 1930s took a similar direction. The Reciprocal Trade Agreements (RTA) Act was an open-ended mandate to sign bilateral trade agreements with other countries. Some thirty such agreements were signed.

35 In many cases the access is already covered by existing agreements, but the negotiation of a formal FTA reduces the uncertainty concerning the continuation of these preferences.

Table 2 *Current bilateral trade agreements involving the US*

Country/Agreement	Date/Status
Israel	1985 (Agricultural Agreement 1996)
Canada (CUSFTA)	1986 (Grandfathered into NAFTA)
NAFTA (Mexico and Canada)	1994
Jordan	2001
Singapore	2004
Chile	2004
Australia (AUSFTA)	2005
CAFTA (Costa Rica, Honduras, Nicaragua, El Salvador, Guatemala)	2006
Dominican Republic (added to CAFTA)	2006
Morocco	2006
Bahrain	2006
Oman	2006
Colombia (CTPA)	Congressional approval awaited
Peru (PTPA)	Congressional approval awaited
Panama (bilateral)	Congressional approval awaited
Korea	Congressional approval awaited
South Africa (SACU)	Negotiations continuing
Thailand	Negotiations continuing
Malaysia	Negotiations continuing
Ecuador	Negotiations continuing
Bolivia	Negotiations continuing
UAE	Negotiations continuing

Source: Author's compilation based on USTR website

The US began to negotiate more bilaterals in 2002, as an expression of a policy of 'competitive liberalization' as articulated by the United States Trade Representative (USTR). This policy consisted of offering swift negotiations to any country that was willing to conform to the terms consistent with the mandate of the US Administration as specified in the Trade Promotion Authority. The list of willing trade partners included Singapore, Morocco and Bahrain. Among the other bilateral agreements with a more significant agricultural component were those with Chile and Australia. Talks with Malaysia, Thailand, Panama, Colombia, Ecuador, Bolivia, the South African Customs Union (SACU), Korea, Oman, the United Arab Emirates (UAE) and Peru are in various stages of completion.[36] The list in Table 2 shows the FTAs that are either in operation, awaiting ratification or

36 SACU includes the Republic of South Africa as well as Botswana, Namibia, Lesotho, and Swaziland.

Table 3 *Summary of United States–Chile Free Trade Agreement (US–Chile FTA), Australia–United States Free Trade Agreement (AUSFTA) and CAFTA–DR–US arrangements for agriculture, and comparison with NAFTA*

	NAFTA	US–Chile FTA	AUSFTA	CAFTA–DR–US
Tariff cuts	Some tariffs eliminated: Others staged over 5, 10 and 15 years	Some tariffs eliminated: Others staged over 4, 8, 10 and 12 years Some cuts delayed for 2 and 4 years	Most tariffs eliminated: Others staged over 4, 10 and 18 years	Some tariffs eliminated: Others staged over 5, 10 and 15 years. Other cuts delayed for 6 or 10 years: duty free after 15 or 20 years
TRQs	Introduced during transition period for sensitive products	No use of TRQs introduced	TRQs for avocados, cotton, peanuts, tobacco, beef and dairy products into the US expanded. Above-quota duties for beef phased out over 18-year period. Current Sugar TRQs not increased: no cuts in above-quota tariff	TRQs for sensitive products in Annex 3.3. Rules on administration of TRQs (in addition to GATT Article XIII)
Agricultural safeguards	TRQs allowed as special safeguard for horticultural crops (Annex 703.3)	Additional duties linked to price trigger (Article 3.18) for goods listed in Annex 3.18 Total duties not to exceed MFN rate. Safeguard not operative after 12 years, or when zero-duty stage reached	Additional customs duties linked to price trigger for horticultural products (Annex 3-A Section A) and to quantity triggers for beef (Annex 3-A section B): price triggers used for beef in 19th year of	Additional duties linked to trigger quantities (Article 3.14) for products listed in Annex 3.14. Total duties not to exceed MFN rate. Safeguard not operative when zero-duty stage reached

Table 3 (*cont.*)

	NAFTA	US–Chile FTA	AUSFTA	CAFTA–DR–US
			agreement (Annex 3-A section C). Safeguard not operative when zero-duty stage reached	
Other safeguards	Safeguards (Chapter 8A): snapback to previous year's tariff on bilateral trade or MFN tariff	Trade remedies (Chapter 8) GATT 1994 Article XIX Safeguards	Safeguards (Chapter 9) GATT 1994 Article XIX Safeguards	Trade Remedies (Chapter 8) GATT 1994 Article XIX Safeguards
Export subsidies	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidised exports to NAFTA markets. Agreement to work together for elimination in the GATT	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidised exports to Chile or the US. Agreement to work together for elimination in the WTO	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidised exports to Australia. Agreement to work together for elimination in the WTO	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidised exports to CAFTA–DR–US markets. Agreement to work together for elimination in the WTO
Domestic support	Agreement to work together in GATT for the reduction of domestic support levels and shift to less trade-distorting instruments	Agreement to work together in WTO for the reduction of domestic support levels and shift to less trade-distorting instruments	Agreement to work together in WTO for the reduction of domestic support levels and shift to less trade-distorting instruments	Agreement to work together in WTO for the reduction of domestic support levels and shift to less trade-distorting instruments
SPS measures	Precursor of WTO SPS Agreement (Chapter 7B)	Affirm commitment to SPS Agreement	Work to resolve trade conflicts over SPS barriers	Affirm commitment to SPS Agreement

Dispute settlement	Dispute settlement mechanism for matters arising from Agreement (Chapter 20). Separate procedures for review of anti-dumping and countervail actions (Chapter 19)	Dispute settlement mechanism for matters arising from Agreement (Chapter 22)	Dispute settlement mechanism for matters arising from Agreement (Chapter 21). Provision for monetary penalties	Dispute settlement mechanism for matters arising from Agreement. (Chapter 20)
Institutions	Committee on Agricultural Trade; Working Group on Agricultural Subsidies; Advisory Committee on Private Commerce; Disputes regarding Agricultural Goods	Working Group on Agricultural Trade; Committee on Sanitary and Phytosanitary Matters	Committee on Agriculture; Standing Technical Working Group on Animal and Plant Health Measures	Committee on Agricultural Trade; Agricultural Review Commission; Committee on Sanitary and Phytosanitary Matters

Source: Author's compilation from FTA texts

are under active discussion. Recent agreements have often been designed as 'templates' for future FTAs within a region. Thus the FTAs with Bahrain, the UAE and Oman are seen as building blocs toward a Middle-East Free Trade Area, and the negotiations with Malaysia and Thailand (along with that already in place with Singapore) are supposed to pave the way for other bilaterals with ASEAN countries. The FTAs themselves usually follow from Trade and Investment Framework Agreements (TIFAs) and Bilateral Investment Treaties (BITs). The US has a considerable number of TIFAs and BITS in place that would form the basis for bilateral FTAs.

What agricultural provisions do these FTAs contain? All of the FTAs have provisions for tariff reductions that affect many food and agricultural goods. However, with few exceptions, the agreements control trade in a range of products considered politically sensitive in one or both partners. For the US these sensitivities include sugar, citrus fruits, peanuts and dairy products, and for the partners the list includes corn and beans along with rice.

Three current agreements have the most actual or potential impact on US agricultural markets and hence on the environment in which policy is formed: the recent FTAs with Chile and Australia, along with the CAFTA–DR–US agreement. Table 3 gives a summary of the main characteristics of each agreement.

1. CAFTA–DR–US

The US and five Central American countries – Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua – began negotiations for a Central American Free Trade Agreement (CAFTA) in 2003. President Bush notified the US Congress of his intention to enter into the CAFTA on 13 February 2004, and it was approved by Congress, under the Trade Promotion Authority granted to the President in 2002. CAFTA–US took effect in 2006. Negotiations with the Dominican Republic were concluded on 15 March 2004 that would fully integrate that country into the CAFTA. In addition, bilateral negotiations are underway with Panama, which if completed will conclude the establishment of FTAs between the US and almost all of the countries in Central America.[37]

The CAFTA–DR–US is intended to help foster economic growth and improved living standards in the Central American region by reducing and eliminating barriers to trade and investment. It essentially converts the non-reciprocal and discretionary benefits that these countries get from the CBI into permanent and reciprocal access to the US market. Though covering all trade, the agricultural component is one of the most important aspects of the FTA. The main agricultural

37 Mechel S. Paggi, Fumiko Yamazaki, and Timothy E. Josling. 'The Central American Free Trade Agreement: What's at Stake for Californian Agriculture?' (2005) Center for Agricultural Business, California State University, Fresno.

provisions of CAFTA–DR–US are summarised in Table 3. The key to the agricultural agreement is market access, with relatively few provisions in the areas of export subsidies and sanitary and phytosanitary regulations. Domestic subsidies are not covered by the agreement.

The CAFTA–DR–US will create improved market opportunities for US agricultural products and related goods and services. Agricultural trade barriers in the Central American countries are higher than those for manufactured goods. CAFTA–DR–US locks in the applied duty rates for many products and ensures that permanent US access to the market is preserved. However the short-term impact on US exports of the CAFTA–DR–US may be modest as the terms of the agreement delay the full benefits of increased access to the countries of the region for US agricultural products of interest. The lengthy phase-in period for increased market access and back-loading of commitment levels suggest the benefits of the agreement may only be realised many years from now.

Increased market access for Central American goods to the US will also be a consequence of CAFTA–DR–US. However, the impact here is likely to be even more limited, as most CAFTA–DR countries have had permanent duty-free access to the US market since the late 1960s under the Generalised System of Preferences (GSP), and, since 1990, under provisions of the CBI and the CBERA that implements the CBI. The CBI was enhanced in 2000 under the terms of the Caribbean Basin Trade Partnership Act (CBTPA) to give access more equivalent to that enjoyed by Mexico under the NAFTA. In fact, approximately 99 per cent of CAFTA–DR–US exports already enter the US market duty free. Duties are paid only on over-quota imports as part of the US tariff-rate quota regimes for sugar, dairy, cotton, meats, and peanuts.[38]

Chile The bilateral FTA with Chile was easier to negotiate than either NAFTA or CAFTA–DR–US. Chile is an important exporter of agricultural products, particularly fruits and vegetables and wine, but the different seasonality makes the produce complementary to rather than competitive with US production. So the beneficiaries were the supermarkets that could ensure year-round supplies. Moreover, Chile is one of the more liberal of the Latin American countries, even on agricultural products, implying that opening up to the US exporters was not such a big move for the Chilean farmer. Besides some controversy over wine labels, the talks went smoothly. It may have helped that Chile is not a significant sugar exporter.

Australia The Australian agreement also involved a country from the Southern Hemisphere, and thus offered some advantages of complementary production. But Australia is a major exporter of meats, dairy products, cereals and sugar, so tight

38 For more details on CAFTA and its potential impact on US agriculture, see *ibid.*

rules had to be built in to the FTA to protect US farmers from competition from Australia. Reluctantly, Australia accepted a long transition period for dairy production and beef, as well as an exclusion altogether of any relaxation of protection for the US sugar sector. This decision may have an impact on the politics of future bilaterals.

2. KORUS FTA

The most ambitious bilateral to have been negotiated since NAFTA is under consideration by Congress at present. The Korea–United States Free Trade Agreement (KORUS FTA) would establish a free trade area between the US and a major economy in East Asia. There was no doubt from the beginning of the talks that agriculture would be a stumbling block, with the Korean government in particular not wishing to open up the highly-protected rice market to US exports. However, the US position had been to include rice, even if access for US rice is introduced slowly over a transition period. In the end, the rice sector was excluded from the agreement. This establishes a precedent if the KORUS FTA were to act as a template for an agreement with Japan.

IV. RTAs, BTAs and the WTO: Key issues for agriculture

Regional and bilateral trade agreements coexist, if somewhat uneasily, with multilateral trade rules as enshrined in the WTO. One of the most significant issues facing negotiators of regional and bilateral pacts is their relationship with the WTO. In the case of agricultural trade, this interaction is more than usually pertinent. This section discusses the interaction between the treatment of agriculture in RTAs and BTAs and the rules of and negotiations under the WTO. This relationship is often one of symbiosis rather than antagonism. Many of the problems that make the incorporation of agriculture in a regime of free regional or bilateral trade exist to complicate moves towards multilateral trade liberalisation. So the solution of these problems at one level can assist with their solution at another.

As prelude to this discussion, it is useful to recall the tangled history of the incorporation of agricultural trade into the multilateral trade system. The GATT, as it emerged in 1947, applied to agricultural trade but also included two articles that specifically modified the impact of the general provisions relating to trade in goods. Article XI, which established the principle that non-tariff trade barriers could only be used under specific circumstances, made way for some types of agricultural programmes. The article recognised the case where an agricultural product is subject to quantitative restrictions on domestic production (Article XI:2 (c)): Under such circumstances quantitative import restrictions were allowed.[39] Many countries

39 Timothy E. Josling, Stefan Tangermann and Thorald K. Warley, *Agriculture in the GATT: Past, Present and Future* (Basingstoke: Macmillan Press, 1996).

relied on this clause to restrict imports by quantitative trade barriers when domestic markets were being managed. The other agricultural 'exception' was to specify different rules for export subsidies of manufactures and primary products. Though the original GATT subjected both primary and manufactured product export subsidies to the same notification and consultation procedures, in 1955 it was agreed to add an explicit prohibition on export subsidies on manufactured goods (Article XVI). Agricultural export subsidies were constrained only by the obligation not to use such subsidies to capture 'more than an equitable share' of world markets. Successive GATT panels failed to come up with a satisfactory definition of this concept, and agricultural export subsidies in effect escaped any disciplines.[40]

The Uruguay Round attempted to address these issues directly. Non-tariff trade barriers were to be converted to tariffs and bound in the WTO schedules. A schedule of tariff reductions for agricultural goods was agreed.[41] TRQs were introduced in cases of tariffication to ensure current market access and open up additional markets. These TRQs were increased from 3 to 5 per cent of consumption over the implementation period. Export subsidies were not totally eliminated, but new ones were banned and existing subsidies declared and entered into country schedules. In addition, domestic subsidies paid to farmers were classified, depending on their notional level of trade distortion, into three categories, which have become known as the Amber Box, the Blue Box, and the Green Box.

Amber Box measures were those tied to output or input prices or to current output levels: their magnitude was calculated as an 'Aggregate Measurement of Support' (AMS). Total AMS has to be reduced by 20 per cent over the implementation period. The Blue Box contained subsidies that were tied to supply control programmes: such subsidies were regarded as less obviously output-increasing. No reduction was required for Blue Box policies, though there were constraints on their increase. Green Box subsidies were defined as those unrelated to price and output ('decoupled') and included research and extension, payments designed to compensate farmers for the cost of compliance with environmental

40 Timothy E. Josling, and Stefan Tangermann, 'Production and Export Subsidies in Agriculture: Lessons from GATT and WTO Disputes Involving the US and the EC', in Ernst-Ulrich Petersmann and Mark Pollack (eds.), *Transatlantic Economic Disputes: The US, the EU and the WTO* (New York: Oxford University Press, 2003). Even these two exceptions did not constrain farm policy in developed countries. A prominent example of this was the imposition of quotas by the US under s 22 of the Agricultural Adjustment Act (as amended) that mandated quantitative restrictions on imports of a number of goods whenever domestic programs were 'materially interfered with' by imports. This required a waiver of the US obligations under Article XI, a waiver that was renewed annually until made irrelevant by the Uruguay Round outcome. The EU also avoided restraints on its Common Agricultural Policy (CAP), which used 'variable levies' to stabilise the duty-paid price of imports. Such an instrument was not easily classified as either a customs duty or a quantitative restriction. The Uruguay Round Agreement on Agriculture specifically bans such variable levies.

41 Developing countries were allowed to use 'ceiling bindings' often at arbitrarily high levels and across many commodities. Actual tariffs applied have generally been well below these ceilings, giving countries ample scope for granting preferential access and for modifying tariff levels with world price changes.

regulations, and domestic food assistance programs. 'Green Box' policies were unconstrained, as having minimal trade distorting effects.

The main contribution of the Uruguay Round Agreement on Agriculture (URAA) was to bring disciplines to bear on agricultural trade and domestic agricultural policies. In addition, future negotiations would be made easier as a result of the simplification of market access restrictions and the categorising of domestic support. A side effect of that contribution was to make regional and bilateral trade agreement easier to negotiate. Conflicts over the opening up of markets to imports were not themselves resolved, but the fact that tariffs had replaced non-tariff trade barriers made the negotiation of a schedule of preferential reductions more straightforward. Even the TRQs became useful, as they provided a way of granting preferences to partner exporters without necessarily increasing the level of imports. Thus the potential rents accruing to suppliers of goods within the TRQ could be used as an inducement to joining an RTA or negotiating a BTA.

Two issues persist in the discussions about the relationship between the treatment of agriculture in regional and bilateral trade agreements and that in WTO. One is the extent to which adherence to Article XXIV of the GATT obliges countries to include agricultural trade in the free-trade provisions. If countries contemplating a regional or bilateral agreement can reasonably argue that agricultural trade is an insignificant part of their trade relations then there would be no compelling motive for including such products in the free-trade arrangements. So far, there has been no definitive ruling from a panel on the question of defining 'substantially all trade'. Clearly, if agricultural trade between two (or more) countries is small because of high trade barriers, the use of current trade flows is circular: agriculture could be left out of the agreement because it is highly protected. So RTAs and BTAs would be denied some benefits from opening up trade flows in farm products. The use of tariff lines, or other such measures, would be much more likely to obligate countries to include agriculture among the sectors for tariff-free trade.

The second issue is the extent to which one can include disciplines on domestic farm subsidies in regional and bilateral agreements. It is often assumed that the conduct of domestic policy is outside the realm of the FTAs, but this is not always the case. The movement towards 'decoupled' policies, encouraged by the URAA, has the advantage of making it easier to have free trade in a commodity and still maintain domestic support policies. Nevertheless, the existence of an active domestic support policy, involving subsidies and market management, complicates the negotiation of free trade in those products.

The issues are clearly connected. If one can omit agricultural trade from the FTA provisions then the question of domestic support does not arise. Conversely, if one cannot exclude agriculture without violating WTO provisions, then the potentially problematic issue of domestic support is unavoidable.

Allied to the issue of the application through RTAs and BTAs of disciplines on domestic support is that of the treatment of export subsidies. Various trade

agreements have tried to include provisions that countries may not use export subsidies in mutual trade. This sounds like a logical provision. However, in practice it is not easy to ban subsidies paid on internal trade without creating an incentive to import from outside and a disincentive to export within the free-trade area. So in effect export subsidies have also to be controlled at the WTO level.

The current Doha Round of WTO talks would, if successfully completed, make a significant difference to the ease at which agricultural trade could be opened up within RTAs and BTAs. Tariff levels would come down by at least 50 per cent and TRQs for sensitive commodities would be expanded. This reduces the degree of preference for partner suppliers (and hence the risk of trade diversion) but it also reduces the shock of adjustment for import-competing sectors. With an agreed schedule of WTO tariff reductions, the marginal impact of faster reductions for regional or bilateral partners may be more tolerable. Additionally, export subsidies would finally be eliminated, a step that RTAs and BTAs have found difficult to accomplish. But the main contribution that the WTO negotiations on agriculture can make to the process of regional and bilateral trade liberalisation could be to further push countries to abandon price supports in domestic markets and embrace direct payments for public goods or for income relief. Such policies will be more compatible with preferential trade agreements as well as good for multilateral trade arrangements.

With WTO talks on agriculture grinding slowly, regional negotiations may, however, take the brunt of attempts to further liberalise agricultural trade and to gain access to new markets for agricultural exports. Thus in agriculture there is a strong degree of complementarity in trade negotiations. Plurilateral talks can erode market access barriers but set up trade flows encouraged by discrimination among suppliers. Multilateral talks can reduce the scope for such trade diversion. The multilateral process can handle subsidy reduction, which in turn makes it easier for countries to agree to opening up regional or bilateral trade. This complementarity, however, depends on progress at the multilateral level. Currently that is the stumbling block.

V. Prospects for the future

What would one expect to see in the future? One possibility is the emergence of more bilaterals with the US, including significant trading countries such as Malaysia and Thailand, and large trading powers such as Japan. This would certainly be accompanied by trade agreements between the EU and these countries. The EU could be content with bilaterals that were less geared to exports of agricultural products. But Asian integration could overshadow such large trade deals. A trade agreement between ASEAN and China would certainly have to include agricultural trade. If India and China were to sign a trade agreement, it would be difficult to imagine that it would not also include provisions for expanded agricultural trade.

It is also possible, particularly if the WTO Doha Round is further postponed, that there could be a networking of existing trade agreements. A new type of regionalism emerged in the mid-1990s as attempts were made to transform existing free-trade networks into actual or potential supra-regional trade agreements that span the continents. This new breed of supra-regional network agreements included both the Asia-Pacific Economic Cooperation forum (APEC) and the Free Trade Area of the Americas (FTAA). These two agreements were different from traditional regional trade blocs, as well as from each other. APEC and the FTAA have overlapping membership (several countries participate in both) and hence tend to join rather than isolate continents. The fact that a country can be a member of more than one such agreement is the key in this regard. This property makes these regional pacts more like networks than closed blocs. In this way they can build on current agreements (FTAA, which builds upon NAFTA and the ALADI agreements) or be neutral toward them (APEC, which includes members of ASEAN, the ANZCERTA, MERCOSUR and NAFTA, as well as countries that belong to no bloc, such as Japan). Even though they differ in certain crucial ways, in particular in their treatment of trade with third countries, both these supra-regional networks represent essentially new ways of negotiating reductions in trade barriers. They would certainly have to include provisions for freer trade in agricultural products.

Not long after the agreement on NAFTA, discussions began on a broader initiative to expand US economic relations with other Latin-American countries. This led ultimately to the declaration at Miami in 1994 of the intention to work toward an FTAA by 2005. There have been sporadic negotiations on the establishment of an FTAA covering thirty-four countries in the hemisphere since 1996. The development of the FTAA slowed at the end of the last decade as Brazil chose to strengthen its economic ties with South American countries before negotiating with the NAFTA countries. At the Miami summit of 2003 the scope for the FTAA was significantly revised. Sensitive issues such as domestic farm support and anti-dumping actions were by agreement left to the WTO. As a consequence, the extent to which the FTAA retains its appeal for the countries in the region may depend on whether a successful Doha Round can be concluded.

At present, talks about these free-trade networks do include agricultural trade. The FTAA, which is intended to consolidate the regional pacts in the Americas, is scheduled to include agricultural products and thus lead toward a single market in the hemisphere. A separate negotiating group on agricultural trade has been set up as part of the FTAA process to guide this process. For countries such as Argentina and Brazil, inclusion of agriculture is imperative. Canada, as a proponent of the FTAA, will be confronted with the need to include agriculture despite the domestic sensitivity in some sectors.

If such an agreement were to be concluded, improved market access for agricultural products, both in US exports to Latin America and their exports to the US, would have to be included. This could have a very significant impact on markets

even if domestic policy were not regulated in the FTAA.[42] The pressure for an FTAA may come from a fear of being excluded from emerging markets while competitors get free access. It is likely that the EU will soon conclude an agreement with MERCOSUR that would include preferential access for farm products (although this would be quota controlled for some years). This would put US exporters at a disadvantage in both the EU and the Latin American markets if an FTAA did not materialise. So an FTAA (and possibly even a strengthened transatlantic trade agreement) may be necessary for the export prospects of several sectors of US agriculture.

42 Mexico and Chile have already signed a number of bilateral (and trilateral) trade agreements with other countries in the region.

8

Services

FEDERICO ORTINO

I. Introduction

The services sector accounts today for two-thirds of global output (65% of GDP in 2004; 45% of GDP in 1960) and represents the fastest growing sector of the global economy. In a world where competitiveness is key to economic development, services play a vital role in ensuring a competitive economy. Service industries provide the infrastructure allowing modern economies to function by linking geographically dispersed economic activities or supplying crucial inputs into products competing in the domestic and global markets.

However, the share of services in global trade has been relatively low as certain characteristics of services, such as intangibility and non-storability, affect their tradability.[1] Recent advances in information technology have nonetheless made trade in certain services now feasible or have greatly reduced its costs. Since 2000 trade in commercial services (including in particular transport, travel, communications, financial, professional services) has risen on average by 11 per cent per year[2] with the share of global export from a few developing countries steadily increasing (China, India, Hong Kong and Singapore are among the top fifteen exporters of services).[3] The growing internationalisation of services also presents certain challenges for developing countries in particular. For example, these include the need to undertake necessary investments in modern IT networks, adapt educational systems to the information age, and design appropriate domestic and regional regulatory structures for service sectors.[4]

In recent years the number of international agreements purporting to liberalise and promote trade in services has increased dramatically. While the General Agreement on Trade in Services (GATS), negotiated as part of the Uruguay Round in the late 1980s/early 1990s, has represented the pioneer – and often the model – in

1 Bernard Hoekman and Aaditya Mattoo, 'International Trade: Trade in Services', in Andrew T. Guzman and Alan O. Sykes (eds.), *Research Handbook in International Economic Law* (Cheltenham: Edward Elgar, 2007), at p. 115.

2 Services account today for 19% of global trade.

3 WTO, *International Trade Statistics 2006* (Geneva: WTO, 2006).

4 See Dominique Njinkeu and Bruno Powo Fosso, 'Intra-African Trade and Regional Integration', 11 November 2006 (copy with author); and UNCTAD, 'Trade in Services and Development Implications', Note by the UNCTAD secretariat, TD/B/COM.1/85 (2 February 2007).

the field,[5] much of the recent and current international treaty making addressing trade in services (as well as trade in goods and foreign investment) has occurred at the regional and bilateral levels.[6] The outlook stemming out of this almost frenetic treaty-making activity is a complex and multilayered network of international rules regulating the transnational movement of services and service providers in essential sectors such as the financial, telecommunication, business and professional sectors.

It should be emphasised at this stage that, international trade rule-making does not always go hand in hand with actual, immediate liberalisation of trade. As has been the case for trade in goods, trade rules function as the underlying framework against which effective liberalisation can gradually occur. This is also true for trade in services. However, as it will be discussed in the following sections, a slightly different approach has been adopted in the area of trade in services given the different types of trade barriers restricting the flow of services compared with those restricting trade in goods.

This chapter is divided in two main parts. Section II describes the basic features of the GATS focusing in particular on the following issues: (a) scope of application, (b) general obligations and disciplines, (c) specific commitments, and (d) sectoral disciplines. Focusing broadly on these same issues, section III will analyse the services chapters of the Regional Trade Agreements (RTAs) that have been notified to the WTO Council for Trade in Services on the basis of Article V of the GATS.[7] This chapter does not address the issue of the level of liberalisation that these RTAs have actually accomplished[8] or the issue of the compatibility of these agreements with GATS.[9]

II. Trade in Services and the GATS

The GATS represents one of the innovative features of the WTO 'single undertaking' stemming out of the Uruguay Round as it provides for the first multilateral, legally

5 Earlier attempts to provide rules for trade in services are the Codes and Declaration concluded within the Organization for Economic Cooperation and Development (OECD) in the 1970s and 1980s. Cf. Philip M. Raworth, *Trade in Services: Global Regulation and the Impact on Key Service Sectors* (New York: Oceana Publications, 2005), Chapter III.

6 For a recent account of this development see Jo-Ann Crawford and Roberto V. Fiorentino, 'The Changing Landscape of Regional Trade Agreements', WTO Discussion Paper No. 8 (2005).

7 There are a total of forty-six notifications from 1 January 1995 until 31 December 2006. See WTO Document at www.wto.org/english/tratop_e/region_e/summary_e.xls. Section III will principally focus on free trade agreements and economic co-operation agreements leaving aside a detailed analysis of custom unions (such as the European Treaty).

8 For a recent analysis of the liberalisation impact of RTAs beyond the GATS, see Martin Roy, Juan A. Marchetti and Aik Hoe Lim, 'Services Liberalization in the New Generation of Preferential Trade Agreements (PTAs): How Much Further than the GATS?', WTO Staff Working Paper No. ERSD–2006–07 (September 2006).

9 For a recent analysis of the compatibility of RTAs (and bilateral investment treaties) with GATS, see Federico Ortino and Audley Sheppard, 'International Agreements Covering Foreign Investment in Services: Patterns and Linkages', in Lorand Bartels and Federico Ortino, *Regional Trade Agreements and the WTO Legal System* (Oxford: Oxford University Press, 2006), pp. 201–14.

enforceable disciplines covering international trade (and investment) in services. The GATS architecture is composed of a three-layered structure: (1) a framework Agreement; (2) eight Annexes addressing sector-specific issues; and (3) individual Members' Schedules of Specific Commitments.

As the GATS is usually employed as a possible model or starting point for regional agreement regulating trade in services, it is worthwhile to set out a few basic features.

A. Scope of application

GATS rules apply to 'measures by Members affecting trade in services' (Article I:1). A 'measure' is defined very broadly in the GATS to embrace any action by a Member in any form such as a law, regulation, rule, procedure, decision, administrative action (Article XXVIII(a)). In theory, 'measures by Members' means measures taken by central, regional or local governments and authorities as well as non-governmental bodies in the exercise of powers delegated by central, regional or local governments or authorities.[10] However, GATS only requires Members to take such reasonable measures as may be available to them to secure compliance with GATS rules by sub-central and non-governmental bodies (Article I.3(a)).[11]

'Measures by Members affecting trade in services' include measures in respect of (i) the purchase, payment or use of a service; (ii) the access to and use of, in connection with the supply of a service, services which are required by those Members to be offered to the public generally; (iii) the presence, including commercial presence, of persons of a Member for the supply of a service in the territory of another Member (Article XXVIII(c)). This list being indicative, the inquiry centres around the term 'affecting'. WTO jurisprudence has interpreted broadly the term 'affecting'. A measure affects trade in service when the measure 'modifies the conditions of competition in supply of a service'.[12] In other words, GATS disciplines apply, in principle, to any measure of a Member to the extent it affects the supply of a service, regardless of whether such measure directly governs

10 On the related issue of attribution for non-mandatory governmental measures as well as for government-endorsed or authorised private measures, see Sharif Bhuiyan, 'Mandatory and Discretionary Legislation: The Continued Relevance of the Distinction under the WTO' (2002) 5(3) *Journal of International Economic Law* 571–604.

11 If this limitation is read in conjunction with Article 22.9 of the DSU, it may be argued that, while the implementation obligations of the responsible Member are limited to such reasonable measures as may be available to it to ensure observance of WTO law, the dispute settlement provisions relating to compensation and the suspension of obligations do apply where the Member concerned has not been able to secure the observance of the WTO Agreement in its territory. In any event, the limitation found in Article I.3(a) of the GATS is a specific and limited exception to the principle that subjects of international law are responsible for the activities of all branches of power within their system of governance, including all regional levels or other subdivisions of government and thus should not be generalised and extrapolated to other authorities of a Member enjoying a degree of independence.

12 See Panel Report, *EC–Bananas III*, para. 7.281; and Appellate Body Report, *EC–Bananas III*, para. 220. See also GATT Panel Report, *Italy–Agricultural Machinery*.

the supply of a service, or whether it regulates other matters but nevertheless affects indirectly trade in services.[13] Furthermore, in line with GATT/WTO jurisprudence, in order to determine whether a measure 'affects' trade in services, there is no need to determine actual effects, rather it is enough to demonstrate a potential effect on trade.[14] Accordingly, in determining the coverage of the GATS, it is sufficient to show that a governmental measure has the potential to affect (i.e., to have an effect on) trade in service.[15]

'Trade in services' is defined as the supply of a service (a) from the territory of one Member into the territory of any other Member (cross-border supply); (b) in the territory of one Member to the service consumer of any other Member (consumption abroad); (c) by a service supplier of one Member, through commercial presence in the territory of any other Member (commercial presence); and (d) by a service supplier of one Member, through presence of natural persons of a Member in the territory of any other Members (temporary presence of natural persons) (Article I.2).

'Natural persons of another Member' (whether for purpose of modes 2 or 4) means a natural person who resides in the territory of that other Member or any other Member and who under the law of that other Member is a national of that other Member or has the right of permanent residence in that other Member (if the Member in which he/she resides accords substantially the same treatment to permanent residents as it does to its own citizens) (Article XXVIII(k)). 'Juridical person of another Member' (whether for purpose of modes 2 or 3) means a juridical person which is either (i) constituted under the law of that other Member and is engaged in substantial business operations in the territory of that Member or any other Member, or (ii) in the case of the supply of a service through commercial presence, owned or controlled by natural persons of that Member or juridical persons of that other Member identified under subparagraph (i) (where 'ownership' is defined as a holding of more than 50 per cent of the person's equity interest and 'control' is defined as the power to name a majority of the person's directors or otherwise to legally direct its actions) (Article XXVIII(m) and (n)).

13 Werner Zdouc, 'WTO Dispute Settlement Practice Relating to the GATS', in Federico Ortino and Ernst-Ulrich Petersmann (eds.), *WTO Dispute Settlement System 1995–2003* (The Hague: Kluwer Law International, 2004), Chapter 21. Cf. Aaditya Mattoo, 'MFN and the GATS', in Thomas Cottier, Petros C. Mavroidis and Patrick Blatter (eds.), *Regulatory Barriers and the Principle of Non-Discrimination in World Trade Law* (Ann Arbor: University of Michigan Press, 2000), at p. 53.

14 Panel Report, *Canada–Automotive Industry*, paras. 10.80 and 10.84. See GATT Panel Report, *Italy–Agricultural Machinery*, para. 12: 'The selection of the words "affecting" would imply, in the opinion of the Panel, that the drafters of the Article intended to cover [. . .] any laws or regulations which *might* adversely *modify the conditions of competition* between [like products]' [emphasis added].

15 In *US–Gambling Services*, however, the Panel and Appellate Body clarified that invoking a total prohibition is not enough for a complaining Member to prevail unless that Member does not also identify the specific measure(s) that is the source of the alleged prohibition. See Appellate Body Report, *US–Gambling Services*, paras. 120–6.

'Commercial presence' is broadly defined as any type of business or professional establishment, including through (i) the constitution, acquisition or maintenance of a juridical person, or (ii) the creation or maintenance of a branch or a representative office within the territory of a Member for the purpose of supplying s service (Article XXVIII(d)).

As specified in the 'Annex on Movement of Natural Persons Supplying Services under the Agreement', the Agreement shall not apply to measures affecting natural persons seeking access to the employment market of a Member, nor shall it apply to measures regarding citizenship, residence or employment on a permanent basis (paragraph 2).

The GATS covers all services except those supplied in the exercise of governmental authority, that is any service which is provided on a non-commercial (non-profit) and non-competitive basis (Article I.3(b) and (c)). In order for a service to be excluded from the scope of application of the GATS both conditions must be met. Although there exists some uncertainty with regard to the cumulative requirements of non-profitability and non-competitiveness, it appears that the nature of the service itself or the characteristics of the service supplier are irrelevant for purposes of deciding the scope of the 'services supplied in the exercise of governmental authority' exception. Accordingly, one can conclude that apart from a limited set of governmental services (such as the police and military), the notion of 'services' in the GATS applies to all services.[16]

B. General obligations and disciplines

Part II of the GATS provides for certain general obligations, in particular the 'most-favoured-nation (MFN) treatment' (Article II), 'transparency' (Article III), 'domestic regulation' (Article VI), and 'recognition' (VII) as well as exceptions such as 'economic integration' (Article V), 'restrictions to safeguard the balance of payments' (Article XII), 'general exceptions' (Article XIV), and 'security exceptions' (Article XIV *bis*).

The scope of application of these *general* provisions may however be limited in two alternative ways.[17] First, each provision may apply only to *specific service sectors or sub-sectors* (usually listed in a Member's schedule of specific commitments).[18] These provisions may be referred to as 'sector-specific conditional

16 Markus Krajewski, *National Regulation and Trade Liberalization in Services: The Legal Impact of the General Agreement on Trade in Services (GATS) on National Regulatory Autonomy* (The Hague: Kluwer Law International, 2003), at p. 73. Cf. Eric H. Leroux, 'What is a ''Service Supplied in the Exercise of Governmental Authority'' Under Article I:3(b) and (c) of the General Agreement on Trade in Services?' (2006) 40(3) *Journal of World Trade* 345–86, at 348.

17 Those provisions that employ both limitations concurrently are referred to as 'specific commitments' and are analysed in the following section.

18 As described in the following section, this follows a 'positive-list' approach, as only sectors that parties have expressly identified are subject to these provisions.

obligations'.[19] On the other hand, if these provisions apply regardless of the existence of specific commitments, they are referred to as 'sector-specific unconditional obligations'.[20] In several cases, the same GATS article contains both sector-specific unconditional and conditional obligations.

Alternatively, the scope of application of these provisions may be limited by allowing each Member to exclude *specific measures* from the reach of the provision (usually by listing the non-conforming measures in an annex to the Agreement).[21] These provisions may be referred to as 'measure-specific conditional obligations'. The MFN provision is the only general obligation of this kind in the GATS as it permits WTO Members to maintain measures inconsistent with the MFN principle provided that such measures are listed in the Annex on Article II Exemptions.[22]

Part II of the GATS also includes four provisions mandating further negotiations relating to aspects on which the negotiators of the Uruguay Round could not reach consensus: further disciplines on domestic regulation (Article VI:4), emergency safeguard measures (Article X:1); government procurement (Article XIII:2); and subsidies (Article XV:1). With one small exception,[23] these negotiations have not produced any substantive outcome.

1. Most-favoured-nation treatment

The principal purpose of the MFN provision in GATS is to ensure equality of opportunity for services and service suppliers from all WTO Members.[24] The MFN provision sets out a three-part test of consistency: (a) whether the measure at issue is a 'measure covered' by the GATS;[25] (b) whether the services or service suppliers concerned are 'like' services or service suppliers;[26] and (c) whether the Member

19 See, e.g., the 'administrative due process requirements' in GATS Article VI:1.

20 See, e.g., the MFN obligation in GATS Article II:1 and the Transparency obligation in GATS Article III:1.

21 This follows a 'negative-list' approach, as only the measures listed in the annex are exempted from the scope of application of the relevant provision.

22 No new exemptions can be added unless recourse has been made to the waiver provisions of the WTO Agreement. Moreover, the MFN exemptions are in principle valid for a period of 10 years from the entry into force of GATS. See Mitsuo Matsushita, Thomas J. Schoenbaum and Petros C. Mavroidis, *The World Trade Organization: Law, Practice and Policy* (Oxford: Oxford University Press, 2004), at p. 240.

23 See the Accountancy Disciplines developed within the Article VI:4 mandate on domestic regulation.

24 Peter Van den Bossche, *The Law and Policy of the World Trade Organization: Text, Cases and Materials* (Cambridge: Cambridge University Press, 2005), at p. 319.

25 See the discussion above regarding the scope of application of the GATS.

26 The GATS does not contain a definition of the term 'like' service providers. The issue of likeness under GATS Article II has only been addressed twice in GATS/WTO jurisprudence, albeit very briefly. In *EC–Bananas III* and *Canada–Automotive Industry*, the relevant statement by both Panels was that 'to the extent that entities provide like services, they are like service suppliers'. See Panel Report, *EC–Bananas III*, para. 7.322, and Panel Report, *Canada–Automotive Industry*, para. 10.248. Looking at the extensive jurisprudence on the issue of the likeness of products under GATT (Appellate Body Report, *EC–Asbestos*, para. 101), it may be said that the likeness test in the GATS should be based *inter alia* on the following factors: (a) service's end-uses in a given market; (b) consumer habits and preferences regarding the service or the service supplier; (c) characteristics of the service or the service supplier; and (d) classification and

accords 'less favourable treatment' to the services or service suppliers of another Member (the MFN obligation in GATS thus extends also to the treatment afforded to services and service providers of non-WTO Members).[27]

2. Transparency

Article III of the GATS provides for certain transparency requirements with regard to 'all relevant measures of general application which pertain to or affect the operation of this Agreement'. First, Members shall publish promptly and at the latest by the time of their entry into force all relevant measures. However, this publication requirement does not arise when publication is 'not practicable' (although even in this case, the information shall nevertheless be made 'publicly available'). Despite the vagueness implicit in the criterion of 'practicability', this provision arguably allows WTO Members lacking the financial resources to publish all measures of relevant application the flexibility to avoid having to incur the full costs of publication (including the wide dissemination of certain material). With regard to the meaning of 'measures of general application', the Panel and Appellate Body in *US–Cotton Underwear* have noted (within the context of a similar provision in Article X of the GATT) that they are meant to encompass those measures that affect 'an unidentified number of economic operators'.[28]

Second, Members shall inform (at least annually) the Council for Trade in Services of the introduction of new, or any changes to existing laws, regulations or administrative guidelines which significantly affect trade in services covered by specific commitments (Article III:3). Moreover, Article III:4 requires Members to establish enquiry points to facilitate transparency, with each enquiry point providing information to other Members in response to requests for specific information or in connection with information that is to be provided pursuant to the notification provisions.

Certain notification requirements are imposed on Members for the benefit of private parties. Article VI:3 of the GATS provides that 'where authorization is

description of the service in the UN CPC system. Cf. Aaditya Mattoo, 'National Treatment in the GATS: Corner-stone or Pandora's Box?' (1997) 31(1) *Journal of World Trade* 107–35, at 128; Zdouc, above n. 13, at pp. 394–401; Van den Bossche, above n. 24, at pp. 323–4.

27 In *EC–Bananas III*, the Appellate Body took the view that 'treatment no less favourable' in Article II:1 of the GATS should be taken to include both *de jure* and *de facto* discrimination (see Appellate Body Report, *EC–Bananas III*, paras. 231–4). Furthermore, from the early GATT practice, the phrase 'no less favourable' has been described as an expression of the underlying principle of *effective* equality of treatment between different foreign products. Accordingly, a measure affords less favourable treatment if it adversely modifies the conditions of competition between imports from two different countries. See GATT Panel Report, *Italy–Agricultural Machinery*, paras. 11–12, and GATT Panel Report, *US–Section 337 Tariff Act*, para. 5.10.

28 See Panel Report, *US–Cotton Underwear*, para. 7.65, and Appellate Body Report, *US–Cotton Underwear*, p. 21.

required for the supply of a service [. . .], the competent authorities of a Member shall [. . .] inform the applicant of the decision concerning the application'.

Transparency requirements are not applicable to confidential information, the disclosure of which 'would impede law enforcement, or otherwise be contrary to the public interest, or which would prejudice legitimate commercial interests of particular enterprises, public or private' (Article III*bis*). The component of this exception allowing confidentiality on grounds of public interest raises issues of definition; for, it is possible to argue that, without qualification, an exception to transparency on the basis of public interest could give a WTO Member a wide margin of discretion, and reduce considerably the scope of the transparency provisions.

3. Domestic regulation and recognition

Article VI of the GATS sets out certain good governance (or administrative due process) standards in particular a duty to 'ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner' (Article VI:1) and a duty to 'maintain or institute as soon as practicable judicial, arbitral or administrative tribunals, or procedures which provide, at the request of an affected service supplier, for the prompt review of, and where justified, appropriate remedies for, administrative decisions affecting trade in services' (Article VI:2).[29]

The GATS provides for a normative mandate to the Council for Trade in Services to develop, through subsidiary bodies, any disciplines on domestic regulation in order to ensure 'that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services'. Furthermore, these disciplines shall aim to ensure that such regulations are, *inter alia*, '(a) based on objective and transparent criteria, such as competence and the ability to supply the service; (b) not more burdensome than necessary to ensure the quality of the service; (c) in the case of licensing procedures, not in themselves a restriction on the supply of the service' (Article VI:4). Although this provision has so far only been applied once with regard to the accountancy sector,[30] it evidences that liberalisation of trade in services, even more than in the case of goods, requires the adoption of *ad hoc* approaches with regard to specific service sectors, in particular when one moves from more shallow to deeper forms of economic integration.[31]

29 For a recent attempt to distinguish between 'substance' and 'administration' of a given measure (within the context of GATT Article X), see Appellate Body Report, *EC–Customs Matters*.

30 WTO, 'Disciplines on Domestic Regulation in the Accountancy Sector', Adopted by the Council for Trade in Services on 14 December 1998, WTO Doc. No. S/L/64 (17 December 1998).

31 Cf. the work carried out within the WTO first by the Working Party on Professional Services (S/WPPS) and currently by the Working Party on Domestic Regulation (S/WPDR). For a recent summary of the current work of the WPDR, see the consolidated working paper prepared by the Chairman of the WPDR in July 2006, JOB(06)/225.

The GATS also envisages the possibility for a Member to recognise the education or experience obtained, requirement met, or licenses or certification granted in a particular country for purposes of the fulfilment of its standards or criteria for the authorisation, licensing or certification of services suppliers. Such recognition may be based upon an agreement or arrangement with the country concerned or may be accorded autonomously (Article VII:1). Such recognition shall not constitute a means of discrimination between countries or a disguised restriction on trade in services (Article VII:3). Wherever appropriate, recognition should be based on multilaterally agreed criteria and Members shall work in co-operation with relevant intergovernmental and non-governmental organisations towards the establishment and adoption of common international standards and criteria for recognition and common international standards for the practice of relevant services trades and professions (Article VII:5).

From the above, three issues seem to be emerging as central in the development of future disciplines on domestic regulation affecting trade in services: necessity test, international standards and recognition of equivalence.[32]

4. Exceptions

There are several provisions in the GATS setting out exceptions to GATS obligations including an Economic Integration exception (Article V), a Balance of Payments exception (Article XII), a General Exception (Article XIV), and a Security Exception (Article XIV/*bis*).

C. Specific commitments

Contrary to the general obligations analysed in the previous section, Part III of the GATS provides for a further set of obligations, which are however dependent on the level of commitments undertaken by each Member. These obligations are in particular the market access (Article XVI) and national treatment (Article XVII) obligations. Accordingly, the market access and national treatment obligations do not apply generally to all measures affecting trade in services, but only come into play if Members choose to commit service sectors or sub-sectors in their Schedules of Specific Commitments. In other words, with regard to market access and national treatment, GATS follows the so called 'positive list' approach, whereby market access and national treatment obligations extend only to those *service sectors* that Members have actually (i.e., positively) inscribed in their individual schedules of commitments (service-specific limitation). However, even in those sectors or sub-sectors that Members have inscribed in their schedules, Members are allowed to reserve the right to maintain or adopt *measures* inconsistent with the market access and national treatment obligations (measure-specific limitation). This is done by

32 See Markus Krajewski, 'Services Liberalization in Regional Trade Agreements: Lessons for GATS "Unfinished Business"?', in Bartels and Ortino, above n. 9, pp. 175–200, at p. 180.

specifying in their schedules any conditions on their market access and national treatment commitments.[33] Accordingly, it is more correct to describe the GATS approach as a 'positive/negative list' or hybrid approach.[34]

As mentioned above, the difference between the general provisions in Part II and the specific commitments in Part III is apparently in their scope of application: while general provisions may be limited by *either* sector-specific limitations *or* service-specific limitations, the latter provisions may be limited by *both* limitations.

1. Market access

With regard to the market access provision, Article XVI:2(a)–(f) identifies, in an apparently exhaustive manner, a number of measures (mostly of a quantitative nature), which Members should not maintain or adopt in the sectors where specific commitments have been undertaken, unless otherwise specified.[35]

In *US–Gambling Services*, the Panel and Appellate Body have given a seemingly broad reading to the market access limitations listed in Article XVI, which would include any measure having an *effect similar* to that of any market access limitations listed in Article XVI:2, regardless of form.[36]

2. National treatment

Article XVII requires each Member to 'accord to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers' (Article XVII:1). Subject to each Member's specific commitments, Article XVII of the GATS sets out a three-tier test of consistency, which requires the examination of whether (1) the measure at issue affects trade in services; (2) the foreign and domestic services

33 A WTO Member may choose to describe either how trade in services is restricted ('No limitation, except . . .') or what types of services transactions are allowed in a listed sector ('Unbound, except . . .').

34 Some commentators have referred to as the 'hybrid' approach because the fixing of the level of openness involves elements of both negative and positive listings. See Carsten Fink and Martin Molinuevo, 'East Asian Free Trade Agreements in Services: Roaring Tigers or Timid Pandas?', The World Bank: Trade Issues in East Asia, Liberalization of Trade in Services (June 2007).

35 GATS Article XVI:2 reads in part as follows: 'In sectors where market-access commitments are undertaken, the measures which a Member shall not maintain or adopt either on the basis of a regional subdivision or on the basis of its entire territory, unless otherwise specified in its Schedule, are defined as: (a) limitations on the number of service suppliers whether in the form of numerical quotas, monopolies, exclusive service suppliers or the requirements of an economic needs test; [. . .]'.

36 The Panel found, and the Appellate Body upheld, that the US ban is: (1) a limitation on the number of service suppliers in the form of numerical quotas within the meaning of Article XVI:2(a) 'because it *totally prevents* the use by service suppliers of one, several or all means of delivery that are included in mode 1' and (2) a limitation on the total number of service operations or on the total quantity of service output in the form of quotas within the meaning of Article XVI:2(c) 'because it . . . *results* in a ''zero quota'' on one or more or all means of delivery include[d] in mode 1'. Panel Report, *US–Gambling Services*, paras. 6.338 and 6.355; Appellate Body Report, *US–Gambling Services*, paras. 239 and 252. For a critique of this decision see Federico Ortino, 'Treaty Interpretation and the WTO Appellate Body Report in US–Gambling: A Critique' (2006) 9(1) *Journal of International Economic Law* 117–48.

and service suppliers are 'like' services or service suppliers;[37] and (3) the foreign services or service suppliers are granted treatment no less favourable.[38]

Article XVII specifies further the content of the national treatment clause: 'A Member may meet the requirement of paragraph 1 by according to services and service suppliers of any other Member, either formally identical treatment or formally different treatment to that it accords to its own like services and service suppliers' (Article XVII:2). 'Formally identical or formally different treatment shall be considered to be less favourable if it modifies the conditions of competition in favour of services or service suppliers of the Member compared to like services or service suppliers of any other Member' (Article XVII:3).[39]

3. Additional commitments: Reference paper on basic telecommunications

Members may negotiate commitments with respect to measures affecting trade in services not subject to scheduling under Articles XVI or XVII, including those regarding qualifications, standards or licensing matters (Article XVIII). The Reference Paper on regulatory principles in basic telecommunications, the result of post-Uruguay Round negotiations on telecommunications, is an example of an 'additional commitment'. Building on Articles VIII and IX of the GATS, the Reference Paper is aimed to strengthen competition disciplines in the area, in particular to ensure that the market power of a former public monopoly service provider is not used to the detriment of new market entrants.

D. Sectoral disciplines

As mentioned above, next to the framework agreement (with its general and specific provisions), the GATS system also provides for several annexes addressing

37 It is recognised that the notion of 'likeness' in the context of GATS Article XVII (as in other contexts) contains a number of interpretative uncertainties, including the relationship between 'like service' and 'like service suppliers' as well as the relationship between different 'modes of supply'. Cf. Krajewski, above n. 16, at pp. 97–107; Zdouc, above n. 13, at pp. 394–5.

38 Cf. Van den Bossche, above n. 24, at p. 367, and Zdouc, above n. 13, at pp. 403–16.

39 The wordings of these two paragraphs draw heavily on the reasoning of two well-known GATT panel reports: *US–Section 337 Tariff Act* and *Italy–Agricultural Machinery*, respectively. Both panels addressed claims under GATT Article III:4, which include a prohibition against discriminatory non-fiscal regulation very similar to GATS Article XVII:1. In line with the GATT/WTO jurisprudence on GATT Article III, the *EC–Bananas III* Panel Report application of the 'less favourable treatment' test in GATS Article XVII rested on the determination of *adverse effects* of the national measure under review *predominantly* on foreign service suppliers. Focusing on the combined effect of the structural features of the regulation under review (differentiating distributors according to their past marketing records) and the actual market shares of service suppliers of EC and non-EC origin (most of the suppliers of Complainants' origin were classified in Category A, while most of the suppliers of EC origin were classified in Category B), the Panel found that the EC regulation operated in such a way as to modify the conditions of competition to the detriment of foreign (non-EC) service suppliers. Panel Report, *EC–Bananas III*, para. 7.335. See also Appellate Body Report, *EC–Bananas III*, paras. 239–40.

sector-specific issues[40] as well as an Understanding on Commitments in Financial Services. These additional sectoral agreements have different functions: to limit the scope of the GATS (e.g., to exclude air transport services), to set out rules and timetable for further negotiations in certain sectors (e.g., maritime transport services and basic telecommunications), or to provide for additional rules and disciplines for certain sectors (e.g., telecommunications, financial services).

While it is not possible here to examine in detail these sectoral agreements, it should be emphasised at least that with regard to the latter function (to provide for additional disciplines) a few of these agreements do go well beyond the provisions set out in the framework agreement. Particularly, those instruments dealing with telecommunication and financial services provide for a set of rules and disciplines that go well beyond those provided in the framework agreement. These additional disciplines may either go beyond the framework agreement in terms of further trade liberalisation or in terms of granting Members more leeway to restrict trade. For example, the 'Understanding on Commitments in Financial Services' and the 'Annex on Financial Services' provide for additional rules dealing with monopoly rights, government procurement, commercial presence and non-discriminatory measures that may be categorised as pro-liberalisation measures as well as additional rules dealing with domestic regulation granting Members the prerogative to take measures for prudential reasons (the so called 'prudential carve-out' in the Annex on Financial Services).

III. Services in Regional Trade Agreements

Since 1995 a total of forty-six economic integration agreements (involving eighty-four countries)[41] have been notified to the Council of Trade in Services pursuant to Article V of the GATS.[42] This section, which is the core of the chapter, addresses certain key issues in the services chapters of RTAs.

A. Scope of application

The first issue to be considered is that of the scope of application of the services chapter in RTAs. This section will be broken down according to the following sub-issues: 'mode of supply', 'bodies', 'beneficiaries', 'excluded categories of services', and 'excluded government activities'.

40 See, e.g., Annex on Movement of Natural Persons Supplying Services under the Agreement, Annex on Air Transport Services, two Annexes on Financial Services, Annex on Negotiations on Maritime Transport Services, Annex on Telecommunications, Annex on Negotiations on Basic Telecommunications.

41 These include fifty-nine countries as members of the following organisations: European Union (EU), Mercado Común del Sur (MERCOSUR), Common Market for Eastern and Southern Africa (COMESA), European Free Trade Association (EFTA) and European Economic Area (EEA).

42 Among the countries with the highest share of these services RTAs are the US (8), Mexico (8), Singapore (7), Chile (6), Australia (5), New Zealand (4), EFTA (4), Korea (3), Japan (3).

1. Mode of supply

Regional trade agreements take principally two approaches with regard to the scope of application of the services chapter based on the mode of supply.[43] One approach follows the GATS *'trade in services' model* and extends the coverage of the services chapter to the four modes of supply defined in Article I of the GATS (cross-border trade; consumer abroad; commercial presence; movement of natural persons). For example, Article 3.1 of the EFTA–Korea Free Trade Agreement (on the scope and coverage of the chapter on trade in services) states that the chapter 'applies to measures affecting trade in services' and Article 3.3 (on definitions) incorporates into the FTA the definition of 'trade in services' provided for in Article I of the GATS.[44]

A second approach follows the North American Free Trade Agreement (NAFTA) *'cross-border trade in services' model* and extends the coverage of the services chapter to 'measures affecting cross-border trade in services', which includes modes 1, 2 and 4. The service chapter in these RTAs does not cover the provision of a service through FDI, which is usually instead covered by a specific chapter on investment. Article 1201 of the NAFTA provides that Chapter 12 on 'Cross-Border Trade in Services' applies to measures relating to cross-border trade in services where 'cross-border trade in services' is defined as the 'provision of a service (a) from the territory of a Party into the territory of another Party; (b) in the territory of a Party by a person of that Party to a person of another Party; or (c) by a national of a Party in the territory of another Party, but does not include the provision of a service in the territory of a Party by an investment, as defined in Article 1139 (Investment – Definitions), in that territory'.[45]

43 For a review of the regulation of 'investment' in RTAs see Chapter 9 in this volume.

44 See, e.g., EFTA–Korea FTA, ('Measures affecting trade in services' and GATS definition of 'trade in services'); Mexico–Nicaragua Free Trade Agreement, (GATS four modes of supply); European Union–Chile Association Agreement (EU–Chile AA), (GATS four modes of supply); Thailand–Australia Free Trade Agreement, (GATS four modes of supply); EFTA–Chile Free Trade Agreement (GATS four modes of supply); Singapore–Australia Free Trade Agreement, Articles 7.1 and 7.2; EFTA–Singapore Free Trade Agreement, Article 22; Singapore–Jordan Free Trade Agreement, Article 4.1; Japan–Singapore New-Age Economic Partnership Agreement (Japan–Singapore EPA), Articles 57–8; United States–Jordan Free Trade Agreement, (no chapter on investment); New Zealand–Singapore Closer Economic Partnership Agreement (NZ–Singapore CEPA), Articles 16–17; EFTA–Mexico Free Trade Agreement, (no real obligations for investment); Protocol of Montevideo for the Trade in Services of MERCOSUR, Article 2.2; and Caribbean Community and Common Market (CARICOM), (chapter on establishment and services overlapping).

45 See NAFTA, Article 1213, para. 2. See also United States–Bahrain Free Trade Agreement, 'Measures adopted or maintained by a Party affecting cross-border trade in services (modes 1, 2, 4, but not 3) by service suppliers of the other Party'; Central American–Dominican Republic–United States (CAFTA–DR–US), Article 11.1; United States–Morocco Free Trade Agreement, Article 11.1; Korea–Singapore Free Trade Agreement, Article 9.2; Japan–Mexico Economic Partnership Agreement (Japan–Mexico EPA), Articles 97.1 and 106; Australia–United States Free Trade Agreement (AUSFTA), Articles 10.1 and 10.14, but see exception in Article 10.3; Korea–Chile Free Trade Agreement, Articles 11.1 and 11.2; United States–Singapore Free Trade Agreement, Articles 8.1 and 8.2; United States–Chile Free Trade Agreement, Article 11.1; European Union–Mexico Free Trade Agreement, Chapter 10; and Canada–Chile Free Trade Agreement, Article H-01. However, in most of these FTAs, certain provisions in the service chapter do apply

The GATS 'trade in services' model may have two variants (in respect to the coverage of investment in services): one where the service chapter covers investment in services on an exclusive basis (whether or not the RTA includes a chapter on investment)[46] and one where both the service and investment chapters apply simultaneously to investment in services.[47]

2. Bodies

As in the GATS, a 'measure by a Party' is usually defined very broadly in RTAs to include measures taken by central, regional or (even local)[48] governments and authorities as well as non-governmental bodies in the exercise of powers delegated by central, regional or local governments or authorities.[49] However, contrary to the GATS, several RTAs do not contain the provision found in Article I.3(a) of the GATS that Members need only take such reasonable measures as may be available to them to secure compliance with GATS rules by sub-central and non-governmental bodies.[50] On the contrary, a few RTAs expressly provide for a stricter obligation to ensure the observance of all obligations and commitments by regional and local governments and authorities.[51]

3. Beneficiaries

As RTAs extend trade benefits to signatory parties only, they provide rules determining which 'service providers of the other party' are covered by the

to measures affecting investment in services (usually the obligations on Market Access; Domestic Regulation and Transparency) as in the US–Singapore FTA, Article 8.2.2.

46 EFTA–Korea FTA, Chapter on Investment, Article 2.2: this Chapter 'shall not apply provided that the sector concerned is covered by chapters on trade in services or financial services'; EFTA–Chile FTA, Article 32; EU–Chile AA, Article 130; and Thailand–Australia FTA, Article 903: 'This Article applies to measures adopted or maintained by a Party relating to: direct investments of investors of the other Party; and investors of the other Party, unless the measure is a measure by that Party affecting trade in services'.

47 See, e.g., Mexico–Nicaragua FTA (although in case of inconsistency, the chapter on services will apply to the extent of the inconsistency); Singapore–Australia FTA; and NZ–Singapore CEPA (although certain provisions in the chapter on investment do not apply to measures 'adopted pursuant to' the chapter on trade in services, see Article 26).

48 Most RTAs include measures by 'local' government, such as the US–Bahrain FTA, Article 10.1.2; EFTA–Korea FTA, Article 3.1.1; CAFTA–DR–US, Article 11.1.2; US–Morocco FTA, Article 11.1.2; and Thailand–Australia FTA, Article 802. The Japan–Mexico EPA includes measures taken by 'federal or central government, state, or prefecture or any other local authority' (Article 106(b)). On the other hand, some RTAs exclude measures taken by local government from the scope of the service chapter. For example, Article 1213 of the NAFTA provides that, for purposes of the service chapter 'a reference to a federal, state or provincial government includes any non-governmental body in the exercise of any regulatory, administrative or other governmental authority delegated to it by that government'. See also Mexico–Chile Free Trade Agreement, Article 10.02; and Canada–Chile FTA, Article H-12.

49 E.g., US–Singapore FTA, Article 8.2.1(c); and EFTA–Korea FTA, Article 3.1.1.

50 E.g., US–Singapore FTA, Article 8.2.1(c); and EFTA–Korea FTA, Article 3.1.1.

51 See EFTA–Korea FTA, Article 1.6: 'Each Party shall ensure within its territory the observance of all obligations and commitments under this Agreement by its respective regional and local governments and authorities, and by non-governmental bodies in the exercise of governmental powers delegated to them by central, regional and local governments or authorities'.

agreement.[52] This is usually done by defining the 'natural person' or 'juridical person' of a party supplying the service (which are the relevant criteria for modes 2, 3 and 4).[53]

A natural person of a party is usually defined on the basis of both residence and nationality requirements. For example, Article 802 of the Thailand–Australia Free Trade Agreement defines natural persons (for purposes of the coverage of the services chapter) to include natural persons who reside in the territory of that party and who, under the law of that party, are nationals of that party. At times, this definition (coverage) is expanded to include either nationals or permanent residents.[54] Other times, the relevant definition of natural person only requires nationality without residency.[55]

A juridical (or legal) person of a party is at a minimum defined as a juridical person which is constituted or organised under the law of that party.[56] Often, and in order to exclude from the beneficiaries of a RTA so-called mailbox companies, the relevant definition also includes the requirement that the juridical person be 'engaged in substantive business operation in the territory' of any party[57] or that its operations 'possess a real and continuous link with the economy' of any party.[58] Those services chapters that extend their coverage to mode 3 (i.e., commercial presence) provide for a specific definition of a juridical person of a party for purposes of this particular mode of supply. For example, the EFTA–Singapore Free Trade Agreement states that a juridical person of another party means 'a juridical person which is [. . .] (ii) in the case of the supply of a service through commercial presence, owned or controlled by: 1. natural persons of that other Party; or 2. juridical persons [constituted or organised under the law of that other party and engaged in substantive business operations in the territory of any Party]'.[59]

52 A similar point can be made for 'services' of the other party. Services chapters in RTAs in fact apply to services that are supplied 'from the territory of the other party', as this is implicit in the definition of mode 1, which is found in both 'trade in services' and 'cross-border trade in services' model RTAs.

53 Using the parallel in trade in goods, commentators refer to these rules as the 'rules of origin' for services. Cf. Fink and Molinuevo, above note 34, pp. 37–8.

54 E.g., Singapore–Australia FTA, Article 1(k), states as follows: '"natural person of a Party" means a natural person who resides in the territory of the Party or elsewhere and who under the law of that Party: (i) is a national of that Party; or (ii) has the right of permanent residence in that Party'. Similarly, EFTA–Singapore FTA, Article 22(j).

55 See EFTA–Korea FTA, Article 3.3.3, which, however, extends the coverage not only to nationals but also to 'permanent residents' of a party if that party accords substantially the same treatment to its permanent residents as to its nationals in respect of measures affecting trade in services. Also, EFTA–Mexico FTA, Article 20.

56 Singapore–Australia FTA, Article 1(f); NAFTA, Articles 201 and 1213, which expands the coverage of the services chapter not just to 'an enterprise constituted or organized under the law of a Party' but also to 'a branch located in the territory of a Party and carrying out business activities there'.

57 EFTA–Singapore FTA, Article 22(l). 58 EFTA–Mexico FTA, Article 20.

59 See also Singapore–Australia FTA, Article 1(f)(ii); EFTA–Korea FTA, Article 3.3.4(b); Thailand–Australia FTA, Article 802 and EFTA–Singapore FTA, Article 22(l).

On the other hand, certain RTAs do not provide for exhaustive definitions of these terms and instead rely on 'denial of benefits' provisions to limit the scope of the beneficiaries of the trade preferences granted in these agreements. According to these provisions a party may deny the benefits of the services chapter to a service supplier of the other party (or parties) if the judicial person is owned or controlled by nationals of a non-Party with which the denying party does not maintain diplomatic relations[60] or if the service is being supplied by an enterprise that has no substantial business activities in the territory of the other party and it is owned or controlled by persons of a non-party or the denying party.[61] Some of these agreements condition the applicability of the denial of benefits option to certain prior notification and consultation requirements.[62]

4. (Excluded) categories of services

While in principle all types of services are included in the service chapter of RTAs, it is very often the case that services chapters exclude certain categories of services from their coverage on a vertical (sector-specific) and/or horizontal (across all sectors) basis.

There are a few service sectors that are often excluded from the coverage of the service chapter. This is either because the agreement contains a specific chapter addressing that particular service sector or because the agreement as a whole does not cover it. For example, service chapters (as well as investment ones) in several RTAs do not cover trade in financial services as this is usually the subject matter of a specific chapter.[63] Another service sector that is usually excluded from the services chapter (as well as from the entire agreement) is 'air services', including domestic and international air transportation services, whether scheduled or

60 E.g. Article 1211(a) allows a NAFTA party to deny the benefits of the services chapter to a service provider of another NAFTA party where the party establishes that: 'the service is being provided by an enterprise owned or controlled by nationals of a non-Party and (i) the denying Party does not maintain diplomatic relations with the non-Party, or (ii) the denying Party adopts or maintains measures with respect to the non-Party that prohibit transactions with the enterprise or that would be violated or circumvented if the benefits of this Chapter were accorded to the enterprise [. . .]'.

61 See US–Singapore FTA, Article 8.11; and similarly Canada–Chile FTA, Article H-11. It is interesting to note that some agreements include both specific definitions of the meaning of a 'juridical person of a party' and a denial of benefits provision.

62 See, e.g., Canada–Chile FTA, Article H-11.2, stating as follows: 'Subject to prior notification and consultation in accordance with Articles L-03 (Notification and Provision of Information) and N-06 (Consultations), a Party may deny the benefits of this Chapter to a service provider of the other Party where the Party establishes that the service is being provided by an enterprise that is owned or controlled by persons of a non-Party and that has no substantial business activities in the territory of the other Party'.

63 See, e.g., US–Bahrain FTA, CAFTA–DR–US, US–Morocco FTA, Korea–Singapore FTA, US–Singapore FTA, and US–Chile FTA. The service chapter in the Korea–Chile FTA expressly excludes application to financial services despite there being no chapter on financial services in the agreement (Article 11.2.3). Similarly, the Central America–Chile Free Trade Agreement excludes financial services from the coverage of the agreement.

non-scheduled, and related services in support of air services, other than aircraft repair and maintenance services and speciality air services (that is non-transportation air services such as aerial firefighting, sightseeing, mapping, glider towing, etc).[64]

Services chapters often exclude from their coverage on a horizontal manner 'services supplied in the exercise of governmental authority', which are usually defined as 'any service which is supplied neither on a commercial basis nor in competition with one or more service suppliers'.[65] This is the same approach followed by the GATS. On the other hand, NAFTA takes a different approach as it lists the categories of services that the services chapter in NAFTA does not prevent a NAFTA party from providing, albeit in a manner not inconsistent with the chapter itself.[66]

5. (Excluded) government activities

Most RTAs exclude certain types of governmental activities from the coverage of the chapter on services either because these activities are covered in other chapters or because they are excluded from the agreement as a whole. The most recurrent ones are 'government procurement' and 'subsidies and grants provided by a party'.[67]

Another area which is excluded in basically all RTAs relates to the movement of natural persons, and in particular to 'measures pursuant to immigration laws and regulations',[68] affecting 'natural persons seeking access to the employment market or employed on a permanent basis in the territory of a party',[69] or 'regarding citizenship,

64 See, e.g., US–Bahrain FTA, Article 10.1.4(b); CAFTA–DR–US, Article 11.1.4(b); US–Morocco FTA, Article 11.1.4(b); Japan–Mexico EPA, Article 97.2(c); AUSFTA, Article 10.1.4(c); EFTA–Chile FTA, Article 22.2 (extending the limited coverage of the services chapter also to the 'selling and marketing of air transport services and computer reservation system services'); Korea–Chile FTA, Article 11.2.3(b); US–Singapore FTA, Article 8.2.3(c); US–Chile FTA, Article 11.1.4(b); Singapore–Australia FTA, Article 22.2–22.3; EFTA–Singapore FTA, Article 21.2; Canada–Chile FTA, Article H-01.2(b); and NAFTA, Article 1201.2(b).

65 See, e.g., US–Bahrain FTA, Article 10.1.6; Japan–Mexico EPA, Article 97.2(g); US–Morocco FTA, Article 11.1.6; and Thailand–Australia FTA, Article 803. At times this is done through incorporation of the relevant provision in the GATS: see, e.g., Article 4.4 of the Singapore–Jordan FTA. On the other hand, certain agreements do not provide for such an exclusion: see, e.g., the EFTA–Korea FTA.

66 Article 1201.3 provides as follows: 'Nothing in this Chapter shall be construed to: [. . .] (b) prevent a Party from providing a service or performing a function such as law enforcement, correctional services, income security or insurance, social security or insurance, social welfare, public education, public training, health, and child care, in a manner that is not inconsistent with this Chapter'.

67 See, e.g., US–Bahrain FTA, Article 10.1.4(c) and (d); CAFTA–DR–US, Article 11.1.4(c) and (d); Korea–Singapore FTA, Article 9.2.3(b) and (c); US–Morocco FTA, Article 11.1.4(c) and (d); Thailand–Australia FTA, Article 803; AUSFTA, Article 10.1.4(b) and (d); Korea–Chile FTA, Article 11.2.3(c) and (d); US–Singapore FTA, Article 8.2.3(b) and (d); US–Chile FTA, Article 11.1.4(c) and (d); Canada–Chile FTA, Article H-01.2(c) and (d); EFTA–Mexico FTA, Article 19.4 and 19.5; and EU–Chile AA, Article 95.3 and 95.4. Only procurement: EFTA–Singapore FTA, Article 21.4. Only subsidies or grants: Singapore–Australia FTA, Chapter 7, Article 2.2(a). Contrary to subsidies and grants, exclusion of procurement from the coverage of the services chapter is usually accompanied by the chapter dealing with procurement in services.

68 Japan–Mexico EPA, Article 97.2(f). 69 US–Singapore FTA, Article 8.2.4.

residence or employment on a permanent basis'.[70] The Singapore–Australia Free Trade Agreement strengthens this exclusion by expressly providing that:

> Nothing in this Chapter shall prevent a Party from applying measures to regulate the entry of natural persons of the other Party into, or their temporary stay in, its territory, including those measures necessary to protect the integrity of, and to ensure the orderly movement of natural persons across its borders, provided that such measures are not applied in such a manner as to nullify or impair the benefits accruing to the other Party under the terms of this Chapter.[71]

B. Main obligations and disciplines

This section addresses four main obligations and disciplines: 'national treatment', 'market access', 'transparency', and 'domestic regulation'. Given the different approaches followed by RTAs compared with the GATS approach, there is no justification in this section to distinguish between 'general' and 'specific' obligations.

1. National treatment

The National Treatment obligation is certainly a central obligation regulating trade in services. It is no surprise that it is found in almost all services chapters of RTAs. National treatment obligations, however, differ depending on their 'formulation' and/or their 'scope of application'.

With regard to their **formulation**, two models may be identified (once again stemming from the national treatment obligations in the NAFTA services chapter and in the GATS). Article 1202.1 of the NAFTA provides that:

> Each Party shall accord to service providers of another Party treatment no less favourable than that it accords, in like circumstances, to its own service providers.[72]

On the other hand, as examined above, Article XVII:1 of the GATS provides that:

> [. . .] each Member shall accord to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers.[73]

The two key differences relate to (a) the *beneficiaries* of the provision ('service providers' v 'services and service suppliers') and (b) to the *comparator* ('in like

70 Singapore–Australia FTA, Chapter 7, Article 2.3. 71 Singapore–Australia FTA, Chapter 7, Article 2.4.

72 Canada–Chile FTA, Article H-02; and US–Singapore FTA, Article 8.3.

73 Some RTAs also follow a hybrid approach, which refers the comparator 'in like circumstances' to both 'services and service providers'. See, e.g., the Mexico–Costa Rica FTA, Article 9-04: 'Cada Parte otorgará a los servicios y a los proveedores de servicios de otra Parte, un trato no menos favorable que el concedido en circunstancias similares a sus propios servicios o proveedores de servicios'. See also Mexico–Nicaragua FTA, Korea–Chile FTA, Japan–Mexico EPA, and Korea–Singapore FTA.

circumstances' v 'like'). These textual differences may have relevant implications in the protection afforded by the national treatment provision. The interpretations rendered by NAFTA and WTO dispute settlement panels/tribunals with regard to the national treatment obligation in the context of trade in services (as well as in other contexts such as trade in goods and investment) shows the relevance of these textual differences. For example, the phrase 'in like circumstances' has been employed by NAFTA tribunals not just to determine the competitive relationship between foreign and domestic enterprises (as the phrase 'like' has been interpreted by WTO panels) but also as a *de facto* public policy justification mechanism.[74]

With regard to the **scope of application**, the national treatment obligation is almost never applicable on a general and unconditional basis; rather its application depends on the extent of the parties' specific commitments or reservations, which are usually attached to and incorporated into the agreement itself. Once again, the two models adopted by RTAs follow the different approaches of the NAFTA services chapter and the GATS.[75] While the national treatment obligation in Chapter 12 of the NAFTA applies to any measure of a party with respect to any service sectors or sub-sectors *unless* they are expressly listed in that party's schedule ('negative list' approach),[76] the national treatment obligation in the GATS *only* applies in sectors inscribed in Members' schedule and subject to any conditions and qualifications set out therein ('positive/negative list' approach).[77]

Those RTAs that follow the NAFTA model usually allow a party to exclude both certain measures and certain sectors/sub-sectors/activities. For example, Article 8.7 of the United States–Singapore Free Trade Agreement provides that the national treatment obligation does not apply to (1) 'any existing non-conforming measure that is maintained by a Party at the central level of government [and] at a regional level of government as set out by that Party in its Schedule to Annex 8A' and (2) 'any measure that a Party adopts or maintains with respect to sectors, sub-sectors or activities as set out in its Schedule to Annex 8B'.[78] The difference between the two sets of reservations is that, at least in principle, the exclusion of 'non-conforming

74 See the 2001 Mexican Tracking Award, at para. 258. Cf. Federico Ortino, 'From 'Non-discrimination' to 'Reasonableness': A Paradigm Shift in International Economic Law?' (2005) 1 *Jean Monnet Working Paper Series* 1–59, at 17–32.

75 For a somewhat different approach see Article 37 on the 'Removal of Restrictions on Provision of Services' of the Revised CARICOM Treaty ('1. Subject to the provisions of this Treaty, Member States shall abolish discriminatory restrictions on the provision of services within the Community in respect of Community nationals. 2. Subject to the approval of the Conference, COTED, in consultation with other competent Organs, shall, within one year from the entry into force of this Treaty, establish a programme for the removal of restrictions on the provision of such services in the Community by Community nationals.').

76 This is the 'negative list' approach as the relevant obligation will apply unless the party does not list any relevant *non-conforming measures* and/or any relevant *uncommitted services sectors or sub-sectors*.

77 We refer to the GATS approach as a 'positive/negative list' approach because the relevant obligation applies only to those sectors that are listed or committed in the Member's schedule (positive listing) and subject to any conditions and qualifications set out therein (negative listing).

78 See also Japan–Mexico EPA, Article 101; and Korea–Chile FTA, Article 11.5.

measure' can apply only to *existing* measures:[79] provisions such as Article 8.7 of the US–Singapore FTA seems to imply that once the non-conforming measure is eliminated, the party's policy will automatically be bound at the more liberal level. On the other hand, the exclusion of certain sectors/sub-sectors/activities applies to both existing and future measures. Moreover, it is common that in the NAFTA model 'negative list' agreements, the national treatment provision does not apply to any existing non-conforming measure maintained by a *local government* of the party independently of their express inclusion in the party's schedule.

On the other hand, those RTAs that follow the GATS model condition the applicability of the national treatment obligation to the specific commitments of the party both in terms of sectors (positive element) and conditions (negative element). For example, Article 4.3.1 of the Singapore–Jordan Free Trade Agreement takes the GATS model 'positive/negative list' approach as it provides that:

> In the sectors inscribed in its Schedule of specific commitments, and subject to any conditions and qualifications set out therein, each Party shall accord to services and service suppliers of the other Party, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers.[80]

For all these agreements, in order to determine the level of actual liberalisation, it is necessary to examine each party's schedule of commitments as well as its laws and regulations.[81]

2. Market access

A market access provision is also very common in services chapters of RTAs, albeit it may take different forms. Usually, these provisions are aimed at prohibiting a set of governmental measures restricting the provision of services apparently whether they are discriminatory or non-discriminatory in nature. The approach to market access in services chapter of RTAs differ depending on (1) the list of measures in principle covered by the prohibition; (2) the normative content of the provision (i.e., what the provision would require); and (3) the actual scope of application (i.e., whether and the extent to which the market access provision is subject to specific commitments, conditions and/or reservations).

With regard to the *measures in principle covered* by the market access prohibition, they may include (a) restrictions of a quantitative nature; (b) restrictions on the type of legal entity required in order to provide a service; and (c) restrictions on foreign equity

79 This exclusion usually extends to the 'continuation or prompt renewal' of any non-conforming measure as well as 'an amendment to' any non-conforming measure (to the extent that the amendment does not decrease the conformity of the measure).

80 See also Thailand–Australia FTA, Article 810; EFTA–Chile FTA, Article 26; and US–Jordan, Article 3.2(b).

81 For a recent, in-depth study assessing the level of actual liberalisation with regards to trade in services in RTAs, see Roy, Marchetti and Lim, above n. 8.

participation. These corresponds to the measures listed in Article XVI:2(a)–(f) of the GATS. Several RTAs follow exactly this approach by either reproducing Article XVI of the GATS verbatim[82] or by incorporating it into the agreement.[83] Other RTAs, including most of the recent United States RTAs, follow a very similar list but omit reference to restrictions on foreign equity participation.[84] As rightly noted by Fink and Molinuevo, this omission does not, however, appear to modify the liberalisation nature of the agreement as foreign equity restrictions would, at least in principle, be caught by the national treatment provision.[85]

Other older RTAs, such as NAFTA, on the other hand, do not have a specific provision on 'market access' but include a similar provision addressing 'quantitative restrictions', which are defined as 'non-discriminatory measures that impose limitations on: (a) the number of service providers, whether in the form of a quota, a monopoly or an economic needs test, or by any other quantitative means; or (b) the operations of any service provider, whether in the form of a quota or an economic needs test, or by any other quantitative means'.[86] Depending on the interpretation of the term 'limitations on the operations of any service supplier', this apparently more limited list of restrictions may have a similar or broader coverage compared to the GATS-based list of market access restrictions. Only very few RTAs do not have any type of market access provision.[87]

With regard to the *normative content* of the market access provisions in services chapters, this is usually fairly unproblematic as a market access provision at least in

82 See, e.g., Thailand–Australia FTA, Article 809; EFTA–Chile FTA, Article 25; and EFTA–Singapore FTA, Article 24.

83 See, e.g., EFTA–Korea FTA, Article 3.5; Singapore–Jordan FTA, Article 4.2; and US–Jordan FTA, Article 3.2(a).

84 See, e.g., Article 10.4 of the US–Bahrain FTA which states as follows:

1. Neither Party may adopt or maintain, either on the basis of a regional subdivision or on the basis of its entire territory, measures that:

(a) impose limitations on:

(i) the number of service suppliers whether in the form of numerical quotas, monopolies, exclusive service suppliers, or the requirement of an economic needs test;

(ii) the total value of service transactions or assets in the form of numerical quotas or the requirement of an economic needs test;

(iii) the total number of service operations or on the total quantity of services output expressed in terms of designated numerical units in the form of quotas or the requirement of an economic needs test; or

(iv) the total number of natural persons that may be employed in a particular service sector or that a service supplier may employ and who are necessary for, and directly related to, the supply of a specific service in the form of numerical quotas or the requirement of an economic needs test; or

(b) restrict or require specific types of legal entity or joint venture through which a service supplier may supply a service.

See also CAFTA–DR–US, Article 11.4; US–Morocco FTA, Article 11.4; and AUSFTA, Article 10.4.

85 See Fink and Molinuevo, above n. 34.

86 NAFTA, Article 1213. See also Canada–Chile FTA, Article H-12.

87 See, e.g., Japan–Mexico EPA.

principle (i.e., subject to its actual scope of application) prohibits parties from adopting or maintaining the measures listed in the market access provision itself. For example, Article 8.5 of the US–Singapore FTA provides that 'A Party *shall not adopt or maintain* [. . .] measures that (a) limit (i) the number of service suppliers [. . .] and (b) restrict or require specific types of legal entity [. . .]'.[88]

However, in some of the older RTAs, such as NAFTA, the only express rule provided for with regard to the 'quantitative restrictions' covered by the services chapter is a mere listing and notification requirements as well as a non-binding obligation to negotiate the liberalisation and removal of those restrictions. Article 1207 of the NAFTA on 'Quantitative Restrictions' provides as follows:

1. Each Party shall set out in its Schedule to Annex V any quantitative restriction that it maintains at the federal level.
2. Within one year of the date of entry into force of this Agreement, each Party shall set out in its Schedule to Annex V any quantitative restriction maintained by a state or province, not including a local government.
3. Each Party shall notify the other Parties of any quantitative restriction that it adopts, other than at the local government level, after the date of entry into force of this Agreement and shall set out the restriction in its Schedule to Annex V.
4. The Parties shall periodically, but in any event at least every two years, endeavour to negotiate the liberalisation or removal of the quantitative restrictions set out in Annex V pursuant to paragraphs 1 through 3.[89]

Nevertheless, even these types of agreements include the possibility for parties to commit to the liberalisation (i.e., the elimination) of non-discriminatory quantitative restriction. For example, Article 1208 of the NAFTA on 'Liberalization of Non-Discriminatory Measures' provided that 'Each Party shall set out in its Schedule to Annex VI its commitments to liberalize quantitative restrictions, licensing requirements, performance requirements or other non-discriminatory measures'.[90]

Finally, significant differences also exist with regard to the actual **scope of application** of the market access provision. Like for the national treatment obligation, the market access provisions in services chapters is never applicable on a general and unconditional basis; rather its application depends on the extent of the parties' specific commitments or reservations, which are usually attached to and incorporated into the agreement itself. As noted with regard to national treatment, a market access provision may either take a NAFTA-based 'negative list' approach[91] or a GATS-based 'positive/negative list' approach.[92]

88 Emphasis added.

89 See also the Korea–Chile FTA, Article 11.6; and Canada–Chile FTA, Article H-07.

90 See also the Korea–Chile FTA, Article 11.8; and Canada–Chile FTA, Article H-08.

91 See, e.g., US–Bahrain FTA, Article 10.4; CAFTA–DR–US, Article 11.4; US–Morocco FTA, Article 11.4; AUSFTA, Article 10.4; and Singapore–Australia FTA, Chapter 7, Article 3.

92 See, e.g., Thailand–Australia FTA, Article 809; EFTA–Chile FTA, Article 25; and EFTA–Singapore FTA, Article 24.

3. Transparency

Transparency requirements are generally very common in RTAs whether they are provided for in a separate chapter applying across the agreement (such as in NAFTA and the recent FTAs concluded by the United States) or as specific provisions found in individual chapters (such as the services chapter). Also with regard to transparency requirements, these agreements follow in general either a GATS-based approach[93] or a NAFTA-based approach, albeit the difference is simply that the latter agreements provide for a marginally broader set of transparency obligations compared to the former.

Transparency requirements differ depending principally on two key features: (1) the mechanisms employed to implement transparency; and (2) the items of information subject to the transparency requirements.

The principal **mechanisms employed to implement transparency** applicable *inter alia* to trade in services include: (a) publication requirements; (b) provision of information requirements; (c) notification requirements; and (d) transparency requirements in administrative proceedings.

Most agreements setting out transparency obligations applying to trade in services include at least a so called 'publication' requirement, whereby, similarly to Article III:1 of the GATS, each party is required to promptly publish or otherwise make available certain measures respecting trade in services.[94] Several of these publication requirements, however, differ from the publication obligation in the GATS as they specifically require parties to make their measures available in such a manner as to enable the other Party and *interested persons* to become acquainted with them. For example, Article 14.1.1 of the New Zealand–Thailand Closer Economic Partnership Agreement (NZ–Thailand CEPA) provides that:

> Each Party shall ensure that its laws, regulations, administrative rulings, procedures and policies and any amendment thereto of general application pertaining to trade in goods, services and investment are promptly published or otherwise made available in such a manner as to enable interested persons from the other Party to become acquainted with them.[95]

93 See, e.g., Singapore–Australia FTA, Article 9.

94 See Japan–Mexico EPA, Article 160; EFTA–Chile FTA, Article 82.1; Korea–Chile FTA, Article 17.3.1; Singapore–Australia FTA, Article 9.1; and EFTA–Korea FTA, Article 3.18.

95 See also Article 18.03 of the Central America–Panama Free Trade Agreement (Panama–El Salvador) stating that: 'Cada Parte se asegurará que sus leyes, reglamentos, procedimientos y resoluciones administrativas de aplicación general que se refieran a cualquier asunto comprendido en este Tratado, se publiquen a la brevedad o se pongan a disposición para conocimiento de las Partes y de cualquier interesado'. Cf. Thailand–Australia FTA, Article 1402.1; AUSFTA, Article 20.2.1; Central America–Chile FTA (Chile–El Salvador), Article 17.03.1; US–Singapore FTA, Article 19.3.1; US–Chile FTA, Article 20.2.1; and US–Bahrain FTA, Article 17.1.1.

Reference to 'interested persons' other than the contracting parties may arguably have an influence on the publication mechanisms that need to be chosen in order to comply with the publication requirements of the treaty.[96]

Differently from the publication requirements under the GATS, some agreements also include the obligation to publish *in advance* any proposed measure and to provide interested persons with a reasonable *opportunity to comment* on such proposed measures.[97] Some of those agreements based on the NAFTA model also include a provision in the services chapter requiring a party, which does not provide advance notice and opportunity to comment pursuant to the disciplines in the chapter on transparency, to address in writing the reasons therefore.[98]

Like Article III:4 of the GATS, most RTAs include provisions requiring parties to provide information and respond to questions from the other party ('provision of information' requirements). Some RTAs also include 'proposed measures' under the scope of these requirements. For example, Article 18.3.2 of the Central America–Dominican Republic–United States Free Trade Agreement (CAFTA–DR–US) provides that 'On request of another Party, a Party shall promptly provide information and respond to questions pertaining to any actual or proposed measure [. . .]'. In addition to these general obligations to provide information, several agreements provide for the establishment of permanent enquiry or contact points in order to facilitate communications between the parties and to provide information on relevant matters.[99]

Equally common are 'notification' requirements (in particular in agreements following the NAFTA-based approach to transparency), whereby parties are required to notify the other party of certain proposed or actual measures. Article 18.3.1 of the CAFTA–DR–US provides that 'To the maximum extent possible, each Party shall notify any other Party with an interest in the matter of any proposed or actual measure that the Party considers might materially affect the operation of this Agreement or otherwise substantially affect that other Party's interests under this Agreement'.[100]

A further form of transparency provisions, which may be found in a few RTAs (but excluded from the transparency requirements in GATS), requires parties

96 Interestingly, Article 1402.3 of the Thailand–Australia FTA specifies that a party may comply with the publication requirements of the agreement 'by publication on the internet'.

97 See, e.g., Article 14.1.3 of the NZ–Thailand CEPA which states that: 'When possible, a Party shall publish in advance any measure referred to in Paragraph 1 that it proposes to adopt and shall provide, where applicable, interested persons with a reasonable opportunity to comment on such proposed measures'. Cf. EFTA–Chile FTA, Article 83.2.

98 See, e.g., AUSFTA, Article 10.8.2. This provision also requires parties at the time of adoption of final regulations relating to trade in services, to the extent possible, to address in writing substantive comments received from interested persons with respect to the proposed regulations (Article 10.8.3).

99 See, e.g., CAFTA–DR–US, Article 18.1.

100 No notification requirements may be found in the agreements following a GATS-based approach to transparency such as EFTA–Chile FTA, Singapore–Australia FTA, Japan–Mexico EPA, Singapore–Jordan FTA, and EFTA–Korea FTA.

to follow certain transparency/due process requirements in administrative proceedings. For example, Article 18.4 of the CAFTA–DR–US provides that:

> [E]ach Party shall ensure that in its administrative proceedings [. . .] (a) wherever possible, persons of another Party that are directly affected by a proceeding are provided reasonable notice, in accordance with domestic procedures, when a proceeding is initiated, including a description of the nature of the proceeding, a statement of the legal authority under which the proceeding is initiated, and a general description of any issues in controversy; (b) such persons are afforded a reasonable opportunity to present facts and arguments in support of their positions prior to any final administrative action, when time, the nature of the proceedings, and the public interest permit [. . .].

It should be noted that, although they generally adopt mandatory language, all these transparency requirements may at times be limited by wording such as 'wherever possible',[101] 'to the extent possible',[102] 'to the maximum extent possible',[103] 'when possible'.[104] Undoubtedly, these limitations leave some discretion to parties in implementing transparency requirements.

The *items of information* that are subject to transparency requirements may differ depending on the specific transparency mechanism.

With regard to 'publication' requirements, reference is usually made to 'measures of general application' either with respect to any matter covered by the agreement (for those agreements with a separate chapter on transparency) or affecting the operation of the services chapter. In particular, those agreements that follow the broad NAFTA-based approach to transparency requirements make express reference to 'laws, regulations, procedures, and administrative rulings of general application' with regard to publication requirements. Most of these agreements also provide for a definition of 'administrative rulings of general application'. For example, Article 18.6 of CAFTA–DR–US provides that:

> For purposes of this Section: 'administrative ruling of general application' means an administrative ruling or interpretation that applies to all persons and fact situations that fall generally within its ambit and that establishes a norm of conduct but does not include: (a) a determination or ruling made in an administrative or quasi-judicial proceeding that applies to a particular person, good, or service of another Party in a specific case; or (b) a ruling that adjudicates with respect to a particular act or practice.[105]

101 See, e.g., AUSFTA, Article 20.4.

102 See, e.g., Central America–Panama FTA (Panama–El Salvador), Article 18.4.

103 See, e.g., Korea–Chile FTA, Article 17.4.1.

104 See, e.g., Thailand–Australia FTA, Article 1401.4.

105 Similarly, Article 14.1.2 of the NZ–Thailand CEPA provides that: 'For the purposes of this Chapter, "administrative ruling of general application" means an administrative ruling or interpretation that applies to all persons and fact situations and that is relevant to the implementation of this Agreement'.

Even some of the agreements following the strict GATS-based approach to transparency specify the items of information that are subject to publication requirement. For example, Article 160 of the Japan–Mexico Economic Partnership Agreement (Japan–Mexico EPA) refers to 'laws, regulations, administrative procedures and administrative rulings and judicial decisions of general application as well as international agreements to which the Party is a party'.

On the contrary, notification and provision of information requirements in the NAFTA-based agreements seem to refer generally to 'measures' that the party considers might materially affect the operation of the agreement or otherwise substantially affect the other party's interests under the agreement.[106] Interestingly, these agreements tend to limit the scope of the notification/provision of information requirements by qualifying the otherwise broad term 'affect' with terms such as 'materially' and ' substantially'.[107]

4. Domestic regulation

Rules on domestic regulation may be found in several RTAs covering services trade.[108] These rules may require parties to (a) administer domestic laws in a reasonable, objective and impartial manner; (b) establish review and appeal mechanisms for administrative decisions; (c) ensure that measures relating to qualification requirements and procedures, technical standards, and licensing requirements do not constitute unnecessary barriers to trade in services (so called 'necessity requirement'); and (d) use relevant international standards.[109] While Article VI of the GATS include all four rules (albeit subject to certain limitations), RTAs vary in their approach to domestic regulation, most of them not going beyond what is provided by GATS.[110]

106 CAFTA–DR–US, Article 18.3.1. Following the approach in Article III:4 of the GATS, other agreements refer to 'measures of general application' in their provision of information requirements. See, e.g., Singapore–Australia FTA, Article 9.3; Singapore–Jordan FTA, Article 4.14.3; and EFTA–Korea FTA, Article 3.18.

107 Cf. UNCTAD, *Transparency: UNCTAD Series on Issues in International Investment Agreements* (Geneva: UN, 2004).

108 Several RTAs also include provisions on mutual recognition which for the most part replicate Article VII of the GATS. A few of these RTAs include at times more detailed provisions on the recognition of professional qualifications and registration procedures (Singapore–Jordan FTA, Article 4.8; Thailand–Australia FTA, Article 806; and Singapore–Australia FTA, Article 23), and higher education qualification (Central America–Panama FTA (Panama–El Salvador), Annex 11.13). At times mutual recognition provisions are included in annexes dealing specifically with professional services. See below next section.

109 Few times, RTAs simply provide for non-discrimination obligation with regard to similar domestic laws. E.g., Article 9.1 of the Australia–New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) requires, on a hortatory basis, that 'licensing and certification measures shall not have the purpose or effect of impairing or restraining, in a discriminatory manner, access of persons of the other Member State to such licensing or certification'.

110 For those RTAs that do not contain rules on domestic regulation applicable generally to trade in services, see, e.g., the EU–Mexico FTA.

With regard to the obligation to **administer domestic laws in a reasonable, objective and impartial manner**, several services chapters in RTAs follow the GATS approach either by reproducing Article VI:1 language[111] or by making express reference to the relevant GATS provisions.[112] In the case of the EFTA–Mexico Free Trade Agreement, such an obligation is found in Article 25 on the 'Right to Regulate'.[113] A few other agreements, following the NAFTA, do not provide for such a general obligation.[114]

With regard to the scope of application, this obligation may apply either only in the service sectors and sub-sectors where commitments have been undertaken (similarly to Article VI:1 of the GATS) or in principle to all service sectors and sub-sectors except as provided in the relevant annex on reservations or non-conforming measures (i.e., negative-list approach). For example, of the seven RTAs concluded by Singapore, which have been notified on the basis of Article V of the GATS, four follow the GATS positive/negative-list approach,[115] two follow a negative-list approach[116] and one does not include such a general obligation.[117] Only in very few instances, the obligation to administer domestic laws in a reasonable, objective and impartial manner applies generally and unconditionally.[118]

Most RTAs include provisions requiring parties to **establish and maintain review and appeal mechanisms for administrative decisions** either as part of the services

111 See, e.g., Singapore–Australia FTA, Article 11; and Protocol of Montevideo for the Trade in Services of MERCOSUR, Article 10.1.

112 See, e.g., EFTA–Korea FTA, Article 3.8; Singapore–Jordan FTA, Article 4.9; and US–Jordan FTA, Article 3.2(c)(ii).

113 '1. Each Party may regulate, and introduce new regulations, on the supply of services within its territory in order to meet national policy objectives, in so far as regulations do not impair on any rights and obligations arising under this Agreement. 2. Each Party shall ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner.' EFTA–Mexico FTA, Article 25.1–2.

114 As mentioned above in the section on transparency, NAFTA does however include a more limited obligation addressing the administration of domestic laws. Article 1804 provides that 'With a view to administering in a consistent, impartial and reasonable manner all measures of general application affecting matters covered by this Agreement, each Party shall ensure that in its administrative proceedings applying measures referred to in Article 1802 to particular persons, goods or services of another Party in specific cases that: (a) wherever possible, persons of another Party that are directly affected by a proceeding are provided reasonable notice, in accordance with domestic procedures, when a proceeding is initiated, including a description of the nature of the proceeding, a statement of the legal authority under which the proceeding is initiated and a general description of any issues in controversy; (b) such persons are afforded a reasonable opportunity to present facts and arguments in support of their positions prior to any final administrative action, when time, the nature of the proceeding and the public interest permit; and (c) its procedures are in accordance with domestic law'. See also Korea–Chile FTA, Article 17.6; Japan–Mexico EPA, Article 162; US–Singapore FTA, Article 19.5; and Central America–Panama FTA (Panama–El Salvador), Article 18.06.

115 NZ–Singapore CEPA, Article 21.1; Japan–Singapore EPA, Article 64.1; EFTA–Singapore FTA, Article 28.1; and Singapore–Jordan FTA, Article 4.9.1.

116 Singapore–Australia FTA, Articles 11.1 and 5.3; and Korea–Singapore FTA, Articles 9.11.1 and 9.6.3.

117 US–Singapore FTA.

118 See, e.g., the Protocol of Montevideo for the Trade in Services of MERCOSUR, Article 10.1.

chapter or as part of the chapter on transparency.[119] For example, Article 163.1 of the Japan–Mexico EPA on 'Review and Appeal' (following a very similar provision in NAFTA) provides that:

> Each Party shall maintain judicial or administrative tribunals or procedures for the purpose of prompt review and, where warranted, correction of administrative actions regarding matters covered by this Agreement. Such tribunals or procedures shall be impartial and independent of the authorities entrusted with the administrative enforcement.[120]

Similarly, most RTAs include a **necessity requirement** with regard to certain measures affecting trade in services. Following the Article VI:5 of the GATS model, certain RTAs require parties to ensure that 'licensing and qualification requirements and technical standards' are based on objective and transparent criteria and not more burdensome than necessary to ensure the quality of a service. However, as mentioned above when analysing GATS rules on domestic regulation, necessity requirements following the GATS model are subject to two important limitations: they can be invoked only if the relevant regulatory measures nullify or impair specific commitments *and* could not reasonably have been expected when specific commitments were made.[121]

Those agreements that follow the NAFTA model with regard to the rules on domestic regulation usually differ from GATS necessity requirement in two respects. First, the necessity requirements found in the services chapter apply only on a best endeavour basis.[122] Second, they usually cover only 'requirements and procedures to the licensing or certification' of service providers of the other party (leaving out 'technical standards').[123] However, a few of these agreements (like NAFTA) contain a chapter on 'technical barriers to trade', which extends its coverage to 'standards-related

119 Again here, GATS Article VI:2, on the one hand, and NAFTA Article 1805, on the other, provide the two models that are followed by subsequent RTAs.

120 See also, Central America–Panama FTA (Panama–El Salvador), Article 18.07.1. Those agreements that follow the NAFTA provision also include a due process-type of procedural right by requiring that parties to such administrative proceedings be provided with 'the right to (a) a reasonable opportunity to support or defend their respective positions; and (b) a decision based on the evidence and submissions of record or, where required by domestic law, the record compiled by the administrative authority'. Cf. NAFTA, Article 1805.2.

121 One notable exception is the necessity requirement found in Article 10.4 of the Protocol of Montevideo for the Trade in Services of MERCOSUR, which do not include either of the two limitations.

122 For example, NAFTA Article 1210.1 provides that: 'With a view to ensuring that any measure adopted or maintained by a Party relating to the licensing or certification of nationals of another Party does not constitute an unnecessary barrier to trade, each Party shall endeavour to ensure that any such measure: (a) is based on objective and transparent criteria, such as competence and the ability to provide a service; (b) is not more burdensome than necessary to ensure the quality of a service; and (c) does not constitute a disguised restriction on the cross-border provision of a service'. See also Korea–Chile FTA, Article 11.10; Japan–Mexico EPA, Article 104.1; and US–Singapore FTA, Article 8.8.1.

123 See NAFTA, Article 1210.1; Korea–Chile FTA, Article 11.10; Japan–Mexico EPA, Article 104.1; Central America–Panama FTA, Article 11.07; and EU–Chile AA, Article 102.1. However, the US–Singapore FTA extends its non-mandatory necessity requirement to 'technical regulations' as well (Article 8.8.1).

measures' that affect both trade in goods and services[124] and provide, *inter alia*, for mandatory (WTO TBT Agreement-like) necessity requirements.[125]

Finally, requirements to **use relevant international standards** may take two forms depending on whether they are found in the provision on domestic regulation in the services chapter or in the chapter on standards-related measures. First, relevant international standards are taken into account to determine whether domestic measures (such as licensing and qualification requirements) comply with the necessity requirements in the RTA. This is the Article VI:5 of the GATS model.[126] A variance to this approach is taken by those RTAs expressly providing that 'domestic regulation prepared, adopted and applied in accordance with international standards shall be rebuttably presumed to comply with the [rules on domestic regulation]'.[127] This is also similar to the approach employed in Article 3.2 of the WTO SPS Agreement.

Secondly, other RTAs require parties to use international standards as a basis for preparing or applying their standards-related measures.[128] This approach is very similar to that characterising Article 2.4 of the WTO TBT Agreement.

C. Sectoral disciplines

Several RTAs set out additional disciplines for specific service sectors in separate chapters (or annexes).[129] Financial services and telecommunications are the two areas for which these agreements include most often additional disciplines. Individual chapters (or annexes or sections) on 'transport', 'professional services' or 'temporary entry of business persons' may also be found in RTAs. Unsurprisingly, all these areas are subject to specific disciplines also within the GATS, mostly in annexes, understandings and reference papers.

The extent and content of the additional disciplines within RTAs may vary from a few provisions replicating the rules generally applicable to trade in services to a set of

124 NAFTA, Article 901; Central America–Panama FTA, Article 9.03; and Mexico–Chile FTA, Article 8-03.1. (It should be noted, however, that Annex 8-01 limits the applicability of the chapter on standards-related measures de facto to computer and related services, only.) On the other hand, a few agreements that exclude 'technical regulations' from the scope of the necessity requirements do not extend the chapter on technical barriers to trade to measures affecting trade in services. See, e.g., Korea–Chile FTA, Article 9.3.

125 E.g. Central America–Panama FTA, Article 9.04.2, provides that: 'No Party may prepare, adopt, maintain or apply any standards-related measures, approval procedures and metrology-related measures with the purpose or effect of creating an unnecessary obstacle to trade with the other Party'.

126 See, e.g., Japan–Singapore EPA, Article 64.6; and Singapore–Australia FTA, Article 11.7.

127 NZ–Singapore CEPA, Article 21.4. See also Mexico–Chile FTA, Article 8-04.4(b); EFTA–Singapore FTA, Article 28.6; and EFTA–Chile FTA, Article 28.6.

128 See, e.g., Central America–Panama FTA, Article 9.02.4; and Central America–Chile FTA, Article 9.04.4.

129 Other agreements may instead provide for specific provision(s) dealing with certain services sectors. See, e.g., Singapore–Jordan FTA, Articles 4.16–4.18, dealing with Telecommunications, Financial Services Cooperation and Transport Cooperation, respectively.

comprehensive and/or additional disciplines distributed among several articles (the latter most often in the case of financial services and telecommunications). For example, the chapter on *financial services* in the European Union–Mexico Free Trade Agreement (which is more detailed than the chapter setting out the general provisions on trade in services) includes provisions very similar to the GATS 'Understanding on commitments in financial services' and 'Annex on financial services', such as provisions on establishment of financial service suppliers, cross-border provision of financial services, national treatment, most-favoured-nation treatment, regulatory and prudential carve outs, data processing, consultations and dispute settlement.

For example, the chapter on *telecommunications* in the Korea–Chile Free Trade Agreement includes many of the rules provided by the 'WTO Reference paper on basic telecommunications' such as 'access to and use of public telecommunications transport networks and services', 'conditions for the provision of enhanced or value-added services', 'standards-related measures', 'monopolies', and 'transparency'.

With regard to *professional services*, some RTAs provide specific annexes aimed at facilitating the provision of services by foreign professionals in particular through development of mutually acceptable standards and criteria for licensing and certification of professional service providers. Additionally, certain RTAs sets out specific sections for 'foreign legal consultants' and the 'temporary licensing of engineers' requiring parties, for example, to consult with their relevant professional bodies in order to develop common standards and criteria for the authorisation of foreign legal consultants and the temporary licensing of foreign engineers.[130]

IV. Brief conclusions

From the perspective of the different approaches that RTAs have adopted in regulating trade in services, the present chapter shows that, despite the fact that all these agreements adopt more or less different rules ('there isn't one agreement like another'), most of them follow in principle the NAFTA and GATS models.[131] And these two models do not take two diametrically opposite approaches to the regulation of trade in services. However, the differences are there, as the chapter has emphasised, for example, with regard to the 'scope of application' of the services chapters, the 'formulation' of the national treatment standard, the transparency requirements and the disciplines on domestic regulation. These differences have not really come to the surface as there has not been much adjudication with regard to all these provisions.[132] And a similar fate has been reserved to the GATS.

130 See, e.g., US–Chile FTA, Annex 11.9, on Professional Services.

131 The third model is that provided by the EC Treaty, which this chapter has not addressed.

132 The only exceptions are certainly the EC Treaty and to a much more limited extent MERCOSUR and NAFTA.

The question that thus arises is whether these RTAs are functioning only as pro-liberalisation instruments, that is to get countries to increase the level of market access in the service sector. This is certainly part of the rationale of the services chapters in RTAs (as well as beyond services). However, one cannot deny other structural benefits of such agreements. For example, any discipline dealing with services regulation that is provided for in a RTA (such as transparency requirements, disciplines on domestic regulation, competition-oriented disciplines in the telecommunications sector) will bring certain benefits not just to the service providers of the other party to the RTA but in principle to all service suppliers. Many barriers to trade in services are in fact embedded in regulatory regimes and governments will often not put in place different regulatory regimes for different supplier countries.[133]

Looking ahead, one strategy to increase the (currently very slow) pace of the liberalisation of trade in services (both at the regional and multilateral levels) may be to strengthen the 'regulatory' agenda of these agreements. In other words, it may be useful to make sure that the liberalisation of trade and investment in services (including several very crucial and sensitive service sectors) are accompanied by a (stronger) international programme of regulatory reforms (involving both regulators and industries) to be implemented at the domestic level. Particularly with regard to services, sustainable liberalisation cannot go ahead in any meaningful way without proper regulation.

133 See Roy, Marchetti and Lim, above n. 8, at 55.

9

Investment

JOSHUA P. MELTZER*

I. Introduction

This chapter addresses the legal and policy issues arising out of Bilateral and Regional Free Trade Agreement (FTA) Investment Chapters.[1]

Part II commences with an examination of the history of treaty-based legal protections for foreign investment. This Part traces the evolution of investment provisions, from Treaties of Friendship, Navigation and Commerce (FNC), through to Bilateral Investment Treaties (BITs), and their most recent incorporation into Investment Chapters in Free Trade Agreements (FTAs).

Part III considers how the different definition of phrases such as 'investor' and 'investment' determine the scope of FTA Investment Chapters. This Part therefore inquires into who the investment chapter applies to, and what will constitute an investment for the purpose of the chapter.

Part IV continues the analysis of States' commitments in the FTA Investment Chapter, but with a focus on their substantive commitments.

Part V focuses on investor-state dispute settlement (ISDS) provisions in FTA investment chapters and outlines the main elements and differences between the ISDS provisions in different FTA Investment Chapters. It also explains how these ISDS provisions use, and rely on, the United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules and the International Centre for Settlement of Investment Disputes (ICSID) Convention, Regulations and Rules ('ICSID Convention').

Part VI outlines the different architectures of FTA Investment Chapters, with a focus on whether States schedule their market access commitments in the form of either a positive or negative list. This part looks at the differences between positive and negative lists and considers the argument for and against each approach.

Finally, Part VII discusses the main issues likely to arise under FTA Investment Chapters and considers the implications of the proliferation of FTAs with Investment Chapters for progress on investment at the WTO.

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1 For the purposes of this chapter, a reference to an FTA Investment Chapter will, unless otherwise stated, include investment chapters in bilateral or regional FTAs.

II. International investment law – From FCNs to FTAs

Investment provisions in international agreements have a long history. During the seventeenth and eighteenth centuries, a combination of capital and expertise led to significant foreign investment from United States (US) and European investors in large infrastructure projects such as railroads and telegraph systems in areas such as Latin America. However, the perceived national interest character of these investments also caused host States, from time to time, to expropriate these investments, thereby highlighting to investors the need for mechanisms to protect their overseas investments.[2]

As a result, the US, in the eighteenth Century, began entering into what have been described as treaties of 'Friendship, Commerce and Navigation' (FCN). As their name suggests, investment was only one component of FCN treaties, which also included commitments on trade and navigation and friendship. The earlier FCN treaties also limited their investment protections to 'special protection' or 'full protection and security'. By the late nineteenth century, however, these treaties included provisions protecting against expropriation, and Most-Favoured-Nation (MFN) and National Treatment (NT) commitments. Some of the FCN treaties negotiated in the early part of the twentieth century also included currency protection provisions. In this way, the FCN treaty project presaged the modern BIT.[3]

During the nineteenth century, expropriation by States of foreign investment in infrastructure was one of the main concerns of foreign investors. During this period, recourse by the investing State in the event of an expropriation was limited to either diplomatic protection, or in some cases, the use of military force, often referred to as 'gunboat diplomacy'.

Legally, there was also disagreement between the foreign investor and the host state over the scope of the expropriation obligation. One view of the obligation of States when expropriating foreign investment was expounded in 1868 by Carlos Calvo, an Argentinian lawyer. The so-called 'Calvo doctrine' stated that foreign investors were only entitled to the level of protection afforded to nationals. The implication of the Calvo doctrine was that the obligations regarding expropriation were to be determined by reference to the host States' domestic laws.[4] Further, a foreign investor, similar to a domestic investor, could litigate a claim against the host State using the domestic court system. By contrast, recourse to diplomatic protection or gunboat diplomacy was considered unlawful.

2 Raymond D. Bishop, James Crawford and Michael W. Reisman (eds.), *Foreign Investment Disputes: Cases, Materials, Commentary* (The Hague: Kluwer Law International, 2005), at p. 3.

3 Kenneth J. Vandevelde, 'The Bilateral Investment Treaty Program of the United States' (1988) 21 *Cornell International Law Journal* 201–76, at 208.

4 See Donald R. Shea, *The Calvo Clause. A Problem of Inter-American and International Law and Diplomacy* (Minneapolis: Minnesota University Press, 1955), at p. 17.

The alternative argument, outlined by Cordell Hull, the US Secretary of State, argued that any expropriation required 'prompt, adequate and effective compensation'.[5] This became known as the 'Hull Rule', and effectively was an argument for an absolute obligation defined by international law and therefore independent of the host State's treatment of its own citizens.

The end of World War II led to the recognition of 'the need for international economic institutions to prevent the type of ''beggar-my-neighbour'' policies that had been so disastrous to world trade and economics during the interwar period and which, in the minds of many leaders, were responsible to a great degree for World War II itself'.[6] This led to the establishment of the World Bank and the IMF, and a proposal to establish an International Trade Organisation (ITO). The ITO was to include provisions on investment, but an inability to get US Congressional support led to its abandonment in 1950, leaving the GATT as the surviving multilateral agreement governing trade.[7]

While the establishment of the GATT meant that trade relations were conducted on a multilateral basis, investment remained to be pursued bilaterally. Therefore, after World War II, the US continued to pursue FCNs with stronger investment protection provisions, and these treaties also often included agreement by the parties to resolve disputes before the International Court of Justice (ICJ).

During the 1960s the rise of the Soviet Union and socialism in developing countries, combined with intense nationalism within recently de-colonised states, led to opposition to foreign investment as either an extension of an ideological battle against capitalism, or by viewing foreign investment as a form of neo-colonialism.[8] This ideological opposition was reinforced by the development economics theory, which encouraged import substitution and the building of an industrial base behind high tariff walls as the policy prescription that would allow least developed economies to industrialise.[9]

This opposition to foreign investment led to a number of significant expropriations. For example, in the 1970s Libya nationalised its petroleum industry and Chile nationalised its copper mining industry. Moreover, the 1979 Iranian Revolution led to the expulsion of US companies and the nationalisation of their assets and in early 1980 Kuwait nationalised its petroleum industry.

5 Henry J. Steiner, Detlev F. Vagts and Harold H. Koh, *Transnational Legal Problems: Materials and Text*, 4th edn (Westbury, New York: Foundation Press, 1994), at pp. 456–7.

6 John H. Jackson, *World Trade and the Law of the GATT* (Indianapolis: Bobbs-Merrill Company, 1969), at p. 37. See, however, Robert E. Hudec, *Essays on the Nature of International Trade Law* (London: Cameron May, 1999), at p. 315 (arguing that the experience of the post-World War II era is that 'without the underlying political animosities, discrimination itself seems to have no necessary effect on the peace of the world').

7 Jackson, above n. 6, at p. 50.

8 Kenneth J. Vandevelde, 'A Brief History of International Investment Agreements' (2005) 12(1) *University of California Davis Journal of International Law & Policy* 157–94, at 166.

9 Robert Gilpin, *Global Political Economy: Understanding the International Economic Order* (Princeton: Princeton University Press, 2001), at p. 308.

At the same time, there was also ongoing disagreement over the legal obligations of host States towards foreign investment. This was reflected in the refusal by developed investing States to vote in favour of two UN General Assembly Resolutions. The first Resolution, adopted on 1 May 1974, was the Declaration of the New International Economic Order, recognising state sovereignty over their natural resources, including a right to transfer ownership of these resources to their nationals.[10] On 12 December 1974, the General Assembly adopted the Charter of Economic Rights and Duties of States, affirming a State's right to expropriate and, while recognising an obligation to pay compensation, noting that compensation should be assessed according to the expropriating State's national laws.[11]

As a result of losing all its foreign investment in World War II, West Germany became the first country to commence negotiating BITs in 1959. This was followed closely by other major capital exporting States such as England, France, Italy, Switzerland, The Netherlands and Belgium. By 1980, Europe had negotiated approximately 150 BITs with developing states. The US commenced its own BIT programme in 1981, but by 1990 only eight BITs had been signed and ratified by the US Senate.[12]

The US's BITs differed from the FCN treaties in that they focused solely on investment, they were largely with developing States, and their provisions also reflected the objective that 'investment matters should be regulated by the market rather than political forces'.[13] The same could be said for those BITs entered into by European states. Therefore, the BITs negotiated by Europe and the US sought to depoliticise investment matters by including absolute obligations regarding expropriation, a requirement to provide fair and equitable treatment, and a commitment to allow currency transfers. The attempt to separate foreign investment from foreign policy was assisted by the establishment of the World Bank International Centre for the Settlement of Investment Disputes in 1966, which allowed BITs to also include the right for investors to have their investment disputes settled by international tribunals, thereby avoiding the foreign investor having to rely on diplomatic protection to assert its claim.[14]

The OECD also supported the push by capital exporting states to affirm these international investment obligations by adopting the Code of Liberalisation of Capital Movements and the Code of Liberalisation of Current Invisible Operations

10 Declaration of the Establishment of a New Economic Order, General Assembly Resolution 3201 (S-VI), UN GAOR, 6th Special Session, 2229th Plenary Meeting, UN Doc. A/RES/3201 (S-VI), 1 May 1974.

11 Charter of Economic Rights and Duties of States, General Assembly Resolution 3281 (XXIX), UN GAOR, 29th Session, 2315th Plenary Meeting, UN Doc. A/RES/3281(XXIX), 12 December 1974.

12 Jeswald W. Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (1990) 24 *International Law* 655–75, at 657.

13 Kenneth J. Vandevelde, 'Of Politics and Markets: The Shifting Ideology of the BITS' (1993) 11 *International Tax & Business Law* 159–86, at 182.

14 Christoph H. Schreuer, *The ICSID Convention: A Commentary* (Cambridge: Cambridge University Press, 2001), at pp. 391 and 398.

in 1961. Under these Codes, each OECD country committed itself to liberalise on a non-discriminatory basis, measures that restricted the movement of capital, including, as a result of subsequent amendments to these Codes, measures restricting foreign direct investment.

The international debt crisis in the 1980s revealed the structural challenges developing countries faced when seeking to repay their foreign debt. The perceived need for developing economies to undertake structural reform was mandated by the use of conditional loans from the IMF.[15] These conditions, referred to as the 'Washington Consensus', which included trade liberalisation and opening their economies to competition from the outside world, had an important impact of the receptiveness of developing countries to foreign investment.

The fall of the Berlin Wall in 1989 and the subsequent collapse of the Soviet Union also led to the unravelling of the ideological opposition to capitalism and foreign investment. This caused an increased willingness by States previously opposed to foreign investment or to international investment commitments to sign BITs. As a result, while 400 BITs were concluded between 1959 and 1989, by June 2006 there were 2,506 BITs.[16]

Further, economic development in the developing world, particularly in Asia, resulted in countries that were traditionally importers of capital becoming exporters as well. Therefore, BITs became viewed offensively by a larger number of countries.[17] By the end of 2005, approximately 26 per cent of all BITs were signed between developing countries, meaning developing countries are party to more than 1,100 BITs and FTAs with investment chapters.[18]

Another consequence of the end of the Cold War for foreign investment was that it became possible again to seek to deal with investment multilaterally. While the establishment of the WTO in 1995 did not include comprehensive investment provisions, some investment disciplines were included. For instance, commercial presence for the delivery of services is regulated as a mode 3 discipline under the GATS, and the TRIPS Agreement also includes protections for intellectual property rights, also considered an investment under BITs. The WTO also contains the TRIMS Agreement, which prohibits Members from conditioning foreign investment on compliance with certain export or import conditions.

While the WTO witnessed the re-emergence of some multilateral rules on investment, failure to adopt a comprehensive approach led to the attempt to negotiate a Multilateral Agreement on Investment (MAI). The OECD was chosen as

15 Gilpin, above n. 9, at pp. 314–5.

16 UNCTAD, *International Investment Rule-Setting: Trends, Emerging Issues and Implications*, TD/B/COM.2/73 (5 January 2007), at p. 3.

17 UNCTAD 2006 World Investment Report, *FDI From Developing and Transition Economies: Implications for Development* (New York and Geneva: UN, 2006), at p. 228.

18 *Ibid.* See also, UNCTAD, *Recent Developments in International Investment Agreements*, IIA Monitor No. 2 (2005), UNCTAD/WEB/ITE/IIT/2005/1, at p. 3.

the forum, with the premise being that the negotiation of such an agreement would be easier amongst developed like-minded countries. It was anticipated that the treaty would be open for accession by developing countries.[19] However, negotiations were discontinued in the late 1990s. While disagreement amongst the OECD countries over issues such as culture and labour was already slowing the negotiating process, a confidential draft, released to NGOs in 1997, led to an effective grass roots campaign against the MAI and killed the initiative.[20]

The failure to negotiate an MAI within the OECD led to further attempts to include investment in the WTO. However, even though the Singapore Declaration (1996) established a Working Group on the Relationship between Trade and Investment to consider the scope for multilateral rules on investment,[21] a lack of support amongst WTO members, including from the US, led to its abandonment in the Doha Round.[22]

As is demonstrated throughout this book, slowness in concluding the Doha Round has led to a number of countries pursuing their trade interests through FTAs. The rationale being, in part, that FTAs could be concluded faster than WTO trade negotiations and provide opportunities for countries to make commitments in areas currently not on the WTO agenda, such as investment.

This has led to a rapid growth in the number of FTAs containing investment provisions. In fact, by June 2006, 244 FTAs included investment provisions, with approximately 87 per cent of these agreements having been concluded since the 1990s.[23]

III. Scope of the Investment Chapter

This Part considers the scope of FTA Investment Chapters by inquiring into to whom, and what, an investment chapter applies and focuses on how important terms in an investment chapter are defined. For example, an FTA's definition of an 'investor' determines to whom the investment chapter applies. There are, however, other provisions in an FTA Investment Chapter that affect its scope and which this Part considers. For example, a denial of benefits provision allows a Party to the FTA to avoid having to apply FTA Investment Chapter commitments to particular investors, thereby also affecting the scope of the chapter.

19 Jürgen Kurtz, 'A General Investment Agreement in the WTO? Lessons from Chapter 11 of NAFTA and the OECD Multilateral Agreement on Investment' (2002) 23(4) *University of Pennsylvania Journal of International Economic Law* 713–89.

20 See Michael J. Trebilcock and Robert Howse, *The Regulation of International Trade*, 3rd edn (London: Routledge, 2005), at pp. 457–60 for an overview of the MAI negotiations; see also Kurtz, above n. 19, at 756–61.

21 WTO, 1996 Singapore Ministerial Declaration, WT/MIN(96)/DEC, 13 December 1996, para. 20.

22 WTO General Council Decision of 31 July 2004, WT/GC/W/535, p. 3.

23 UNCTAD, *International Investment Arrangements: Trends and Emerging Issues* (New York and Geneva: UN, 2006), at p. 8; see also UNCTAD, above n. 16, at p. 8.

A. Definition of an investment

1. The 'asset-based' or 'enterprise-based' definition

The definition of an 'investment' is an important determinant of the scope of an FTA Investment Chapter. Most FTA Investment Chapters use an asset-based definition by defining an investment as 'every kind of asset'.[24] However, the definition of an investment as 'every kind of asset' begs the question of what constitutes an 'asset'. Most FTA Investment Chapters assist with this inquiry by providing an open-ended list of the types of assets that are investments.[25] Some FTA Investment Chapters, such as the United States–Chile Free Trade Agreement, Korea–Chile Free Trade Agreement and the Central American–Domican Republic–United States Free Trade Agreement (CAFTA–DR–US), also require that assets have the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit or the assumption of risk.[26]

An alternative approach to the open-ended definition of an investment is to use a comprehensive but finite definition of what constitutes an investment. This is the approach taken in the Draft COMESA Common Investment Area (CCIA) Investment Framework Agreement where, in Article 1.7 paragraphs (a)–(e), there is a specific and finite list of what constitutes an investment.

Still yet, other FTA Investment Chapters, such as the North American Free Trade Agreement (NAFTA) and the Canada–Chile Free Trade Agreement, define an investment using an asset-based and enterprise-based definition. For example, the Canada–Chile FTA defines an investment as including an enterprise, an equity security of an enterprise, or a debt security of an enterprise.

2. Foreign direct investment and portfolio investment

Whether an FTA Investment Chapter covers only foreign direct investment (FDI) or also extends to include portfolio investment is another way that the scope of an Investment Chapter is determined by the definition of an investment. However, FTAs do not define what constitutes portfolio investment or foreign direct investment, reflecting the fact that there is no clear point where the acquisition of an equity interest in a company becomes a direct investment.

24 See, e.g. United States–Chile Free Trade Agreement, Article 10.27; Singapore–Australia Free Trade Agreement, Chapter 8, Article 1.1(c); and India–Singapore Comprehensive Economic Cooperation Agreement (India–Singapore CECA), Article 6.1.1.

25 See, e.g., US–Chile FTA, Article 10.27; and Singapore–Australia FTA, Chapter 8, Article 1.

26 US–Chile FTA, Article 10.27; Korea–Chile FTA, Article 10.1; and CAFTA–DR–US, Article 10.28. See also *Salini Costruttori S.p.A. and Italstrade S.p.A.* v. *Kingdom of Morocco*, ICSID Case No. ARB/00/4, Decision on Jurisdiction (23 July 2001), where the tribunal, interpreting the reference to an 'investment' in ICSID Article 25(1) stated that an investment implies the presence of (a) a contribution of money or other assets of economic value; (b) a certain duration; (c) an element of risk; and (d) a contribution to the host State's development.

Most FTA Investment Chapters cover both FDI and portfolio investment.[27] This coverage is achieved by using an asset-based definition of an investment that lists as an asset, 'shares, stock and other forms of equity participation in an enterprise'.[28] In those FTAs that use an enterprise-based definition of an investment, direct and portfolio investment is covered by defining an investment as including equity in an enterprise.[29]

The European Union–Chile Association Agreement (EU–Chile AA) also includes, in Title III, Chapter III, limited commitments with regards to 'establishment' in the non-services sectors.[30] The definition in this Agreement of 'establishment' would also extend the scope of these commitments to FDI and portfolio investment.

Not all FTAs cover portfolio investment. For instance, the Framework Agreement on the ASEAN Investment Area (AIA) states in the 'scope' part of the AIA, that the Agreement does not cover portfolio investment,[31] while the Thailand–Australia Free Trade Agreement also limits its pre-establishment investment commitments to FDI only.[32]

3. 'Direct' and 'indirect' investment

What constitutes an 'investment' in FTA Investment Chapters is often defined as including assets that are owned or controlled 'directly or indirectly' by the foreign investor.[33] What constitutes direct ownership or control of an investment is an absence of an intermediary between the investment and the investor. Therefore, indirect ownership or control refers to the existence of one or more intermediaries (regardless of nationality) between the investors and the investment.[34] As a result, an investment in the territory of an FTA Party can be owned or controlled by investors of the other FTA Party through investments established in third countries that are not party to the FTA.

Finally, the ability for an investment to be owned or controlled, directly or indirectly, also allows for the existence of more than one owner or controller of an investment.[35] For example, an investment could be directly owned or controlled by Company A as well as being owned or controlled by Company B through Company A.

4. Ownership and control

In most FTAs, ownership or control is left undefined.[36] This largely reflects the difficulty of providing definitions of ownership and control that do not lead to an

27 See the Canada–Chile FTA, Article G-40; Japan–Singapore New-Age Economic Partnership Agreement (Japan–Singapore EPA), Article 72; India–Singapore CECA, Article 6.1.1; Korea–Singapore FTA, Article 10.1; and US–Chile FTA, Article 10.27.

28 US–Singapore FTA, Article 15.1.13(a). 29 See, e.g., Canada–Chile FTA, Article G-40.

30 The EU–Chile AA also includes commitments on mode 3 services in the Services Chapter.

31 AIA Framework Agreement, Article 2. 32 Thailand–Australia FTA, Article 903.

33 See, e.g., Japan–Singapore EPA, Article 72; and US–Chile FTA, Article 10.27.

34 *Aguas del Tunari S.A.* v. *Republic of Bolivia*, ICSID Case No. ARB/02/3, Decision on Respondent's Objections to Jurisdiction, para. 236.

35 *Ibid.*, para. 237. 36 See, e.g., US–Chile FTA and the Korea–Singapore FTA.

over- or under-inclusion of investments within their scope.[37] However, some FTAs provide guidance to treaty interpreters on how to define ownership or control. For example, the Japan–Singapore New-Age Economic Partnership Agreement (Japan–Singapore EPA) and Thailand–Australia FTA define ownership as 50 per cent of the equity interest of an enterprise, and control as 'the power to name a majority of its [the enterprise's] directors or otherwise to legally direct its actions'.[38]

The issue of whether an investment is owned or controlled normally arises when the investment is an enterprise rather than, for example, the equity in that investment. This is because in the case of equity, ownership is easily established. However, whether the possession of say 25 per cent equity in an enterprise constitutes control of that enterprise is a more ambiguous proposition. Therefore, even where FTAs do define control, definitions are broad and serve more as directions than bright lines. This approach has also been followed by arbitral tribunals, who have defined control broadly by finding that whether a minority shareholder controls an enterprise requires an inquiry into 'legal rights conveyed in instruments or agreements such as the articles of incorporation or shareholders' agreement or a combination of these'.[39]

B. Definition of an investor

The definition of what constitutes an investor also determines the scope of an FTA Investment Chapter. This is because this definition determines not only who falls within the scope of the investment chapter commitments, but will also determine whether the substantive investment chapter commitments apply to the pre- and post-establishment phase of an investment, or to the post-establishment phase only.

1. An investor as a 'natural person'

Most FTA Investment Chapters define an investor as both a natural person and an enterprise or juridical person.[40] These FTAs define a natural person as a citizen or national of a Party, and the laws of that Party regarding citizenship and nationality define whether a person is in fact a citizen or national. For example, according to Annex 2.1 of the US–Chile FTA, a Chilean is to be determined according to Article 10 of the Constitucion Politica de la Republica, and a US citizen is defined according to the existing provisions of the US Immigration and Nationality Act.

37 *Aguas del Tunari S.A.* v. *Republic of Bolivia*, para. 246.

38 Japan–Singapore EPA, Article 72; and Thailand–Australia FTA, Article 103(o).

39 *Aguas del Tunari S.A.* v. *Republic of Bolivia*, para. 264.

40 See AUSFTA, Article 11.17; US–Chile FTA, Article 10.27; Canada–Chile FTA, Article G-40; and Japan–Singapore EPA, Article 72.

Furthermore, most FTAs broaden the scope of a 'natural person' to include permanent residents.[41] Interestingly, in the Japan–Singapore EPA, Singapore extends the definition of an investor to include a permanent resident, while Japan limits the definition to its citizens.[42]

A related issue is how the FTA should deal with dual citizens. There are two main approaches to this issue. The first is to define citizenship broadly, thereby including those persons with dual citizenship.[43] An alternative approach is to limit the scope of the FTA by requiring dual citizens to establish residency,[44] or in a similar vein, to limit citizenship to their dominant and effective nationality.[45]

2. An investor as an 'enterprise'

Most FTA Investment Chapters also define an investor as an enterprise and use the 'place of incorporation' to establish whether the enterprise is an investor of an FTA Party.[46] For example, the US–Chile FTA defines an enterprise, *inter alia*, as 'any entity constituted or organized under applicable law ... including a branch of an enterprise'.[47]

Many FTA Investment Chapters also include a branch of an enterprise within the definition of an enterprise. For example, the US–Chile FTA, Australia–United States Free Trade Agreement (AUSFTA) and Canada–Chile FTA include within the Investment Chapter a definition of an enterprise that draws on the definition of an enterprise in the 'general definition' part of the FTA, and extends the definition, for the purposes of the investment chapter, to include 'a branch of an enterprise'.

However, in these FTAs, the Investment Chapter also qualifies the extent that a branch of an enterprise will be an enterprise for the purposes of the FTA. This is done by defining 'an enterprise of a Party' as only applying to 'a branch located in the territory of a Party and carrying out business activities there'.[48] Or in the case of the India–Singapore Comprehensive Economic Co-operation Agreement (India–Singapore CECA), an enterprise does not include 'any legal entity, which is established and located in the territory of a Party with negligible or nil business operations or with no real and continuous business activities carried out in the territory of that Party'.[49]

41 See, e.g., Australia–United States Free Trade Agreement AUSFTA, Article 1.1 and Annex 1-A; CAFTA–DR–US, Article 2.1 and Annex 2.1; Canada–Chile FTA, Article B-01; Korea–Singapore FTA, Chapter 2; and Korea–Chile FTA, Article 2.1.

42 Japan–Singapore EPA, Article 72(f).

43 See, e.g., Korea–Singapore FTA, Chapter 2; India–Singapore CECA, Article 6.1, para. 5; and Canada–Chile FTA, Article B-01.

44 Japan–Singapore EPA, Article 72(f).

45 US–Chile FTA, Article, 10.27; and AUSFTA, Article 11.17.6.

46 See, e.g., Canada–Chile FTA, Article B-01; and Korea–Singapore FTA, Chapter 2.

47 US–Chile FTA, Articles 2.1 and 10.27.

48 US–Chile FTA, Article 10.27; AUSFTA, Article 11.17.2; and Canada–Chile FTA, Article G-40.

49 India–Singapore CECA, Article 6.1.6.

C. Pre- and/or post-establishment investment

Another important issue affecting the scope of an FTA Investment Chapter is whether its commitments cover measures that apply to the post-establishment stage of an investment, or extend to measures that affect the pre-establishment investment stage. A measure that applies to the pre-establishment stage of an investment limits the ability of an investor from the other FTA Party to make an investment in its territory. This would include, for example, a measure adopted by one FTA Party that prohibits an investor from the other FTA Party from investing in a particular sector. A measure that applies to the post-establishment stage affects an FTA Party's investor or its investment once established in the territory of the other FTA Party. For example, a measure that requires an investment of an FTA Party to employ local staff would constitute a measure affecting the post-establishment stage of an investment.

All FTA Investment Chapters apply to measures that affect the post-establishment phase of an investment. However, not all FTA Investment Chapters apply to measures that affect the pre-establishment investment stage.[50] Whether an FTA Investment Chapter applies to pre-establishment measures is determined in the definition of an investor of a Party by the phrase 'that attempts to make',[51] or 'seeks to make'.[52] In the case of the Korea–Chile FTA, it is determined by the phrase 'that makes a juridical act in the territory of the other Party towards materializing an investment within it'.[53]

Even where Parties choose to define an investor in a manner that extends the scope of the FTA Investment Chapter to measures that affect pre- and post-establishment investments, only a limited number of the substantive commitments in the Investment Chapter will apply to the pre-establishment investment phase. In particular, the commitments to provide NT and MFN treatment, and on performance requirements, are the main substantive provisions in FTA Investment Chapters that apply to measures that affect the pre- and post-establishment phase of an investment, and even these can be limited to measures that affect post-establishment investments.

Whether a substantive commitment applies to pre-establishment measures is determined in the NT commitment for example, by the phrase 'establishment, acquisition, expansion' of an investment.[54] This can be contrasted with the Thailand–Australia FTA, where the application of the NT commitment to only the

50 See, e.g., Singapore–Australia FTA, Chapter 8, Article 1; AUSFTA, Article 11.17.5; and Japan–Singapore EPA, Article 72(c).

51 See, e.g., Canada–Chile FTA, Article G-40; and US–Chile FTA, Article 10.27.

52 See, e.g., Korea–Singapore FTA, Article 10.1; and Thailand–Australia FTA, Article 1(m).

53 Korea–Chile FTA, Article 10.1.

54 See, e.g., NAFTA, Article 1102.1; US–Chile FTA, Article 10.2; Canada–Chile FTA, Article G-02.1; and Singapore–Australia FTA, Chapter 8, Article 3.

'management, conduct, operation and sale or other disposition of investments', limits it to post-establishment matters only.[55]

Further, some FTAs include pre-establishment commitments for limited sectors, while maintaining a broader post-establishment commitment for a broader range of sectors. For example, the India–Singapore CECA Investment Chapter divides the NT commitment into two separate paragraphs, one dealing with the 'establishment, acquisition or expansion' of investments, namely, a pre-establishment commitment, and the other with the management, conduct, operation, liquidation, sale and transfer, namely, a post-establishment commitment.[56]

D. Denial of benefits

A denial of benefits provision affects the scope of a FTA Investment Chapter by giving a Party a right to deny the benefits of the Investment Chapter to an investor of the other Party. For example, a number of FTA Investment Chapters allow the Parties to exclude from the scope of the FTA Investment Chapter investors of the other Party that are enterprises owned or controlled by investors from non-Parties and/or the denying Party and where the enterprise was established for the sole purpose of being used as a vehicle for getting the benefits of the FTA Investment Chapter when making an investment into the territory of the other FTA Party.[57]

These FTAs achieve this by requiring, as a condition for falling within the scope of the FTA Investment Chapter, that these enterprises have 'substantial' or 'substantive' business activities in the territory of a FTA Party.[58] What constitutes a 'substantive' or 'substantial' business presence is undefined in these FTAs. However, in light of the objective of these provisions, a 'substantial' or 'substantive' business presence should require enough activity to outweigh the incentive created by the FTA for investors of a non-Party, or the denying Party, to invest in an FTA Party solely for the purposes of falling within the scope of an FTA Investment Chapter's protections when making an investment in the territory of the other FTA Party.

IV. The substantive commitments in an FTA investment chapter

Part IV analyses the main substantive commitments normally found in an FTA Investment Chapter and considers how arbitral tribunals have interpreted these commitments in BITs and under NAFTA.

55 Thailand–Australia FTA, Article 906(b). 56 India–Singapore CECA, Article 6.3.

57 See, e.g., US–Chile FTA, Article 10.11; Canada–Chile FTA, Article G-13.2; Singapore–Australia Free Trade Agreement, Chapter 8, Article 18; and AUSFTA, Article 11.12. See also Japan–Singapore EPA, Article 72 (a)(h), which excludes from the definition of an enterprise of a Party, 'an enterprise owned or controlled by persons of non-Parties and not engaging in substantive business operations in the territory of the other party'.

58 Singapore–Australia FTA, Chapter 8, Article 18, refers to 'substantive business operations', whereas the phrase 'substantial business activities' is used in US–Chile FTA, Article 10.11; AUSFTA, Article 11.12; and Canada–Chile FTA, Article G-13.

A. National treatment

The non-discrimination norm that underpins the multilateral trading system is an important pillar of FTA Investment Chapters. In the WTO context, the non-discrimination norm is reflected in numerous provisions, most famously in the Article I MFN provision and Article III NT provisions of the GATT. However, Article XX of the GATT, Article III, XIV and XVII of the GATS and Articles III and IV of the TRIPS Agreement also include prohibitions on discrimination.

The prohibition on discrimination in WTO rules is largely justified by economic welfare arguments that discrimination creates an inefficient allocation of resources and therefore reduces member State welfare.[59]

Any allegation that a measure is inconsistent with a State's FTA Investment Chapter NT commitment usually requires consideration of three main issues. First, whether the foreign and domestic investors and/or their investments are in 'like circumstances'? Second, whether the foreign investor/investment has received less favourable treatment than the domestic investor/investment that is in like circumstances? And third, whether there is a legitimate government policy that justifies treating the investment/investor as not being in like circumstances?[60]

1. Is the domestic and foreign investor/investment in 'like circumstances'?

Similar to the WTO context, the NT obligation in an FTA Investment Chapter requires that the domestic and foreign investor/investment be in 'like circumstances' before differences in treatment can be deemed discriminatory.[61] Other FTA Investment Chapters uses the phrase 'like economic activity',[62] while some do not use any comparator at all.[63]

The phrase 'like circumstances' is also used in the NT obligation in Article XVII of GATS and the phrase 'like products' is used in the NT commitment in Article III of the GATT. These phrases all perform a similar function, namely, to limit the obligation to situations were the investors are properly compared. The prohibition on discrimination, whether in an FTA investment chapter or in the WTO, is the flipside of a positive obligation to treat like foreign and domestic investors and their

59 Hudec, above n. 6, at pp. 284–8; see Robert Howse, 'The Legitimacy of the WTO', in Jean-Marc Coicaud and Veijo Heiskanen (eds.), *The Legitimacy of International Organizations* (New York & Tokyo: UN University Press, 2001), pp. 355–407, for an explanation of the limits of the economic welfare case for legitimising the WTO.

60 NAFTA Ch 11 Arbitral Tribunal, *SD Myers Inc.* v. *Government of Canada* ('*Myers* v. *Canada*') (Award of 10 April 2001), para. 250; and NAFTA Ch 11 Arbitral Tribunal, *Pope & Talbot Inc* v. *Government of Canada* ('*Pope & Talbot*') (Award on the Merits of Phase 2, 10 April 2001), para. 78.

61 See AUSFTA, Article 11.3; CAFTA–DR–US, Article 10.3; Canada–Chile FTA, Article G-02.1; Korea–Chile FTA, Article 10.3; Japan–Singapore EPA, Article 73; and India–Singapore CECA, Article 6.3.

62 EU–Chile AA, Title III, Chapter III, Article 132.

63 Draft CCIA Investment Framework Agreement, Article 8.

investments equally. Or, in other words, discrimination occurs when equally situated persons are treated differently.[64]

The phrase 'like circumstances' therefore refers to a standard against which we can assess whether in fact the foreign and domestic investors are equally situated. Once established that a foreign and domestic investor/investment are in 'like circumstances', we can conclude that the less favourable treatment being accorded to the foreign investor, compared with the like domestic investor, constitutes discrimination.[65]

The phrase 'like circumstances' has been interpreted by a number of NAFTA tribunals by drawing on the approach taken to the phrase 'like products' in Article III of the GATT.[66] NAFTA tribunals have also found that the existence of an exceptions provision in Article XX of the GATT, and the absence of an exceptions provision to the NAFTA Investment Chapters, creates a 'legal context' that justifies a particular interpretation of the phrase 'like circumstances' in Article 1102 of the NAFTA.[67]

However, in the recent decision of *Methanex Corp.* v. *United States, Decision of the Tribunal on Petitions from Third Persons to Intervene as 'Amici Curiae'*,[68] the tribunal questioned this approach of using WTO Appellate Body decisions regarding Article III of the GATT to interpret NAFTA Investment Chapter provisions.[69] Nevertheless, in order to understand the approaches that NAFTA tribunals have taken to the NT commitment in NAFTA, it is helpful to briefly describe the approach that the WTO Appellate Body has taken to the GATT NT commitment.

As a general matter, the burden of proof is on the complaining WTO member to establish a *prima facie* case that the impugned measure is inconsistent with the NT commitment in Article III of the GATT. Article III:2 of the GATT disciplines internal taxes or internal charges of any kind, while Article III:4 of the GATT applies to 'all laws regulations, and requirements affecting the products' internal sale'.

Article III.2 of the GATT first sentence and Article III.4 of the GATT both refer to 'like products', however, the WTO Appellate Body has interpreted the scope of these

64 See Julia Ya Qin, 'Defining Nondiscrimination Under The Law Of The World Trade Organization' (2005) 23(2) *Boston University International Law Journal* 215–97, at 224, for a discussion of the concept of equality.

65 See Robert E. Hudec, 'GATT/WTO Constraints on National Regulation: Requiem for an "Aim and Effects" Test' (1998) 32 *The International Lawyer* 619–49, at 623, where Hudec observes that, '[f]or a regulatory measure to produce any difference in treatment at all, the regulation must divide products subject to the regulation into two or more categories. The finding of discrimination ultimately rests on a finding that the product distinction is illegitimate'.

66 The reference by Arbitral tribunals to WTO jurisprudence on GATT Article III rather than GATS Article XVII reflects the limited number of WTO cases that have addressed this GATS commitment.

67 *Myers* v. *Canada*, para. 245.

68 NAFTA Ch 11 Arbitral Tribunal, *Methanex Corp.* v. *United States, Decision of the Tribunal on Petitions from Third Persons to Intervene as 'Amici Curiae'* ('*Methanex*') (15 January 2001).

69 *Ibid.*, Part IV, Chapter B, p. 19; however, see *United Parcel Service of America, Inc.* v. *Govt of Canada*, separate statement of Dean Ronald A. Cacc, para. 57, where he observes that: '[t]he wording of Article 1102 suggests a very close parallel to the national treatment obligations contained in the GATT and the GATS, as well as other international trade and investment agreements and treaties.'

phrases differently. With regards to the first sentence of Article III.2 of the GATT, the Appellate Body has used a narrow understanding of 'like products' by focusing on the physical characteristics of the products, its tariff classification, end-uses in the given market and consumer's tastes and habits.[70] In contrast, the Appellate Body has given the phrase 'like products' in Article III:4 of the GATT a broader meaning, as extending to products that are competitive and/or substitutable.[71]

Another important element in Article III of the GATT is the role of Article III.1 and its statement of the general principle that measures 'should not be applied to imported or domestic products so as to afford protection to domestic production', and the role that this paragraph plays in assessing whether two products are 'like products'.[72] The Appellate Body has found that the reference in the second sentence of Article III.2 of the GATT to GATT Article III.1, and its ad Note, requires a party to establish that 'the dissimilar taxation of the directly competitive or substitutable imported domestic products ''is applied so as to afford protection to domestic production'''.[73] However, whether a tax has been applied so as to afford protection does not require an assessment of the subjective intentions of the legislators. Instead, the Appellate Body will look at 'the statutory purposes or objectives – that is, the purpose or objectives of a Member's legislature and government as a whole – to the extent that they are given objective expression in the statute itself'.[74]

In contrast, due to the absence of a specific reference to Article III.1 in Article III.2, first sentence, and Article III.4 of the GATT, the presence of protection application does not need to be separately established.[75] However, the Appellate Body has made it clear that Article III.1 informs and provides important context for interpreting all of Article III, including Article III.4.[76] This means that the phrase 'like products' must be interpreted to give effect to the Article III.1 general principle.[77]

Should a measure be found to violate Article III, then a member State can seek to justify the measure under Article XX of the GATT. Under the subparagraphs in Article XX (a) to (j), 'the legitimacy of the declared policy objective of the measure, and the relationship of that objective with the measure itself and its general design

70 See, e.g., Appellate Body Report, *Japan–Alcoholic Beverages*, p. 20.

71 Appellate Body Report, *EC–Asbestos*, paras. 96 and 99. 72 *Ibid.*, para. 98.

73 Appellate Body Report, *Japan–Alcoholic Beverages*, p. 27

74 Appellate Body Report, *Chile–Alcoholic Beverages*, para. 62. See Donald H. Regan, 'Further Thoughts on the Role of Regulatory Purpose Under Article III of the General Agreement on Tariffs and Trade' (2003) 37(5) *Journal of World Trade* 737–60, at 741, where he states that: 'The *Chile* Appellate Body makes explicit the further point, which was always just below the surface in the *Japan* report, that the bridge between the design, architecture and structure on the one hand and a finding of illegality on the other hand, is a finding, based on design, architecture and structure, of protectionist purpose'. See also Hudec, above n. 65, at 631, who argues that the role of 'protective application' in *Japan–Alcoholic Beverages* is really an inquiry into purpose.

75 Appellate Body Report, *Japan–Alcoholic Beverages*, pp. 18–19; Appellate Body Report, *EC–Bananas III*, para. 216; and Appellate Body Report, *EC–Asbestos*, para. 98.

76 Appellate Body Report, *EC–Asbestos*, para. 93. 77 *Ibid.*, para. 98.

and structure, are examined'.[78] There is also the added requirement that the measure pass the tests in the chapeau to Article XX, which includes the requirement that the measure not be applied in a manner that would constitute arbitrary or unjustifiable discrimination between countries where the same conditions prevail.[79]

As noted, NAFTA tribunals, when interpreting Article 1102 of the NAFTA, have drawn on the WTO Appellate Body's interpretation of Article III of the GATT. They have done this by condensing the two-step analysis under the GATT (i.e., assessing whether the measure is consistent with Article III and if not, seeing whether the measure can be justified under Article XX of the GATT) into a two-step analysis under the single Article 1102 NT provision of the NAFTA.

Under the first step, for the tribunals in *Myers* v. *Canada* and *Pope & Talbot Inc.* v. *Government of Canada*, foreign and domestic investors/investments are in 'like circumstances' when they are in the same 'sector' as the national investor, where 'sector' includes the concepts of 'economic sector' and 'business sector'.[80] In *United Parcel Service of America* v. *Government of Canada*, the tribunal inquired into whether UPS was 'competing in the same market for the same market share' as Canada Post.[81] However, the tribunal in *Methanex* stated that 'it would be perverse to ignore identical comparators if they were available and to use comparators that were less ''like''', thereby narrowing the 'like circumstances' inquiry.[82]

This approach of these tribunals, while at first glance appealing, ultimately provides no criteria against which we can assess whether two investments are in 'like circumstances'. For example, is a foreign and domestic investment that produces an identical product in 'like circumstances' if the foreign investment uses an environmentally harmful production process, while the domestic investment uses a production process that does not harm the environment?[83]

This approach by the tribunal in *Methanex* into what constitutes 'like circumstances' needs to also be seen in light of its interpretation of the phrase

78 Appellate Body Report, *US–Shrimp*, para. 149.

79 *Ibid.*, para. 160. 80 *Myers* v. *Canada*, para. 250; and *Pope & Talbot*, para. 78.

81 NAFTA Ch 11 Arbitral Award, *United Parcel Service of America* v. *Government of Canada*, (*'UPS'*) Award on the Merits of the Arbitral Tribunal, 24 May 2007, para. 83.

82 *Methanex*, Part IV, Chapter B, p. 8; see also *Feldman*, Final Award 16 December 2002, para. 171.

83 See Donald H. Regan, 'Regulatory Purpose and ''Like Products'' in Article III.4 of the GATT (With Additional Remarks on Article III:2)' (2002) 36(3) *Journal of World Trade* 443–78, at 447, where he observes with regard to the 'like products' phrase in GATT Article III that, 'in order to have a usable conception of ''likeness'' we need to know which properties matter. We need an answer to the question, ''Like in what respects?'''. See also Henrik Horn and Joseph H.H. Weiler, 'EC Measures Affecting Asbestos and Asbestos-Containing Products' (2004) 3(1) *World Trade Review* 129–51, at 138–41, for an analysis of a 'methodology' where what constitutes 'likeness' is not necessarily determined by the market. See also Fernando Gonzalez Rojas, *The Notion of Discrimination in Article 1102 of NAFTA*, Jean Monnet Working Paper No. 05/05 (New York University School of Law, Spring 2005), at p. 15, where he argues that when tribunals define 'like circumstances' broadly that the 'ultimate ''filter'' to distinguish between lawful and legitimate measures will reside not in the like circumstances analysis, but in the capacity of the Parties to demonstrate that their measures are not *motivated* by the investors' nationality'.

'relating to' in Article 1101 of the NAFTA, which defines the scope of the chapter. Here the *Methanex* tribunal read the phrase 'relating to' as requiring an inquiry into the intent of the Californian legislature when enacting the measure.

This inquiry by the *Methanex* tribunal into the intent of the Californian legislator can be contrasted with the Appellate Body's approach to Article III of the GATT. As noted above, while the Appellate Body rejected an explicit inquiry into the legislator's purpose under Article III.2 first sentence and Article III.4, commentators have argued that the focus of the Appellate Body on whether two products are in a competitive relationship is a necessary, but not sufficient, condition for determining whether two products are alike.[84] Similarly, others have argued that the Appellate Body applies a 'smell test' 'to know whether the measure has a bona fide regulatory purpose and to what extent its market effects are protective'.[85]

Therefore, the *Methanex* tribunal's inquiry into the intent of the Government under Article 1101 may avoid the need, under the 'like circumstances' inquiry, to engage in a 'smell test' – to assesses whether the comparator chosen by the Government can be justified by a government policy other than discrimination based on the investor's nationality.

2. Is there less favourable treatment?

Tribunals have established that the requirement of no less favourable treatment in Article 1102 of the NAFTA means treatment that is 'equivalent to, not better or worse than, the best treatment accorded to the comparator'.[86] FTAs between the US–Chile, US–Singapore, CAFTA–DR–US and the India–Singapore CECA use the legally equivalent phrase 'treatment no less favourable'.[87]

Once a tribunal has established the best treatment against which the treatment accorded to the foreign investor/investment is to be assessed, it needs to be determined whether there is a *de minimis* level of less favourable treatment below which a violation will not arise.

In the WTO context, Article III.2, first sentence, requires that taxes not be applied to imported goods that are 'in excess' of those applied to like domestic goods. The Appellate Body has interpreted the phrase 'in excess of' as not requiring a *de minimis* level of dissimilar taxation.[88] Article III.4, however, adopts a similar approach to FTA Investment Chapters by requiring each WTO member to accord '*treatment no less favourable* than that accorded to like products of national origin (emphasis added).' The Appellate Body has observed that 'whether or not imported products are treated ''less favourably'' than like domestic products should be assessed by examining whether a

84 See Regan, above n. 83, at 445. 85 Hudec, above n. 6, at 634–5.

86 *Myers* v. *Canada*, para. 42; *Pope & Talbot*, paras. 41–2; and *Methanex*, Part IV, Chapter B, para. 21.

87 US–Chile FTA, Article 10.2; US–Singapore FTA, Article 15.4; CAFTA–DR–US, Article 10.3; and India–Singapore CECA, Article 6.3.

88 Appellate Body Report, *Japan–Alcoholic Beverages*, p. 23.

measure modifies the *conditions of competition* in the relevant market to the detriment of imported products'.[89] Therefore, formally different treatment accorded to two products will not, in and of itself, establish less favourable treatment, unless this treatment modifies the conditions of competition in favour of the domestic good.[90]

In the investment context, one tribunal has referred to the need for a 'disproportionate benefit for nationals over non-nationals'.[91] However, the tribunal in *Pope & Talbot* appeared to find that any differences in treatment would violate NAFTA's national treatment commitment.[92]

Finally, the relationship between the 'like circumstances' test and the level of less favourable treatment required, remains unclear, particularly in light of the inquiry by *Methanex* into the intent of the measure under Article 1101 of the NAFTA. Recalling that *Methanex* left open the possibility that the phrase 'like circumstances' could include identically situated domestic and foreign investors/investments, or be stretched to include investors/investments that are less identical, it remains an open question whether a tribunal will require a greater amount of less favourable treatment when the investors/investments are in the same sector than when they are identically situated, and whether, for instance, evidence of discriminatory intent could lead to an NT violation in the absence of a *de minimis* level of less favourable treatment.[93]

3. The search for a legitimate government policy

Some FTA Investment Chapters include an exceptions provision modelled on either Article XX of the GATT or Article XIV of the GATS.[94] Other FTAs do not apply an exceptions provision to the FTA Investment Chapter.[95] Tribunals have dealt with the absence of an exceptions provision by undertaking a second step in the 'like circumstances' analysis by finding that less favourable treatment accorded to foreign investors/investments than domestic investments/investors in the pursuit of legitimate policy goals can be justified on the grounds that these investors/investments are not in 'like circumstances'.

For example, in *Myers* v. *Canada*, the tribunal quotes with approval the OECD Declaration on International and Multinational Enterprises 1976 and the review by the OECD in 1993, to conclude that:

> the assessment of 'like circumstances' in Article 1102 must take into account the general principles that emerge from the legal context of the NAFTA, including both its concern with the environment and the need to avoid trade

89 Appellate Body Report, *Korea–Beef*, para. 137. 90 *Ibid*., para. 144.
91 *Myers* v. *Canada*, para. 252. 92 *Pope & Talbot*, para. 78. 93 Rojas, above n. 83, at p. 45.
94 See, e.g., India–Singapore CECA, Article 6.11; Singapore–Australia FTA, Chapter 8, Article 19; Korea–Singapore FTA, Article 21.2; and Japan–Singapore EPA, Article 83.
95 See, e.g., CAFTA–DR–US, Article 21.1; Korea–Chile FTA, Article 20.1; Canada–Chile FTA, Article O-01; and AUSFTA, Article 22.1.

> distortions that are not justified by environmental concerns. The assessment of 'like circumstances' must also take into account circumstances that would justify governmental regulations that treat them differently in order to protect the public interest.[96]

Therefore, under this approach, the existence of a legitimate policy would result in a finding that the domestic and foreign investor/investment are not in like circumstances. In contrast, where an FTA Investment Chapter includes an exception provision, a finding that the domestic and foreign investor/investment are not in like circumstances and that the foreign investor is receiving less favourable treatment than the like domestic investor/investment, would need to be established before this inquiry into a legitimate government policy would arise.

Understanding the concept of 'like circumstances' in this manner has also presented tribunals with the need to determine what constitutes a legitimate government regulation. A natural starting point is Article XX of the GATT. However, there is also nothing to suggest that what constitutes a legitimate government regulation should be limited by that list.[97]

We therefore observe tribunals drawing from Article XX by referring to legitimate policy goals as including the public interest,[98] and protection of the environment.[99] However, the *Pope & Talbot* tribunal seemed to dispense with the need for an exclusive list of legitimate policy goals and instead reframed the inquiry into whether the measure relates to any 'rational government policy'.[100]

NAFTA tribunals have also addressed the applicable relationship of the measure to the policy goal. For instance, the tribunal in *Pope & Talbot* stated that it will require a 'reasonable nexus' between the structure and design of the measure and the goal of the measure.[101] In the later case of *Marvin Roy Feldman Karpa (CEMSA)* v. *United Mexican States*, the tribunal explained that where less favourable treatment has been shown, the onus is then on the defendant to show that there is a 'rational justification' for the less favourable treatment.[102] This can be contrasted to use in Article XX of the GATT of the phrases 'relating to' and 'necessary to' to connote different relationships between the measure and the policy goal. Here, the Appellate Body has held that a 'relating to' requires only a 'rational connection' between the measure and the policy goal, whereas, a

96 *Myers* v. *Canada*, para. 250.

97 See Henrik Horn and Petros C. Mavroidis, 'Still Hazy After All These Years: The Interpretation of National Treatment in the GATT/WTO Case-Law on Tax Discrimination' (2004) 15(1) *European Journal of International Law* 39–69; see also Hudec, above n. 65, at 622, who observes that GATT 'Article XX imposes rather severe limitations on this type of regulatory justification'; however, see also Tania Voon, *Cultural Products and the World Trade Organization* (Cambridge: Cambridge University Press, 2007), at pp. 9–11, where the author outlines the argument that GATT Article XX is not a closed list.

98 *Myers v. Canada*, para. 250. 99 *Ibid.*, para. 250. 100 *Pope & Talbot*, para. 98.

101 *Ibid.*, para. 98

102 NAFTA Ch 11 Arbitral Tribunal, *Marvin Roy Feldman Karpa (CEMSA)* v. *United Mexican States ('Feldman')* (Award of 16 December 2002), paras. 181–2.

measure is 'necessary' when there is no alternative measure less inconsistent with the GATT that the Member could reasonably be expected to employ.[103]

Finally, while NAFTA tribunals have sought to address the absence of a list of exceptions to the Investment Chapter, there remains the issue of the operation of a GATT Article XX- or GATS Article XIV- type chapeau. Both contain the discipline that measures not 'be applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where like conditions prevail, or a disguised restriction on international trade'.[104] The WTO Appellate Body has interpreted the chapeau as embodying:

> the recognition on the part of WTO Members of the need to maintain a balance of rights and obligations between the right of a Member to invoke one or other of the exceptions of Article XX specified in paragraphs (a) to (j), on the one hand, and the substantive rights of the other members under the GATT 1994, on the other hand.[105]

Therefore, in those FTAs that are without an exceptions provision, the absence of a chapeau to discipline discrimination in the application, rather than the design of a measure, means that a measure deemed consistent with some FTA Investment Chapters NT commitments could be found to be inconsistent with the same NT provision in FTAs where the measure is also assessed through the disciplines of an exceptions provision's chapeau.[106]

B. Most-favoured-nation treatment

There is an efficiency rationale for including an MFN provision in Investment Chapters in FTAs.[107] An MFN clause in an FTA investment chapter avoids the privileges accorded under the FTA being eroded when one of the FTA parties offers better concessions in future FTAs. Or in other words, an MFN clause seeks to at least ensure equality of competitive opportunities between foreign investors and their investments.

103 Appellate Body Report, *EC–Asbestos*, paras. 170–2; see also GATT Panel Report, *Thailand–Cigarettes*, para. 75.

104 GATS Article XIV refers to 'services' instead of 'international trade'.

105 Appellate Body Report, *US–Shrimp*, para. 156; see also Robert Howse, 'The Appellate Body Ruling in the Shrimp/Turtle Case: A New Legal Baseline for the Trade and Environment Debate' (2002) 27(2) *Columbia Journal of Environmental Law* 491–521, at 503.

106 Note that in those FTA Investment Chapters that do not include an exceptions provision, the commitment of performance requirements includes an inbuilt list of exceptions, including a GATT Article XX-style chapeau.

107 Hudec, above n. 6, at pp. 284–8. However, see Jurgen Kurtz, 'The MFN Standard and Foreign Investment – An Uneasy Fit?' (2005) 5(6) *Journal of World Investment and Trade* 861–86, at 867, who argues that in contrast to the GATT MFN clause an MFN provision in an FTA Investment Chapter will also apply to behind-the-border measures. Therefore, the argument that MFN provisions in FTA Investment Chapters are necessarily welfare enhancing is harder to establish than in the trade context.

An MFN clause, however, can lead to a form of moral hazard by creating an incentive for a State to make only minimal investment protections and liberalisation commitments in order to free-ride off any more favourable commitments the other FTA Party may offer under future FTAs.[108] Therefore, the decision whether to include an MFN clause also reflects one FTA Party's satisfaction with the level of commitments undertaken by the other FTA Party and the likelihood of making more favourable commitments under a future FTA that would undermine the preferential treatment granted in that FTA.[109]

As a result of these factors, a number of FTA Investment Chapters, such as the Korea–Singapore Free Trade Agreement, India–Singapore CECA and the Japan–Singapore EPA, include NT provisions but opted against including MFN provisions. In contrast, NAFTA, AUSFTA, US–Chile FTA, US–Singapore FTA, Korea–Chile FTA, Canada–Chile FTA and CAFTA–DR–US, all include NT and MFN clauses. The Draft CCIA Investment Framework Agreement and the AIA Framework Agreement also include MFN clauses, however, these only apply to investors and investments of parties to these agreements.

1. *Ejusdem generis* – the scope of an MFN clause

The principle of *ejusdem generis* refers to the rule that the scope of the MFN clause is to be determined by the subject matter to which it refers. This principle is reflected in Article 9 of the International Law Commission (ILC) Draft Article on Most-Favoured-Nation Clauses 1978, which states that '[u]nder a most-favoured-nation clause the beneficiary State acquires, for itself or for the benefit of persons or things in a determined relationship with it, only those rights which fall within the limits of the subject matter of the clause'.[110] The ILC commentaries to this Article, referring to the *Anglo-Iranian Oil Company Case*, describe the rationale for this principle as resting on the common intention of the parties – 'that the clause can only operate in regard to the subject matter which the two States had in mind when they inserted the clause in their treaty'.[111]

The subject matter of MFN clauses in an FTA Investment Chapter therefore refers to the range of more favourable treatment that one FTA Party can accord to a third Party and which then must also be extended to the other FTA Party.

108 Warren F. Schwartz and Alan O. Sykes, 'The Economics of the Most-Favoured-Nation Clause', in Jagdeep S. Bhandari and Alan O. Sykes (eds.), *Economic Dimension in International Law: Comparative and Empirical Perspectives* (Cambridge: Cambridge University Press, 1997), at p. 59.

109 See Hudec, above n. 6, at p. 307, where he observes that under the treaty system governing trade in the period 1860–1914, that 'almost every tariff agreement was exposed to the risk of having its value undercut by significant discriminatory concessions made to other parties in subsequent negotiations'.

110 *Yearbook of the International Law Commission*, 1978, vol. II, Pt Two, p. 27.

111 *Anglo-Iranian Oil Company Case (Jurisdiction)*, The Judgment of the International Court of Justice in the case of The United Kingdom v. Iran, rendered on 22 July 1952, ICJ Reports 1952, p. 110.

Divergent interpretations of the scope of the MFN clause in BITs reveal shortcomings with the *ejusdem generis* rule. The first shortcoming is that the rule does not in fact provide a rule. This is because what it says in effect is that the scope of the MFN clause is what the MFN clause says it is. The circularity of this reasoning therefore requires tribunals to supplant this 'rule' with the additional interpretative guide that the MFN clause only refers to matters that the Parties intended, meaning that the clause is to be interpreted according to the Party's intentions.

The statement that the *ejusdem generis* rule is justified by the Party's intentions is not at first glance controversial. However, upon closer analysis it becomes clear that this interpretative approach is inconsistent with the customary international law rules of interpretation as stated in Articles 31 and 32 of the Vienna Convention on the Law of Treaties ('Vienna Convention').[112] This is because it makes an inquiry into the intentions of the Parties, the initial and indeed most important step in an interpretation of an MFN clause, thereby elevating intention from a supplementary means of interpretation under Article 32 of the Vienna Convention. This interpretative process stands in contrast to the process outlined in Article 31 of the Vienna Convention, which requires the text to be interpreted in light of its context, object and purpose.

The relegation by Article 32 of the Vienna Convention of Party's intentions to a supplementary or secondary role highlights the limits of Party's intentions as means of interpreting a treaty. While basing an interpretation of a treaty on the Party's intentions is superficially consistent with notions of State sovereignty, it quickly runs into the problem of whose intentions count – the negotiators of the treaty, the executive that signed the treaty or the Parliament that ratified the treaty.[113] Even if this problem could be satisfactorily resolved there remains the problem of determining the relevant intentions.

As a result of these limits with Party's intentions as an effective interpretative guide, we can identify a move away from the *ejusdem generis* rule towards the interpretative process in Article 31 of the Vienna Convention. This evolution of interpretative approaches towards the MFN clause is most evident in a series of cases that has addressed the extent that MFN clauses can be relied upon by disputing investors to incorporate more favourable dispute settlement provisions than the defending State has agreed to in other investment agreements.[114]

112 Done at Vienna, 23 May 1969, in force 27 January 1980, 1155 UNTS 331; (1969) 8 ILM 679, UKTS (1980) 58.

113 James B. White, *Justice as Translation: An Essay in Cultural and Legal Criticism* (Chicago: University of Chicago Press, 1994), at p. 113.

114 Compare the reliance of the Tribunal in *Maffezini*, below n. 116, para. 56, on the *ejusdem generis* rule to interpret the MFN clause with the approach of later tribunals in *Plama*, below n. 120, para. 188, and *Telenor*, below n. 123, para. 92, who follow Article 31 of the Vienna Convention and make no reference to the *ejusdem generis* rule.

However, while the tribunals in these cases do refer to Articles 31 and 32 of the Vienna Convention as the appropriate interpretative process, there is in fact only a limited and often mechanical application of these rules of interpretation. Further, Article 31 in particular does not call for a linear step-by-step interpretative process as there is nothing in Article 31 that prioritises text for instance, over context, object, or purpose. Instead, Article 31 of the Vienna Convention requires a more holistic approach, reaching a conclusion on the ordinary meaning of the term at issue only upon an examination of all the 'relevant elements'.[115] As a practical matter, this may require a step-by-step process, keeping in mind that the text, context, object and purpose form part of the same overall analysis.

Therefore, despite a convergence by these tribunals on Articles 31 and 32 of the Vienna Convention as the correct methodology for interpreting MFN clauses, these cases reach conflicting interpretations of the scope of MFN clauses in BITs. One line of cases, comprising *Emilio Agustin Maffezini* v. *The Kingdom of Spain*,[116] *Siemens A.G.* v. *The Argentine Republic*,[117] and *Suez, Sociedad General de Aguas de Barcelona S.A. and InterAguas Servicios Integrales del Aguas S.A.* v. *The Argentine Republic*,[118] has understood the scope of an MFN clause as not being limited to the 'substantive' protections provided to investment, and therefore being capable of referring to dispute settlement provisions as well. The other line of cases, comprising *Salini Contruttori S.p.A and Italstrade S.p.A.* v. *The Hashemite Kingdom of Jordan*,[119] *Plama Consortium Limited* v. *Republic of Bulgaria*,[120] and *Telenor Mobile Communications* v. *The Republic of Hungary*,[121] has interpreted largely identical MFN clauses as not extending to more favourable dispute settlement provisions in other investment agreements, unless it is expressly made clear that this is the intended scope of the MFN clause.

Starting with the text, in *Maffezini*, the MFN clause referred to 'all matters' while in *Siemens* and *Aguas* the MFN clause referred to 'treatment'. Despite the textual

115 Federico Ortino, 'Treaty Interpretation and the WTO Appellate Body Report in US–Gambling: A Critique' (2006) 9(1) *Journal of International Economic Law* 117–48, at 131; see also Robert L. Howse and Donald H. Regan, 'The Product/Process Distinction – An Illusory Basis for Disciplining "Unilateralism" in Trade Policy' (2000) 11(2) *European Journal of International Law* 249–89, who observed that 'words generally do not have any context-independent "ordinary meaning" '.

116 *Emilio Agustin Maffezini* v. *The Kingdom of Spain* (*Maffezini*), Decision of the Tribunal on Objections to Jurisdiction, ICSID Case No. ARB/97/7 (25 January 2000).

117 *Siemens A.G.* v. *The Argentine Republic* (*Siemens*), Decision on Jurisdiction, ICSID Case No. ARB/02/8 (3 August 2004).

118 *Suez, Sociedad General de Aguas de Barcelona S.A. and InterAguas Servicios Integrales del Aguas S.A.* v. *The Argentine Republic* (*Aguas*), Decision on Jurisdiction, ICSID Case No. ARB/03/17 (16 May 2006).

119 *Salini Contruttori S.p.A and Italstrade S.p.A.* v. *The Hashemite Kingdom of Jordan* (*Salini (Jordan)*), Decision on Jurisdiction, ICSID Case No. ARB/02/13 (12 November 2004).

120 *Plama Consortium Limited* v. *Republic of Bulgaria* (*Plama*), Decision on Jurisdiction, ICSID Case No. ARB/03/24 (8 February 2005).

121 *Telenor Mobile Communications* v. *The Republic of Hungary* (*Telenor*), ICSID Case No. ARB/04/15 (Award of 13 September 2006).

differences, they were both considered wide enough to include dispute settlement provisions, or in other words, there was nothing in the clauses that suggested they should be narrowed so as to exclude dispute settlement.[122]

In contrast, all the MFN clauses in *Salini (Jordan)*, *Plama* and *Telenor* referred to 'treatment', however, in these cases the tribunals reached the opposite conclusion, that according to the ordinary meaning of the terms of the MFN clause 'there is no warrant for construing the above phrase (the MFN clause) as importing procedural rights'.[123]

What this suggests is that there is nothing in the word 'treatment' that is conclusive of whether it extends to dispute settlement provisions in other FTAs or investment agreements.[124] However, in FTAs such as US–Chile, Canada–Chile and US–Singapore, the type of 'treatment' covered by the MFN clause is limited to the 'establishment, acquisition, expansion, management, conduct, operation and sale or other disposition' of the investment. Therefore, the 'treatment'' in these FTA MFN clauses is not as open-ended as in the MFN clauses in the BITs, and the failure to refer to dispute settlement in the FTAs arguably reveals an intention to exclude dispute settlement from the scope of the MFN clause.

Furthermore, what constitutes 'treatment' also needs to be assessed in light of whether it is in fact more favourable treatment. As the tribunal noted in *Plama*: ' . . . what if one BIT provides for UNCITRAL arbitration and another provides for ICSID? Which is more favourable?'[125] The tribunal in *Plama* also suggested that a choice is better than no choice – however, even this assumption should be questioned.[126]

The inconclusiveness of the text of the MFN clause led these tribunals to use other justifications for their decisions. One justification was that access by investors to dispute settlement provisions are essential for protecting investors' rights accorded under investment agreements.[127] Another was that the purpose of the BITs revealed in their preambles and title an intention of States to protect and promote investments.[128]

However, the tribunals in *Telenor* and *Plama*[129] argued that the preamble and title are 'legally insufficient' to show that the MFN clause extends to dispute settlement provisions in other treaties.[130] To the extent that these tribunals were warning of the need to avoid reading one particular telos into a BIT at the expense of others, this resonates with modern FTAs, which include comprehensive commitments on a range of areas in addition to investment, such as on goods, services, intellectual property and telecoms. As a result, any attempt to establish the scope of an MFN

122 *Maffezini*, para. 56; *Siemens*, para. 103; and *Aguas*, para. 55.
123 *Telenor*, para. 92. See also *Plama*, para. 204; and *Salini (Jordan)*, para. 119.
124 See *Plama*, para. 189. 125 *Ibid.*, para. 208. 126 *Ibid.*, para. 208.
127 *Maffezini*, paras. 54–5; and *Aguas*, para. 60. 128 *Siemens*, para. 43; and *Aguas*, para. 57.
129 *Telenor*, para. 95; and *Plama*, para. 192. 130 *Plama*, para. 192.

clause by reference to a single goal of an FTA Investment Chapter would ignore that FTAs embrace a multitude of goals and purposes that represent an 'overall balance of rights and obligations'.[131]

The *Maffezini* tribunal finally sought to limit the effect of its broad application of the MFN clause by introducing policy exceptions, endorsed by the tribunals in both *Siemens* and *Aguas*.[132] These policy exceptions would not allow the dispute settlement provisions in the original treaty to be upset when shown that they were 'envisaged as fundamental conditions for the acceptance of the agreement in question'.[133] While this approach was followed by the tribunal in *Siemens*,[134] other tribunals have refused to followed *Maffezini's* policy exceptions, and instead have emphasised interpreting BITs using 'the ordinary cannons of interpretation, not to displace, by reference to general policy consideration concerning investor protection, the dispute resolution mechanisms specifically negotiated by the Parties'.[135]

It is suggested, however, that the different facts in each case, and specifically, what each investor was asking of the MFN clause, provides one way of understanding the different outcomes in these cases and the implications for FTA Investment Chapter MFN clauses.[136]

In *Maffezini, Siemens* and *Aguas*, the tribunals addressed the same provision in the Spain–Argentina BIT, namely, the requirement that local courts be given eighteen months to resolve a dispute before it could be referred to international arbitration. In all these cases the investors were seeking to avoid this requirement by reference to dispute settlement provisions in other BITs that allowed for a period of only six months of negotiation before the dispute could be referred to international arbitration.

In contrast, the investors in *Salini (Jordan)*, *Plama* and *Telenor* were asking the tribunals to interpret the MFN clause in a manner that would have produced significantly more radical effects. For example, in *Salini (Jordan)* the investor sought to use the MFN clause to extend the scope of the jurisdiction of the tribunal under the Italy–Jordan BIT to include contractual disputes on the basis that dispute settlement provisions in other BITs to which Jordan was a Party allowed for the arbitration of contractual disputes by international tribunals. While in *Plama* and in *Telenor*, the BIT dispute settlement provisions were limited to claims of expropriation. In these cases the investors sought to extend the jurisdiction of the tribunal by reference to the dispute settlement provisions in other BITs to which these States were a party that did not limit the jurisdiction of tribunals in this manner.

131 US–Singapore FTA, Preamble. 132 *Maffezini*, para. 62; and *Siemens*, para. 109.

133 *Maffezini*, para. 62: This was outlined in Maffezini as including instances where consent to arbitration was conditioned on exhaustion of local remedies, a fork-in-the-road provision, where the agreement provided for a particular arbitration forum such as ICSID, and highly institutionalised dispute settlement provisions such as in NAFTA.

134 *Siemens*, para. 109. 135 *Telenor*, para. 95. 136 *Plama*, para. 211; and *Telenor*, p. 98.

Interestingly, if the *Mafezzini* tribunal had been confronted with the same facts as in *Plama* and *Telenor*, it would probably have reached the same result as these later tribunals. However, the reverse may not necessarily be true because in *Maffezini* there was a lack of evidence that it was the intention of the Parties that the scope of the MFN clause should include dispute settlement provisions.

What this suggests for MFN clauses in FTA Investment Chapters is that in those cases where the investor is seeking to use the MFN clause to extend the jurisdiction of a tribunal, whether a tribunal adopts the approach in *Maffezini* or the approach in *Plama* and *Telenor*, the results may be similar although the reasoning would be different.

Moreover, where an investor is seeking to use an MFN clause to access what it considers to be more favourable treatment offered to other investors with respect to procedural issues such as the timing of international disputes, then as long as the investor can show that a shorter time-line for instance, is in fact more favourable treatment, then, depending on whether a tribunal adopted the reasoning in *Maffezini* or in *Plama* and *Telenor*, we could expect divergent outcomes.

2. Temporal scope of the MFN clause

The extent that an MFN clause requires a State party to an FTA with an MFN clause to extend the benefits that State accords to other States also depends on the temporal application of the MFN clause.

Regarding an MFN clause's temporal application, most FTAs exclude from the scope of the MFN clause international agreements in force or signed prior to that FTA. In the case of the US–Chile FTA, Canada–US Free Trade Agreement (CUSFTA) and NAFTA, this limitation is captured in Annex II, which is where each Party lists those sectors where a Party wishes to maintain the flexibility to introduce measures that either liberalise or restrict their commitments under the FTA.

C. Fair and equitable treatment and full protection and security

The obligation to provide fair and equitable treatment and full protection and security is an absolute standard because, in contrast to NT and MFN treatment obligations, it is not defined by how the host State treats its nationals. In this sense, this obligation provides a floor for the treatment of foreign investors below which host States agree not to go.

Three approaches can be identified in FTA Investment Chapters to the commitment to provide fair and equitable treatment and full protection and security. One approach, taken in FTAs such as US–Singapore, CAFTA–DR–US, US–Chile, AUSFTA, and Korea–Singapore, describes the obligation to provide fair

and equitable treatment and full protection and security as part of the minimum standard of treatment under customary international law.[137] For example, the US–Singapore FTA makes it clear that 'the concepts of ''fair and equivalent treatment'' and ''full protection and security'' do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights'.[138] These FTAs also include provisions that prohibit a claimant from relying upon a breach of another provision of the FTA to establish a breach of the obligation to provide fair and equitable treatment.[139]

A second approach requires States to accord fair and equitable treatment in accordance with international law. This approach is followed in NAFTA and Canada–Chile.[140] A third approach is to simply refer to a commitment to provide 'fair and equitable treatment' without limiting it to the minimum standard of treatment or to international law. This approach is taken in the Thailand–Australia FTA and the Draft CCIA Investment Framework Agreement.[141]

Finally, some FTAs, such as the India–Singapore CECA and the Singapore–Australia Free Trade Agreement, do not include a commitment to provide fair and equitable treatment or full protection and security.

The following looks at how tribunals have interpreted these three formulations of the commitment to provide fair and equitable treatment. It is worth noting, however, that there is overlap in the scope of each of these fair and equitable treatment commitments. For instance, some international tribunals have interpreted a stand-alone commitment to provide fair and equitable treatment as being substantially the same as the customary international law minimum standard of treatment,[142] while others have interpreted the obligation to provide fair and equitable treatment at international law as being equivalent to fair and equitable treatment as a stand alone commitment.[143]

137 US–Singapore FTA, Article 15.5; CAFTA–DR–US, Article 10.5; US–Chile FTA, Article 10.4; AUSFTA, Article 11.5; and Korea–Singapore FTA, Article 10.4.

138 US–Singapore FTA, Article 15.2.

139 *Ibid.*, Article 15.5; CAFTA–DR–US, Article 10.5; US–Chile FTA, Article 10.4; AUSFTA, Article 11.5; and Korea–Singapore FTA, Article 10.4.

140 NAFTA, Article 1105; and Canada–Chile FTA, Article G-05.

141 Thailand–Australia FTA, Article 909.2; and Draft CCIA Investment Framework Agreement, Article 5.1(a).

142 Judge Asante in his dissenting opinion in *Asian Agricultural Products Ltd. (AAPL)* v. *Republic of Sri Lanka*, ICSID Case No. ARB/87/3 (Award of 27 June 1990), equated the 'fair and equitable treatment' standard with the international minimum standard of treatment; *American Manufacturing & Trading (AMT) (US), Inc.* v. *Republic of Zaire*, ICSID Case No. ARB/93/1 (Award of 21 February, 1997), p. 29; *Alex Genin, Eastern Credit Limited, Inc. and A.S. Baltoil (US)* v. *Republic of Estonia*, ICSID Case No. ARB/99/2 (Award of 25 June 2001); and *Azurix Corp.* v. *Argentina*, ICSID Case No. ARB/01/12 (Award of 26 July 2006), para. 364.

143 *Tecnicas Medioambientales Tecmed, S.A.* v. *United Mexican States* ('*Tecmed*'), ICSID Case No. ARB(AF)/00/2 (Award of 29 May 2003), para. 155.

The customary international law minimum standard of treatment

First articulated in the 1926 *United States* v. *Mexico General Claims Commission* ('*Neer Claim*'), the international minimum standard stated that:

> *. . . the propriety of governmental acts should be put to the test of international standards . . . the treatment of an alien, in order to constitute an international delinquency should amount to an outrage, to bad faith, to wilful neglect of duty or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency, Whether the insufficiency proceeds from the deficient execution of a reasonable law or from the fact that the laws of the country do not empower the authorities to measure up to international standards is immaterial.*[144]

The customary international law minimum standard of treatment has, however, evolved since its formulation in the *Neer Claim*, and therefore the scope of the obligation remains contested.[145]

For instance, some FTAs provide non-exhaustive definitions of the standard. For example, the US–Chile FTA states that, '"fair and equitable treatment" includes the obligation not to deny justice in criminal, civil or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principle legal systems of the world'.[146] Other FTAs, such as the Korea–Singapore FTA Investment Chapter, also adopt this elaboration of the meaning of 'fair and equitable treatment', but without reference to 'the principle legal systems of the world'.[147]

In NAFTA, the commitment to provide fair and equitable treatment is tied to international law. However, in 2001 the NAFTA Free Trade Commission, comprising all NAFTA member States, issued the following Note of Interpretation:

1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.
2. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.
3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).

This Interpretative Note has formed the basis for the 'fair and equitable treatment' commitment in those FTAs that tie this commitment to the minimum standard of

144 *United States* v. *Mexico General Claims Commission* ('*Neer Claim*') (1926) 4 RIAA 60.

145 *ADF Group Inc.* v. *United States of America*, ICSID Case No. ARB(AF)/00/1 (Award of 9 January 2003), para. 179; and *Mondev International Ltd* v. *United States of America* ('*Mondev*'), ICSID Case No. ARB (AF)/99/2 (Award of 11 October 2002), para. 125.

146 US–Chile FTA, Article 10.4.2(a). 147 Korea–Singapore FTA, Article 10.5.2.

treatment. As a result, decisions of NAFTA tribunals that post-date this Note also shed important light on the content of this standard.

For example, the tribunal in *Waste Management, Inc.* v. *United Mexican States*, reviewing decisions of former NAFTA tribunals on the 'fair and equitable treatment' standard, stated that conduct infringes the standard when it is:

> . . . arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety – as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying the standards it is relevant that the treatment is in breach of representations made by the host Sate which were reasonably relied on by the claimant.[148]

The tribunal in *Mondev* also made it clear that 'a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith'.[149] The tribunal in *Tecmed* further elaborated on the content of the standard by referring to the good faith principle.[150] Here, the tribunal stated that this requires the host State to 'act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor'.[151]

1. Fair and equitable treatment as defined by international law

Article 1105 of the NAFTA describes the standard as 'fair and equitable treatment in accordance with international law', and therefore the approach of several NAFTA tribunals prior to the FTC Interpretative Note sheds light on the content of this obligation. Article G-05 of the Canada–Chile FTA also describes the standard as 'fair and equitable treatment in accordance with international law'.[152]

The significance of defining fair and equitable treatment according to international law is that tribunals have been prepared to interpret this commitment by reference to all sources of international law, including treaties such as BITs, customary international law, and other general principles of international law.[153]

As a result, tribunals have treated this as a broader commitment than when it is framed as part of the minimum standard of treatment at customary international law. Therefore, the tribunal in *Metalclad* included an obligation of transparency as

148 *Waste Management, Inc.* v. *United Mexican States* ('*Waste Management*'), ICSID Case No. ARB(AF)/98/2 (Award of 2 June 2000), 43 ILM 967, paras. 98–9.

149 See *Mondev*, para. 161. 150 See *Tecmed*, para. 154. 151 *Ibid.*

152 Note that the heading of Article G-05 is 'Minimum Standard of Treatment', which suggest that Canada does not consider there to be a distinction between fair and equitable treatment at international law and when defined as part of the customary international law minimum standard of treatment.

153 OECD, 'Fair and Equitable Treatment Standard in International Investment Law', OECD Working Papers on International Investment No. 2004/3 (September 2004), at p. 20.

part of the fair and equitable treatment commitment.[154] Further, the tribunal in *Myers* v. *Canada* found that a breach of the NAFTA NT provision could constitute a violation of the obligation to provide fair and equitable treatment.[155] The tribunal in *Pope & Talbot* appeared to un-couple the standard from international law entirely, by stating that 'investors are entitled to the international law minimum, plus the fairness elements'.[156]

This trend was also evident in *Tecmed*. In that case, the tribunal referred to the 'basic expectations' of the investor when it stated that the fair and equitable treatment standard requires the host State 'to act consistently, i.e. without arbitrarily revoking any pre-existing decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities'.[157] This approach has been criticised as raising an investor's 'basic expectation' into a treaty commitment.[158]

2. Fair and equitable treatment as a stand-alone commitment

The obligation to provide fair and equitable treatment, stated as a stand-alone commitment, is not legally equivalent to the obligation to provide fair and equitable treatment when stated as part of the minimum standard of treatment at customary international law.[159] This is because such a commitment should be understood as self-contained and interpreted in light of whether 'a particular treatment meted out to that investor is both ''fair'' and ''equitable'' '.[160]

Other tribunals have interpreted the obligation to provide fair and equitable treatment as entitling investors 'to the international law minimum plus the fairness elements'.[161] One commentator has gone so far as to observe that an obligation to provide 'fair and equitable treatment' 'is likely to be sufficient to cover all conceivable cases, and it may well be that other provisions of the Agreements affording substantive protection are no more than examples or specific instances of this overriding duty'.[162]

The requirement to provide fair and equitable treatment was initially referred to in the 1948 Havana Charter for an International Trade Organisation[163] (Article

154 *Metalclad Corporation* v. *United Mexican States* ('*Metalclad*'), ICSID Case No. ARB(AG)/97/1 (Award of 30 August 2000), para. 99.
155 See *Myers* v. *Canada*, para. 266. 156 See *Pope & Talbot*, para. 110. 157 See *Tecmed*, para. 154.
158 *MTD Equity Sdn Bhd & MTD Chile S.A.* v. *Chile*, ICSID Case No. ARB/01/7 (21 March 2007), para. 67.
159 UNCTAD, *Investment Provisions in Economic Integration Agreements* (New York and Geneva: UNCTAD, 2006), at p. 105; however, see *Tecmed*, para. 155.
160 *Saluka Investments BV (The Netherlands)* v. *The Czech Republic* ('*Saluka v. Czech Republic*'), UNCITRAL Arbitral Tribunal (Partial Award of 17 March 2006), para. 282; and UNCTAD, *Fair and Equitable Treatment*, UNCTAD Series on Issue in International Investment, vol. 3 (New York and Geneva: UNCTAD, 1999).
161 *Pope & Talbot* (Award on The Merits of 10 April 2001), para. 110.
162 F.A. Mann, 'British Treaties for the Promotion and Protection of Investments' (1981) 52 *British Yearbook of International Law* 241–54.
163 Done at Havana on 24 March 1948, never ratified.

11.2), as a requirement to afford international investments 'just and equitable treatment'. The US's FNC treaties, as precursors to BITs, also included an obligation to provide 'fair and equitable' treatment.

The Thailand–Australia FTA refers to a requirement to accord fair and equitable treatment[164] while the Japan–Singapore EPA states that '[e]ach Party shall accord to investments in its territory of investors of the other Party fair and equitable treatment and full protection and security'.[165] These formulations of the 'fair and equitable treatment' standard are also reflected in numerous BITs, such as those used by Switzerland, Germany and Sweden.[166]

When the fair and equitable treatment standard is phrased as a stand-alone commitment, one approach to interpreting this standard has been to regard it as an autonomous standard not linked to international law and to be interpreted according to its plain meaning,[167] taking into account the treaties' object and purpose and circumstance of its conclusion.[168]

Relying on the terms of the treaty to give the fair and equitable treatment standard its content without reference to other sources of international law and other arbitral decisions provides significant scope for it to become a subjective standard reflecting a particular tribunal's sense of what is fair and equitable on that day. Conflicting interpretations of this standard are therefore inevitable,[169] which will undermine one of the goals of FTA investment chapters, namely, increased certainty and predictability in the investment conditions of the Parties to the treaty.[170] As a result of these problems, even where the standard is framed without reference to international law, tribunals often seek to interpret the commitment applying the applicable law, as defined in either the Agreement under which the dispute arises or in ICSID or UNCITRAL.[171] The following outlines how tribunals have interpreted the obligation.

164 Thailand–Australia FTA, Article 909. 165 Japan–Singapore EPA, Article 77.1.

166 See, e.g., Switzerland–Iran BIT, Article 4; Switzerland–Jordan BIT, Article 2; Germany–China BIT, Article 4; Germany–Ethiopia BIT, Article 1; Sweden–Laos BIT, Article 3; and Sweden–Philippines BIT, Article 3.

167 See Mann, above n. 164.

168 *Saluka* v. *Czech Republic*, para. 294; and *Ronald S. Lauder* v. *The Czech Republic* ('*Lauder* v. *Czech Republic*'), UNCITRAL Arbitral Tribunal Final Award of 3 September 2001.

169 See *Lauder* v. *Czech Republic*; and *CME Czech Republic B.V.* v. *The Czech Republic*, UNCITRAL Arbitral Tribunal Partial Award (Merits) of 13 September 2001, where these two tribunals applied the same stand-alone clause to the same facts and reached conflicting outcomes. However, the tribunal in *Saluka* v. *Czech Republic*, at paras. 284–5, argued that a stand-alone fair and equitable treatment standard does not 'invite the tribunal to decide the dispute in a way that resembles a decision *ex aequo et bono* . . . it does not set out totally subjective standards which would allow the Tribunal to substitute, with regard to the Czech Rpublic's conduct to be assessed in the present case, its judgement on the choice of solutions for the Czech Republic's [sic]'.

170 *Occidental Exploration and Production Company* v. *Republic of Ecuador*, LCIA Case No. UN3467, Final Award of 1 July 2004, para. 183, where the tribunal notes, referring to the BIT preamble, that 'the stability of the legal and business framework is thus an essential element of fair and equitable treatment'.

171 Where the Parties to the FTA fail to specify the applicable law, ICSID Article 42.1 directs the tribunal to apply 'the law of the Contracting States party to the dispute (including its rules on conflict of laws) and such rules of international law as may be applicable'. UNCITRAL Arbitration Rules, Article 33.2, does not refer to

First, commentators and tribunals have recognised that it includes an obligation of due process and not to deny justice. A denial of justice in international law has been described as, 'a denial, unwarranted delay or obstruction of access to courts, gross deficiency in the administration of judicial or remedial process, failure to provide those guarantees which are generally considered indispensable to the proper administration of justice or a manifestly unjust judgement'.[172] This conception of denial of justice has been found by arbitral tribunals to be an element of the obligation to accord investors fair and equitable treatment.[173]

Arbitrariness has also been seen by tribunals as an element of the obligation of due process and therefore considered to be an element of the fair and equitable treatment standard,[174] describing it has a 'wilful disregard of due process of law, an act which shocks, or at least surprises, a sense of judicial propriety'.[175]

Tribunals have also found that the 'fair and equitable treatment' standard requires the State to act in a transparent manner. For instance, in *Tecmed*, the tribunal described the standard as requiring the State 'to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor'.[176] This obligation of transparency was also found to exist by the tribunals in *Metalclad* and *Waste Management*.[177]

D. Full protection and security

FCN treaties articulated an obligation to provide full protection and security prior to the obligation to provide fair and equitable treatment.[178] Today, the scope of the obligation to provide full protection and security will partly depend on whether it is defined as limited to the customary international minimum standard of treatment or phrased as being a separate stand-alone commitment.[179]

All FTAs that include a commitment to provide fair and equitable treatment also include a commitment to provide full protection and security, except for the Draft CCIA Investment Framework Agreement, which limits the commitments to fair and equitable treatment only.

international law but does not allow a decision *ex aequo et bono* unless expressly authorised by the Parties; see also *MTD Equity Sdn. Bhd. & MTD Chile S.A.* v. *Chile*, ICSID Case No. ARB/01/7 (21 March 2007), para. 44.

172 Draft Convention Prepared By the Research in International Law of the Harvard Law School, Supplement to (1935) 29 *American Journal of International Law*.

173 *Mondev International Ltd* v. *United States*, ICSID Case No. ARB(AF)/99/2 (Award of 11 October 2002); and *Robert Azinian and others* v. *The United Mexican States*, ICSID Case No ARB(AF)/97/2 (Arbitral Award 1 November 1999), paras. 102–103.

174 *Electronic Sicula S.p.A. (ELSI) (United States of America* v. *Italy)* ('*Electronic Sicula*') [1989] ICJ Reports 15 (20 July 1989), p. 30.

175 *Ibid.*, p. 76. 176 *Tecmed*, para. 154; see also *Saluka* v. *Czech Republic*, para. 307.

177 *Waste Management*, paras. 98–9.

178 UNCTAD, *Bilateral Investment Treaties in the Mid-1990s* (New York and Geneva: UN, 1998).

179 *Asian Agricultural Products Ltd* v. *Republic of Sri Lanka*, ICSID Case No. ARB/87/3 (Final Award of 27 June 1990), para. 50.

The obligation to provide full protection and security is commonly understood as an 'obligation for the host State to adopt all reasonable measures to physically protect assets and property from threats or attacks which may target particularly foreigners or certain groups of foreigners'.[180]

Tribunals have made it clear that the obligation to provide full protection and security is not an obligation of strict liability;[181] instead, they have defined this obligation as one of 'due diligence', described as 'the reasonable measures of prevention which a well-administered government should be expected to exercise under similar circumstances'.[182] For example, the tribunal in *American Manufacturing & Trading, Inc* v. *Zaire* found a breach of Zaire's obligation to provide full protection and security due to its failure to stop the looting of AMT by Zairian armed forces. In this case, the tribunal refused to define this either as an obligation of conduct or result and instead relied on the additional obligation in the BIT on the Parties to provide compensation in cases of strife as confirming the responsibility of Zaire for losses and damages by AMT.[183]

In recent cases, tribunals have conflated the obligation to provide full protection and security with the fair and equitable treatment standard, stating that 'treatment that is not fair and equitable automatically entails an absence of full protection and security'.[184] In defining this obligation as part of the fair and equitable treatment standard, these tribunals have also extended this obligation beyond providing physical protection.[185] It is, however, unlikely that tribunals will conflate the commitment to provide fair and equitable treatment with the commitment to provide full protection and security in FTAs such as US–Singapore where the full protection and security standard is limited to 'police protection required under customary international law'.[186]

E. Expropriation

The expropriation obligation is one of the most important and arguably most controversial of the protections afforded in FTA investment chapters. Traditionally,

180 Georgio Sacerdoti, 'Bilateral Treaties and Multilateral Instruments on Investment Protection' (1997) 269 *Recueil des Cours* 251–460, at 347.

181 *Asian Agricultural Products Ltd* v. *Republic of Sri Lanka*, para. 50; *Ronald S. Lauder* v. *The Czech Republic*, para. 308; and *Saluka* v. *The Czech Republic*, para. 484.

182 *Asian Agricultural Products Ltd* v. *Republic of Sri Lanka*, paras. 76–7.

183 *American Manufacturing & Trading, Inc.* v. *Zaire* ('*AMT v. Zaire*'), ICSID Case No. ARB/93/1 (Award of 21 February 1997), paras. 6.08–6.14.

184 *Occidental Exploration and Production Company* v. *Republic of Ecuador*, para. 187.

185 *Azurix* v. *Argentine Republic*, ICSID Case No. ARB/01/12 (Award of 14 July 2006), para. 408; however, see *PSEG Global Inc.*, *The North America Coal Corporation and Konya Ilgin Elektrik Üretim ve Ticaret Limited Sirketi* v. *Republic of Turkey*, ICSID Case No. ARB/02/05 (Award 19 January 2007), para. 258, where the tribunal sought to limit those cases when a breach of the 'fair and equitable treatment' commitment would also constitute a breach of the 'full protection and security' commitment, to an 'exceptional situation'.

186 US–Singapore FTA, Article 15.52(b).

the expropriation debate focused on how a State could lawfully expropriate an investment and how the level of compensation was to be valued.[187] On the one hand, the Hull Rule required 'prompt, adequate and effective' compensation while on the other hand, the Calvo Doctrine argued that it was only necessary to provide 'appropriate compensation, in accordance with the rules in force in the State taking such measures in the exercise of its sovereignty'.[188]

As discussed above, growing appreciation of the important development benefits of investment have led countries to accept that instances of expropriation should be subject to an international law standard regarding the payment of compensation. Therefore, the main debate today regarding the expropriation obligation is over the scope of what constitutes indirect expropriation (discussed below).[189]

1. Lawful expropriation

Under customary international law, an expropriation is prohibited unless it fulfils four conditions: (1) the measure is for a public purpose; (2) it is non-discriminatory; (3) in accordance with due process; and (4) compensation is paid.[190]

Most FTA Investment Chapters reflect these conditions for a lawful expropriation.[191] Many FTA Investment Chapters, when referring to expropriation being in accordance with 'due process of law', also require that an expropriation must be carried out consistently with the minimum standard of treatment as defined in the Investment Chapter. This approach is followed in US–Singapore, US–Chile, Korea–Chile, Canada–Chile and Korea–Singapore.[192]

Other FTAs adopt slightly different formulations regarding how a State can lawfully expropriate. For instance, the India–Singapore CECA refers to 'a purpose authorized by law', rather than a 'public purpose', and makes it clear that any expropriation of land shall always be deemed 'a purpose authorized by law'.[193] However, given the latitude tribunals normally extend to a State's assessment of what constitutes a 'public purpose', this provision was likely included to provide

187 Rudolf Dolzer, 'Indirect Expropriations: New Developments?' (2002) 11 *New York University Environmental Law Journal* 64–93, at 64.

188 Steiner, Vagts and Koh, above n. 5, at p. 418. See Green H. Hackworth, *Digest of International Law* (Washington, DC: Government Printing Office, 1940–44), vol. 3, Sec. 228, at pp. 655–65, for the notes exchanged during the dispute in 1938 between the US and Mexico concerning expropriation by Mexico of US owned properties.

189 See Dolzer, above n. 189, at 64.

190 See *Restatement of the Law Third, Foreign Relations Law of the United States* (1987), Section 712; and *Antoine Goetz and others* v. *Republic of Burundi*, ICSID Case No. ARB/95/3 (Award of 10 February 1999).

191 See, e.g., US–Singapore FTA, Article 15.6; AUSFTA, Article 11.7; Canada–Chile FTA, Article G-10; Japan–Singapore EPA, Article 77; CAFTA–DR–US, Article 10.7; Korea–Chile FTA, Article 10.13; and the Draft CCIA Investment Framework Agreement, Article 16.

192 US–Singapore FTA, Article 15.6; US–Chile FTA, Article 10.9; Korea–Chile FTA, Article 10.13; Canada–Chile FTA, Article G-10; and the Korea–Singapore FTA, Article 10.13.

193 India–Singapore CECA, Article 6.5.

certainty for the Parties and therefore does not alter the scope of their expropriation obligation.[194]

All of these disciplines on expropriation reflect customary international law, and in some FTA Investment Chapters, this is made explicit. For example, Annex 11-B of the AUSFTA, the exchange of letters under the India–Singapore CECA, Annex 10-C of the CAFTA–DR–US, the side letter to the US–Singapore FTA and Annex 10-D to the US–Chile FTA, state that the expropriation provisions are intended to reflect customary international law.

2. Public purpose

The requirement that an expropriation be for a public purpose is based on the proposition that:

> [I]f international law recognizes the undoubtedly very wide power of the State to appropriate the property of aliens on the ground that, as under municipal law, the interests of the individual must yield to the general interest and public welfare, the least that can be required of the State is that it should exercise power only when the measure is clearly justified by the public interest.[195]

While the requirement that expropriation be in accordance with a 'public purpose' seeks to prohibit the 'abusive exercise of power to expropriate and to give legal sanction to manifestly arbitrary acts of expropriation',[196] international law also recognises that what constitutes a 'public interest' is to be assessed according to the domestic law of the expropriating State. Therefore, in practice, the discipline that an expropriation be for a public purpose still provides States with a wide degree of latitude to expropriate.

What constitutes a public purpose is not defined in these FTAs. A plain text reading of the texts, however, suggests that expropriations for a private benefit will not constitute a public purpose.[197]

3. Non-discriminatory

All FTA Investment Chapters require expropriation to be non-discriminatory. In the expropriation context, one commentator has described discrimination as entailing two concepts:

> [F]irst, the measures directed at a particular party must be for reasons unrelated to the substance of the matters, for example, the company's

194 See, e.g., *Tippets, Abbett, McCarthy, Stratton* v. *TAMS-AFFA Consulting Engineers of Iran* ('*Tippets* v. *TAMS-AFFA*'), Iran–US Claims Tribunal (Award No. 141–7–2 of 22 June 1984), 6 Iran-US CRT 219, pp. 225–6.

195 Fourth Report on States Responsibility by F.V. Garcia-Amador, Special Rapporteur, 'State Responsibility', in *Yearbook of the International Law Commission 1959* (New York: UN, 1960) vol. II, UN Doc. A/CN.4/119, para. 59.

196 *Ibid.*

197 As outlined above, Article 6.5.3 of the India–Singapore CECA clarifies that an expropriation of land shall be deemed as being for a public purpose.

> nationality. Second, discrimination entails like persons being treated in an inequivalent manner.[198]

This standard was followed in *Amoco International Finance Corp.* v. *Islamic Republic of Iran*, where the claimant argued that the expropriation was discriminatory because the Japanese share of the investment was not expropriated. In this case, the defendant argued that the expropriation of the American share in the investment was not based on nationality, but instead on other legitimate factors, such as the Japanese share not being an operational concern at the time of the expropriation.[199] The tribunal accepted these as justifiable grounds for drawing a distinction between the American and Japanese investment, and as a result, the tribunal found that the expropriation was not discriminatory.[200]

4. Due process of law

The Japan–Singapore EPA, NAFTA, US–Chile FTA, Canada–Chile FTA and AUSFTA all require that an expropriation be conducted in accordance with due process of law.[201] This requirement therefore disciplines the manner in which the expropriation is conducted.

What constitutes 'due process' is not defined in these FTAs, though it would appear to include the requirement that the process of expropriation be fair, transparent, subject to judicial review and participation by the affected investor.[202]

International law has allowed States significant discretion to determine what constitutes due process, only intervening when the process falls below the minimum standard of treatment.[203] In fact, a failure to accord 'due process' when expropriating may only arise when there is discrimination.[204] In the absence of discrimination, it is argued that State actions that are consistent with their domestic law do not breach international law. Others have argued, however, that arbitrariness will also constitute a breach of the due process requirement.[205]

Finally, it is worth recalling that a number of FTAs require expropriation to be in accordance with the minimum standard of treatment and that this standard also incorporates due process required.[206] Thus, a breach of the minimum standard of treatment commitment could not lead to an expropriation consistent with the FTA.

198 Abul F.M. Maniruzzaman 'Expropriation of Alien Property and the Principle of Non-Discrimination in International Law of Foreign Investment: An Overview' (1998) 8(1) *Journal of Transnational Law & Policy* 57–78, at 69.

199 *Amoco International Finance Corp.* v. *Islamic Republic of Iran*, Iran–US Claims Tribunal (Award 310–56–3 of 14 July 1987) (Chamber 3), 15 Iran–US CTR 189, paras. 140–2.

200 *Ibid.*

201 Japan–Singapore EPA, Article 77; NAFTA, Article 1110; US–Chile FTA, Article 10.9; Canada–Chile FTA, Article G-10; and AUSFTA, Article 11.7.

202 *Waste Management*, paras. 98–9. 203 See Garcia–Amador, above n. 197, para. 61.

204 *Sedco, Inc.* v. *National Iranian Oil Company*, Iran–US Claims Tribunal (Award ITL 59–129–3 of 27 March 1986), 10 Iran–US CTR 189.

205 See Garcia–Amador, above n. 197, para. 62. 206 See *Waste Management*, paras. 98–9.

5. Compensation

Once a Party to an FTA establishes that the expropriation was (1) for a public purpose; (2) non-discriminatory; and (3) done in accordance with due process of law, an obligation of compensation arises.

Public knowledge of an intended expropriation Most FTAs require that compensation be 'paid without delay at the date of expropriation', and that compensation be paid at the 'fair market value'.[207] However, because an expropriation can arise as a result of a series of acts over time, this raises the possibility of an intended expropriation becoming public knowledge, thereby reducing the value of the investment prior to the date of expropriation. The Canada–Chile FTA addresses this situation by stating the compensation paid 'shall not reflect any change in value occurring because the intended expropriation had become known earlier'.[208]

Assessing the value of the expropriated investment Most FTAs require compensation to be equivalent to the fair market value of the investment.[209] Some FTAs also outline how a Party to the FTA is to assess the fair market value of the expropriated asset. For example, the Canada–Chile FTA states that 'valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value'.[210] In other FTAs, such as the Japan–Singapore EPA and the US–Chile FTA, the expropriation provision does not address how fair market value is to be assessed, leaving it to the Government (or an arbitral tribunal) to make this calculation.[211]

Currency of payment FTA Investment Chapters also address the currency in which compensation is to be paid and the related issues of which exchange rate is to be used. For example, the US–Chile FTA requires compensation to be in 'a freely useable currency', which is defined as determined by the IMF.[212] For Parties to FTAs whose currency is not 'freely useable', different formulations are used so as not to prescribe payment in their own currency. For example, the Canada–Chile FTA requires payment to be made in a G7 currency.[213] In the case of the AUSFTA, compensation can be designated in a freely useable currency or the Australian dollar.[214]

207 See, e.g., Japan–Singapore EPA, Article 77.4; and Canada–Chile FTA, Article G-10.3.

208 See also, Korea–Singapore FTA, Article 10.13; Japan– Singapore EPA, Article 77; and AUSFTA, Article 11.17.2.

209 US–Singapore FTA, Article 15.6; AUSFTA, Article 11.7; Canada–Chile FTA, Article G-10; Japan–Singapore EPA, Article 77; CAFTA–DR–US, Article 10.7; Korea–Chile FTA, Article 10.13; Draft CCIA Investment Framework Agreement, Article 16; US–Chile FTA, Article 10.9; and Korea–Singapore FTA, Article 10.13.

210 Canada–Chile FTA, Article G.10.2.

211 See Japan–Singapore EPA, Article 77; and US–Chile FTA, Article 10.9.

212 US–Chile FTA, Article 10.27. 213 Canada–Chile FTA, Article G-10.4. 214 AUSFTA, Article 11.7.

Those FTA Investment Chapters that allow the fair market value of the investment to be designated in a currency that may not be freely transferable also address the situation when that currency is not transferable. For example, under the AUSFTA, if the Australian dollar is not transferable on the date of payment then the compensation paid cannot be less than the fair market value of the investment converted into a freely useable currency.

Other FTAs, such as the Japan–Singapore EPA, do not address the issue of changes in exchange rates when compensation is denominated in a currency other than a freely useable currency, effectively shifting the risk of currency fluctuations onto the investor.

6. Interest

In FTA Investment Chapters, interest is usually to be paid from the date of expropriation to the date when compensation is paid. The US–Chile FTA defines this interest rate as a 'commercially reasonable rate' and links the interest rate to the currency of compensation by requiring the interest rate to also be a 'commercially reasonable rate for that currency'.[215] A similar approach is also taken in the Canada–Chile FTA.[216] In contrast, the Japan–Singapore EPA requires only an 'appropriate interest'.[217]

7. Direct and indirect expropriation

All FTA Investment Chapters include disciplines on direct and indirect expropriation. However, different FTAs use different formulations to express this commitment. For example, the Japan–Singapore FTA Investment Chapter refers to 'measures equivalent to expropriation or nationalization'.[218] In contrast, the Korea–Singapore FTA Investment Chapter states that 'neither Party may, directly or indirectly, nationalize or expropriate an investment of an investor of the other Party'.[219] The Canada–Chile FTA Investment Chapter takes a similar approach to the Korea–Singapore FTA,[220] but includes the phrase, 'or take(s) a measure tantamount to nationalization or expropriation of such an investment'.[221] The only major departure from these formulations is in the Draft CCIA Investment Framework Agreement, which largely follows the 1967 OECD Draft Convention on the Protection of Foreign Property, and defines expropriation as including 'any measures attributable to the government of a member State which have the effect of depriving an investor of the ownership or control of, or a substantial benefit from, the investment and shall be interpreted to include all

215 US–Chile FTA, Article 10.10.3. 216 Canada–Chile FTA, Article G-10.4.
217 Japan–Singapore EPA, Article 77.4. 218 *Ibid.*, Article 77.2.
219 Korea–Singapore FTA, Article 10.13. 220 Canada–Chile FTA, Article G-10.
221 For a discussion, see *Myers* v. *Canada*, paras. 285–6; see also *Tecmed*, para. 114, which clarified that measures 'tantamount to nationalization or expropriation' do not address a type of expropriation in addition to direct and indirect expropriation.

forms of expropriation such as nationalization and attachment as well as creeping expropriation'.[222]

Another group of FTA Investment Chapters include text that elaborates on the commitment not to directly or indirectly expropriate. These include CAFTA–DR–US, US–Singapore, US–Chile, India–Singapore, and the AUSFTA.[223] All of these elaborations on the meaning of direct and indirect expropriation are substantially similar, and therefore the following analysis regarding this test is applicable to all these FTAs.

There has yet to be tribunal interpretation of the FTA Investment Chapter provisions that include text which elaborate on what constitutes direct or indirect expropriation. All of these FTA Investment Chapters state that these provisions 'reflect customary international law concerning the obligation of States with respect to expropriation'. Therefore, one way of approaching the text is to assess first how customary international law approaches the distinction between direct and indirect expropriation. However, this ignores both the lack of consistency in the approach of customary international law to this issue,[224] and the text, which under Article 31 of the Vienna Convention (which is also part of customary international law), is the starting point for any interpretative exercise.[225] Therefore, a better approach is to interpret the text in light of its context, object and purpose, taking into account the intentions of the Parties, expressed, for example, in Annex 10-D of the US–Chile FTA Investment Chapter, that these provisions reflect customary international law. Or in other words, customary international law provides the parameters within which these provisions should be understood.

Moreover, because there is currently no one answer at customary international law to assess whether a measure constitutes an indirect expropriation, where FTAs include text that addresses how this assessment it to be made, as in Annex 10-D of the US–Chile FTA, this not only reflects customary international law but also contributes to the development of customary international law on indirect expropriation. One consequence of this is the potential for divergent outcomes under FTAs that do not elaborate on the approach to indirect expropriation and those that do include such provisions. The following analysis seeks to draw out where these differences could arise.

8. Direct expropriation

Annex 10-D to the US–Chile FTA is a representative example of those FTAs that address how to assess when direct or indirect expropriation arises. Firstly, paragraph 2

222 Draft CCIA Investment Framework Agreement, Article 1.5.

223 AUSFTA, Annex 11-B; US–Chile FTA, Annex 10-D; India–Singapore CECA, Annex 3; CAFTA–DR–US, Annex 10-C; and US–Singapore FTA, Side-Letter on Expropriation.

224 See Dolzer, above n. 189, at 81–90.

225 See Ortino, above n. 117, at 131; see also Howse and Regan, above n. 117, at 261, who observed that 'words generally do not have any context-independent ''ordinary meaning'' '.

clarifies what will need to be established to show an expropriation, namely interference with a tangible or intangible property right or property interest in an investment.

Paragraph 3 then addresses what constitutes a direct expropriation, namely a nationalisation or formal transfer of title or outright seisure. Nationalisation may be understood as referring to changes or measures that affect an entire sector or country, whereas the term expropriation is applied to more discrete acts. However, 'distinguishing "nationalisation" from "expropriation" may indeed have little practical effect in the reality of international legal relations',[226] and, therefore, this distinction will be assumed to be of little relevance for the purposes of this discussion.

The description of direct expropriation in Annex 10-D largely reflects the position at customary international law.[227] For instance, the reference to property as constituting a tangible or intangible property right is consistent with the approach in NAFTA, as well as many other BITs.[228]

The reference to expropriation of a 'property interest in an investment' in paragraph 2 of Annex 10-D also makes it clear that a business may comprise numerous property rights, each of which may be subject to an expropriation. This is consistent with the approach of NAFTA tribunals in *Pope & Talbot* and *Myers* v. *Canada*, which both considered that a right to sell into a market can be a property interest separate from the investment.[229] Therefore, there is likely to be no difference in the scope of the obligation not to directly expropriate between those FTAs that include text equivalent to Annex 10-D of US–Chile, and those that do not include such a provision.

9. Indirect expropriation

Regarding the definition of indirect expropriation, Annex 10-D of the US–Chile FTA elaborates on what constitutes 'indirect expropriation', defining it as arising when 'an action or series of actions by a Party has an effect equivalent to direct expropriation without formal transfer of title or outright seizure'.

Paragraph 4 of Annex 10-D then establishes the following guidelines for determining when there is an indirect expropriation:

> (a) The determination of whether an action or series of actions by a Party, in a specific fact situation, constitutes an indirect expropriation, requires a case-by-case, fact-based inquiry that considers, among other factors:
>
> (i) the economic impact of the government action, although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred;

226 Martin Domke, 'Foreign Nationalizations: Some Aspects of Contemporary International Law' (1961) 55 (3) *American Journal of International Law* 585–616.

227 OECD, '"Indirect Expropriation" and the "Right to Regulate" in International Investment Law', OECD Working Papers on International Investment No. 2004/4 (September 2004), at p. 3.

228 See UNCTAD, above n. 180.

229 See *Pope & Talbot* (Interim Award of 26 June 2000), para. 96; and *Myers* v. *Canada*, paras. 292–6.

(ii) the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and
(iii) the character of the government action.

(b) Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations.

What constitutes an indirect expropriation requiring compensation, as distinct from a regulatory non-compensable measure, is ultimately a question about the scope of the expropriation obligation. This is because most regulations or series of regulations can have an impact on the economic value of an investment. For example, an environmental regulation can impose significant costs on business, and in some cases, render that business unviable. Alternatively, changes in a State's taxation regime can also impose large costs on business. The point at which the impact of a measure becomes severe enough so as to amount to an indirect expropriation has important implications on a Government's scope to regulate. This has led commentators to argue that too broad an expropriation obligation could lead to regulatory chill.[230]

As a result, international tribunals have long recognised that an assessment of whether a measure is an indirect expropriation or merely regulation that does not require compensation is largely determined by the particular facts of each case, thereby defying clear rules on how to draw this distinction.[231] Therefore, the statement in Annex 10-D paragraph 4(a) that an assessment of what constitutes indirect expropriation requires 'a case-by-case, fact-based inquiry', reflects the approach that tribunals must take when assessing claims of indirect expropriation.[232]

Where to draw the line between indirect expropriation and non-compensable regulation also reflects debate over the rationale for prohibiting expropriation. One approach is that the distinction between indirect compensation and non-compensable regulation is a question of when the cost of regulation should be borne by the individual instead of the State,[233] or that the expropriation obligation is justified by the principle of unjust enrichment.[234] Others have argued that the expropriation obligation is justified by a need to ameliorate a foreign investor's lack of 'voice' in the host states' political process, and the difficulty of exit due to the nature of direct investment, which makes foreign investors particularly susceptible

230 Vicki L. Been and Joel C. Beauvais, 'The Global Fifth Amendment? NAFTA's Investment Protections and the Misguided Quest for an International ''Regulatory Takings'' Doctrine' (2003) 78 *New York University Law Review* 30–143, at 132.

231 See *Saluka* v. *Czech Republic*, para. 265.

232 George C. Christie, 'What Constitutes a Taking of Property Under International Law?' (1962) 38 *British Yearbook of International Law* 307–38, at 338.

233 Rosalyn Higgins, 'The Taking of Property by the State: Recent Developments in International Law' (1982-III) 176 *Recueil des Cours* 259–392, at 276.

234 Andrew Newcombe, 'The Boundaries of Regulatory Expropriation in International Law' (2005) 20(1) *ICSID Review–Foreign Investment Law Journal* 1, at 34.

to incurring the costs of state laws.[235] A further more general rationale is that the expropriation obligation, like all other investor protection provisions in an FTA Investment Chapter, allow developing countries to commit to a level of protection in order to attract foreign investment.[236]

10. The economic impact of the government action

Under FTA Investment Chapters, the economic impact of the government action on the investment is one of the main determining factors of when an indirect expropriation has occurred.[237] The extent of the economic impact is also to be assessed in light of both its effect on legal title as well as the ability of the owner to use and enjoy their property.[238]

This was recognised in *Starrett Housing*, where the tribunal, assessing whether the appointment of Iranian managers to an American housing project constituted expropriation, stated that, 'it is recognized by international law that measures taken by a State can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated, even though the State does not purport to have expropriated them and the legal title to the property formally remains with the original owner'.[239] The duration of the regulation is also relevant.[240] Merely temporary takings will, under customary international law, not constitute expropriation.

Debate remains, however, over whether economic impact is the sole criteria for assessing whether a measure constitutes indirect expropriation, or whether other factors, such as the intent of the government, can be taken into account. These two approaches are referred to as the 'sole effect doctrine' and the 'government purpose doctrine'.

According to the 'sole effect doctrine', the effect of the measure on the investment is the dominant criteria.[241] Under the 'government purpose doctrine', a tribunal is able to take into account the purpose and context of the measure as well as its economic impact, allowing a tribunal to balance the goal of the measure with the harm to the property interest.[242] Rudolf Dolzer frames the issue as follows:

> [I]s there any specific point within the spectrum of diverse effects of governmental measures on property at which and beyond which compensation is

235 *Ibid.* See also Been and Beauvais, above n. 232, at 100–8, where they argue against this 'political process failure theory' as providing adequate justification for the expropriation obligation in NAFTA.

236 Rudolf Dolzer, 'The Impact of International Investment Treaties on Domestic Administrative Law' (2004–2005) 37(4) *New York University Journal of International Law & Politics* 953–72, at 954.

237 See OECD, above n. 229, at p. 10. 238 See Dolzer, above n. 189, at 79.

239 *Starrett Housing Corp.* v. *Islamic Republic of Iran* ('*Starrett Housing v. Iran*'), Iran–US Claims Tribunal (Award No. ITL 32–24–1 of 19 December 1983), 4 Iran-US CRT 122, p. 154.

240 See *Tecmed*, para. 116; and *Myers* v. *Canada* (Partial Award of 13 November 2000), para. 284.

241 See Dolzer, above n. 189, at 79.

242 OECD, 'Indirect Expropriation and Governmental Measures Affecting Property of Nationals Not Requiring Compensation: Criteria to Articulate the Difference', DAFFE/IME/WD/(2004)2 (26 March 2004), para. 28.

> required regardless of the objective and the nature of the governmental measure, or does the taking doctrine require a balance of interests which weighs the effect of the property on the one hand and the objective of the governmental measure on the other?[243]

The balancing approach is used by the European Court of Human Rights (ECHR) when applying Article 1 of Protocol 1 of the European Convention of Human Rights. In this context, the ECHR has required that the measure be proportionate to its goals and balances between the interests of the community in the measure and the private interests of the person who is bearing the cost of the measure.[244]

Customary international law does not prescribe one particular approach. A range of cases support either the sole doctrine approach or alternatively, have taken into account the purpose and object of the impugned measure. Cases that have taken the sole doctrine approach include the Permanent Court of International Justice in the *Factory at Chorzow* case[245] and tribunals in *Tippets* v. *TAMS-AFFA*, *Metalclad*, and *Antoine Biloune and Marine Drive Complex Ltd* v. *Ghana Investments Centre and The Government of Ghana*.[246] In contrast, the tribunals' decisions in *Myers* v. *Canada*, *Seal-Land Services, Inc.* v. *The Government of the Islamic Republic of Iran, Ports and Shipping Organization*,[247] *CME Czech Republic B. V. (The Netherlands)* v. *The Czech Republic*,[248] and *Revere Copper & Brass, Inc.* v. *Overseas Private Investment Corp*,[249] have approached the expropriation analysis in a manner that took into account the intent of the government in enacting the measure.

As a result of the divergence of case law on this matter, one commentator has argued that 'it is so far impossible to characterize either alternative approach as dominant or as representing the mainstream of international thinking'.[250]

In light of this uncertainty at customary international law, the US–Chile FTA Annex 10-D and all other equivalent provisions in the other FTA Investment Chapters have effectively taken a position on the appropriate weight to be given by a

243 See Dolzer, above n. 189, at 80.

244 Helen Mountfield, 'Regulatory Expropriations in Europe: The Approach of the European Court of Human Rights' (2002) 11(1) *New York University Environmental Law Journal* 136–47, at 141; see also *Tecmed*, para. 122.

245 *Factory at Chorzow (Germany* v. *Poland)*, 1928 PCIJ (Series A) No. 17 (Judgment of 13 September 1928).

246 *Antoine Biloune (Syria) and Marine Drive Complex Ltd (Ghana)* v. *Ghana Investments Centre and The Government of Ghana*, UNCITRAL Arbitral Tribunal (Award on Jurisdiction and Liability of 27 October 1989), 95 ILR 183.

247 *Sea-Land Services, Inc.* v. *The Government of the Islamic Republic of Iran, Ports and Shipping Organization*, Iran–US Claims Tribunal (Award No, 135–33–1 of 22 June 1984), 6 Iran-US CTR 149.

248 *CME Czech Republic B.V. (The Netherlands)* v. *The Czech Republic* (The Netherlands/Czech Republic BIT) (UNCITRAL Partial Award of 13 September 2001).

249 *Revere Copper & Brass, Inc.* v. *Overseas Private Investment Corp.* ('*Revere Copper v. OPIC*') (Award of 24 August 1978), 17 ILM 132 1 (1978).

250 See Dolzer, above n. 189, at 90.

tribunal to economic impact. In this regard, Annex 10-D paragraph 4(a)(i) directs a tribunal that when considering the economic impact of government action:

> [A]lthough the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred.

As a result, these FTA Investment Chapters make it clear that the sole effect doctrine is not to be used when establishing whether indirect expropriation has occurred, and instead, other factors, also elaborated on in the FTA Investment Chapter Annex, are to be taken into account. For those FTAs that do not include such provisions, the uncertain state of customary international law in this area means that tribunals have greater discretion to decide whether to focus on the economic impact as the sole criteria for assessing whether an indirect expropriation has occurred, or to weigh the economic impact with the intent of the measure.

11. Reasonable investment-backed expectations

The requirement in FTA Investment Chapters that a tribunal assess the 'extent to which the government action interferes with distinct, reasonable investment-backed expectations' is also a reflection of customary international law. The possibility that an investor's reasonable investment-backed expectations could effectively create an obligation on a state not to act in a particular manner has been analogised to the domestic law of estoppel, which similarly imports an inquiry into good faith.[251] While international tribunals have yet to explicitly equate an inquiry into reasonable expectation with an estoppel-like analysis, it has been recognised that, 'the principle of good faith is the corollary in public international law of the principle of protection of legitimate expectations'.[252]

Other international tribunals have described this as an inquiry into whether 'undertakings or assurances [were] given in good faith to such aliens as an inducement to their making the investment affected by the action',[253] or whether 'the treatment is in breach of representations made by the host State which were reasonably relied upon by the claimant'.[254]

In *Methanex*, the tribunal appeared to rely partly on equity to conclude that the US had not breached any representations made to Methanex by observing that Methanex had itself understood the role of lobbyists in forming regulation in the US and had in fact 'itself deployed lobbyists', suggesting that Methanex needed to come to the tribunal with clean hands before it could claim a breach of representation.[255]

251 See Been and Beauvais, above n. 232, at 72.

252 *Opel Austria GmbH* v. *Council of the European Union*, Case T-115/94, Court of Justice of the European Communities – Fourth Chamber, 22 January 1997, para. 93.

253 See *Revere Copper* v. *OPIC*, p. 1331. 254 See *Waste Management*, para. 98.

255 See *Methanex*, Part IV, Chapter D, para. 9.

International tribunals have also made it clear that the principle of reasonable expectations does not insulate an investor from risk associated with an investment in a foreign country. Therefore, changes of regulation in response to changing economic, social or political circumstances that impact on an investment will not necessarily be considered expropriations.[256]

12. Character of the government action and the police powers exception

The character of the government action refers to the right of a government to promote recognised social purposes and general welfare such as public health and safety. The extent to which a tribunal focuses on such purposes, will, at least to some extent, be a product of whether they consider economic impact the sole determinative criteria or whether they are prepared to balance economic impact with other legitimate government purposes.

When a State can show that the measure falls within its police powers, then no obligation to provide compensation will be deemed to have arisen.[257] The scope of the police powers exception remains open to debate.[258] However, a common starting point is the American Law Institute's Restatement (Third) of Foreign Relations Law of the United States, which includes within the scope of the police powers exception general taxation, regulation, forfeiture for crime, or other action of the kind that is commonly accepted as within the police power of the states.

There are two distinct conceptions of the role of the police powers exception. One conception is to understand the police powers exception as a controlling element that once established, provides a complete defence to any claims for compensation. An alternative approach is to include the police powers as a factor that is considered in the weighing and balancing of the measure. For example, Allen Weiner notes that a tribunal needs to examine 'whether a regulation is an exercise of the police power or is directed at a public welfare purpose, as opposed to a protectionist one'.[259] Under this approach, the distinction between a measure taken pursuant to the police powers and measures to pursue legitimate social purposes or welfare objectives blurs, and instead, a tribunal will need to examine the economic impact, and whether the measure is an exercise of its police powers or is directed at a public welfare objective.[260]

Those FTA Investment Chapters that include provisions equivalent to Annex 10-D of the US–Chile FTA have adopted this approach. This is because not only do

256 See *Starrett Housing v. Iran*; and *Feldman*.

257 See *Tecmed*, para. 119. 258 See *Saluka v. Czech Republic*, para. 263.

259 Allen S. Weiner, 'Indirect Expropriation: The Need for a Taxonomy of "Legitimate" Regulatory Purposes' (2003) 5(3) *International Law Forum (Du Droit International)* 166–75, at 175.

260 *Saluka* v. *Czech Republic*, para. 263, observed that, ' . . . international law has yet to identify in a comprehensive and definitive fashion precisely what regulations are considered "permissible" and "commonly accepted" as falling with the police or regulatory power of States and, thus, non-compensable'.

these provisions state that economic impact cannot on its own establish expropriation, but also paragraph 4(b) states that 'non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations'. Read together, these provisions make it clear that when interpreting Annex 10-D, a tribunal would be required to assess not only the economic impact and the legitimate investment-backed expectation of the investor, but will also need to take into account the purpose of the measure, and what goals it seeks to achieve. Certainly, where the measures are about health, safety and the environment, then it is likely that a tribunal will find that there is no indirect expropriation, even where there has been a complete taking of the investor's property.

However, Annex 10-D paragraph 4(b) of the US–Chile FTA is qualified, by the phrase 'in rare circumstances'. This phrase would operate such that once it is established that the measure falls within paragraph 4(b), the burden of proof would shift to the investor to establish that this was nevertheless a 'rare circumstance', where the measure should still be an indirect expropriation that requires compensation. No guidance is given in the FTA Investment Chapter provisions regarding what could constitute a rare circumstance. However, drawing on the approach of the ECHR and *Tecmed*, it could be argued that a lack of proportionality between the means employed to achieve the government's aim, could constitute a rare circumstance.[261]

In those FTA Investment Chapters that do not contain these more elaborate provisions on what constitutes indirect expropriation, then customary international law will apply. This may lead to a tribunal adopting the approach outlined above. However, given the uncertainty regarding the role of the police powers exception and whether it is a controlling factor, or merely one that is part of the overall assessment of whether the government action constitutes expropriation, then 'it is plausible that a balancing concept may, in such areas as environmental law, yield results different from those reached under an analysis focused only on the effect of the measure'.[262] For example, the *Metalclad* tribunal refused to consider the purpose for which the Mexican Government enacted the Ecological Decree.[263] Instead, the tribunal found that the Decree's effect of barring work at the landfill site constituted expropriation.[264]

F. Performance requirements

FTA Investment Chapters that include an agreement to prohibit performance requirements are a common feature of FTA Investment Chapters.[265] Provisions on

261 See *Tecmed*, para. 122; and Mountfield, above n. 246, at 141.

262 See Dolzer, above n. 189, at 80. 263 See *Metalclad*, para. 111. 264 *Ibid.*, para. 109.

265 US–Chile FTA, Article 10.5; AUSFTA, Article 11.9; Korea–Chile FTA, Article 10.7; CAFTA–DR–US, Article 10.9; Japan–Singapore EPA, Article 75; Korea–Singapore FTA, Article 10.7 and India–Singapore CECA, Article 6.23.

performance requirements in FTA Investment Chapters are derived from the WTO TRIMS agreement. Under these provisions, the Parties agree not to condition the ability of investors from the other FTA from making an investment in their territory, on that investor undertaking various acts, such as exporting a given amount of goods or services or using a certain amount of domestic goods or services in their investment.

A number of FTA Investment Chapters include performance requirements that are WTO TRIMS-Plus. TRIMs-Plus commitments are found in the US–Chile, AUSFTA, CAFTA–DR–US, Korea–Chile and Japan–Singapore.[266] These obligations extend to services, and include commitments not to require an investment to transfer 'technology, a production process or other proprietary knowledge to a person in its territory'.[267]

In certain FTAs, such as Canada–Chile and Korea–Chile, these TRIMs-Plus performance requirements also include a commitment to apply these obligations towards all investments in its territory.[268] Alternatively, the Korea–Singapore FTA (Footnote 10-3) requires an investor from the FTA part to show that they have suffered 'loss through the imposition of performance requirements to an investment of investor [sic] of a non-party', before the obligation not to impose performance requirements on investments from non-Parties arises. Therefore, while the legal commitment is bilateral only, failure to apply the performance requirements commitments to investments of non-parties would breach the FTA.

The rationale for including 'multilateral' Performance Requirement commitments within an FTA is to avoid the otherwise adverse incentive that would arise. This is because should an FTA Party remain free to impose performance requirements on all investments other than those from the other Party to the FTA, an incentive to prefer investments from non-Parties would be created as these investments could be required to comply with performance requirements.

Many of these TRIMS-Plus performance requirements are nevertheless subject to a range of exceptions. For example, under the Canada–Chile FTA, either Party can condition receipt of an advantage in connection with an investment in its territory on compliance with a requirement to do the following in its territory: (i) locate production; (ii) provide a service; (iii) train or employ workers; (iv) construct or expand particular facilities; (v) carry out research and development.[269]

The India–Singapore CECA is an example of an FTA that includes commitments on performance requirements that do not go beyond their TRIMS commitments. However, because the TRIMS Agreement only includes an indicative list of what

266 US–Chile FTA, Article 10.5; AUSFTA, Article 11.9; CAFTA–DR–US, Article 10.9; Korea–Chile FTA, Article 10.7 and Japan–Singapore CECA, Article 75.

267 Canada–Chile FTA, Article G-06.

268 *Ibid*., Article G-01.1(c); and Korea–Chile FTA, Article 10.2.1(c).

269 Canada–Chile FTA, Article 6–06.4.

constitutes a TRIMS, there is nothing in the text of the TRIMS Agreement that prohibits a WTO Member arguing for the TRIMS disciplines to be applied to requirements not in the indicative list; an outcome apparently confirmed by the Panel in *Canada–Automotive Industry*.[270]

This lack of certainty regarding the scope of the TRIMS Agreement is why many FTA Investment Chapters that are TRIMS-Plus also include a provision clarifying that the performance requirements listed therein 'do not apply to any other requirement other than the requirements set out in those paragraphs'.[271]

V. Investor-State dispute settlement (ISDS) provisions in FTA Investment Chapters

This Part looks at the different types of ISDS provisions in FTA investment chapters. ISDS provisions are a common feature of BITs and have been incorporated into most FTA Investment Chapters. However, the scope and substance of ISDS provisions in FTAs differ widely. As a general matter, the different approaches can be classified broadly into those that adopt the NAFTA approach to ISDS and those that continue to follow the BIT approach to ISDS. There are also a few FTA Investment Chapters, such as the AUSFTA, that do not include ISDS provisions.[272]

Under the BIT approach, ISDS provisions are generally limited to confirming that the Parties consent to international arbitration and to providing investors with a right to commence arbitration under either the ICSID Convention or the ad hoc UNCITRAL Arbitration Rules.[273] This approach has been continued in FTA Investment Chapters such as the Korea–Singapore FTA.

The NAFTA-style approach goes beyond the BIT approach to ISDS by specifying in detail the arbitration procedures to be followed by a tribunal, including a number of provisions not found in ICSID or UNCITRAL. For example, provisions for consolidation of claims, procedural mechanisms avoiding frivolous claims, commitments regarding transparency, appointment of experts and the right for

270 Panel Report, *Canada–Automotive Industry*, para. 10.89. 271 US–Chile FTA, Article 10.5.4.

272 Note that AUSFTA Article 11.16 does include a commitment to enter into consultations with a view towards allowing an ISDS claim and establishing ISDS procedures upon request from a Party based on a change of circumstances affecting the settlement of disputes within the scope of the FTA Investment Chapter; see also William S. Dodge, 'Investor-State Dispute Settlement Between Developed Countries: Reflections on the Australia–United States Free Trade Agreement' (2006) 39(1) *Vanderbilt Journal of Transnational Law* 1–38, at 22, who argues that an optimal approach in AUSFTA would require the investor to exhaust local remedies after which it could resort to international arbitration; see also Ann Capling and Kim R. Nossal, 'Blowback: Investor-State Dispute Mechanisms in International Trade Agreements' (2006) 19(2) *Governance*: *An International Journal of Policy, Administration, and Institutions* 151–72, who present reasons why Australia and the US agreed not to include an investor-State dispute mechanism in AUSFTA and its implications for future FTA Investment Chapters.

273 See, e.g., Korea–Singapore FTA, Article 10.19.

the tribunal to accept amicus briefs are additional ISDS provisions which are absent from the ICSID and UNCITRAL arbitration rules.[274]

Some FTA Investment Chapters, such as the Japan–Singapore EPA, have adopted a middle of the road approach or NAFTA-lite, whereby they have incorporated only some of these more detailed ISDS procedural provisions. The following is an analysis of the more significant FTA/ISDS provisions.

A. Scope of the ISDS provisions

In most cases, those persons that can claim under an FTA ISDS provision will be the investor of the other FTA Party. For example, the US–Chile FTA allows a claim to be made by an investor of the other Party on its own behalf or on behalf of its investment in the territory of the other Party.[275]

FTA ISDS provisions in Canada–Chile and Korea–Chile further limit the scope of their ISDS provisions by not allowing an investment (i.e., the domestic legal entity created by the investor) to make a claim under the ISDS provisions.[276] These provisions ensure that it is the investor of the other Party that is the party to the ISDS action. A similar outcome is achieved in the India–Singapore CECA where 'an enterprise duly organized under the law of a Party shall not be treated as an investor of the other Party, but any investments in that enterprise by investors of that other Party shall be covered under this Chapter'.[277] Prohibiting the investment from bringing a claim avoids a host Government being engaged in international arbitration against a company that is its own national.[278]

1. Frivolous claims

Several FTA Investment Chapter ISDS provisions seek to reduce the possibility that investors may raise frivolous claims. For example, the US–Singapore FTA and US–Chile FTA state that 'a tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favour of the claimant may be made'.[279] These ISDS provisions also allow a tribunal in these instances to award costs and attorney fees against the prevailing party.[280]

274 Followed by the US–Chile FTA, Articles 10.14–10.26; CAFTA–DR–US, Articles 10.15–10.27; and Korea–Chile FTA, Article 10.19–10.42. See also UNCTAD, *Dispute Settlement: State–State*, UNCTAD Series on Issues in International Investment Agreements (New York and Geneva: UN, 2003).

275 US–Chile FTA, Article 10.15.

276 Canada–Chile FTA, Article G–18.4; and Korea–Chile FTA, Article 10.21.

277 Singapore–India CECA, Article 6.2.2.

278 UNCTAD, *Investment Provisions in Economic Integration Agreements* (New York and Geneva: UN, 2006), at p. 119.

279 US–Singapore FTA, Article 15.19.4; and US–Chile FTA, Article 10.19.4.

280 US–Singapore FTA, Article 15.19.6; and US–Chile FTA, Article 10.19.6.

B. Appointment of arbitrators under ICSID and UNCITRAL

The ISDS provisions in FTA Investment Chapters allow an investor of either Party to submit a claim to arbitration under either the ICSID or UNCITRAL rules.[281] ICSID and UNCITRAL both contain detailed provisions on the appointment of arbitrators.[282] Under those FTAs that adopt the BIT-style approach, such as the India–Singapore CECA and Korea–Singapore FTA, the process for appointing arbitrators is determined solely by whether the investor chooses to submit a claim under the ICSID or UNCITRAL arbitration rules.[283]

In contrast, those FTAs that use the NAFTA-style ISDS provisions, such as Korea–Chile, US–Chile, Canada–Chile and the Japan–Singapore EPA, include detailed provisions regarding the appointment of arbitrators that operate in conjunction with the ICSID or UNCITRAL processes.[284]

2. Number of arbitrators

Where an investor submits a dispute for settlement under the UNCITRAL Arbitration Rules, Article 5 provides that should the parties to the dispute fail to agree on one arbitrator, then the tribunal is to comprise three arbitrators. Arbitration under ICSID is not limited to either one or three arbitrators as under Article 37.1 a tribunal can comprise one or any uneven number of arbitrators. However, Article 37.2(b) requires a tribunal to consist of three arbitrators when the parties fail to agree on the number of arbitrators.

The ISDS provisions in both the Korea–Singapore FTA and the India–Singapore CECA do not specify whether a tribunal is to comprise either one or three arbitrators. Therefore, it is possible that arbitration under these FTAs that use the ICSID Convention could be before a Panel comprising more than three arbitrators.

Those FTA Investment Chapters that provide greater direction on the appointment of arbitrators all require a tribunal to comprise three arbitrators unless the disputing parties otherwise agree.[285] This forecloses the option in ICSID of a tribunal comprising more than three arbitrators.

3. Appointment of arbitrators

UNCITRAL and ICSID also provide different processes for the appointment of arbitrators. Under Article 7.1 of the UNCITRAL Arbitration Rules, each Party is

281 See, e.g., US–Singapore FTA, Article 15.15.5; Canada–Chile FTA, Article G-21; and India–Singapore CECA, Article 6.21.3.

282 See ICSID Convention, Articles 27–40; and UNCITRAL Arbitration Rules, Articles 5–8.

283 India–Singapore CECA, Article 6.21; and Korea–Singapore FTA, Article 10.19.

284 Korea–Chile FTA, Chapter 10, Section C; US–Chile FTA, Chapter 10, Section B; Canada–Chile FTA, Chapter G, Section II; and Japan–Singapore EPA, Article 82.

285 See, e.g., Canada–Chile FTA, Article G–24; Korea–Chile FTA, Article 10.27; and US–Chile FTA, Article 10.18.

required to appoint an arbitrator and for these two arbitrators to agree on the third arbitrator. In contrast, Article 37.1(2) of the ICSID Convention requires each disputing party to appoint an arbitrator and for the disputing parties to agree on the appointment of the third and presiding arbitrator.

Under ICSID, if either Party to the dispute fails to appoint an arbitrator, the ICSID Chairman, defined as the President of the World Bank, appoints those arbitrators not yet appointed from the Panel of Arbitrators.[286]

In contrast, UNCITRAL adopts different approaches for appointing an arbitrator that a Party to the arbitration failed to appoint, and for appointing the third arbitrators that the other two arbitrators failed to appoint. In the first case, the appointing authority, to be agreed upon by the parties, is to appoint the arbitrator/s not appointed by the Parties to the arbitration. In the event the Parties fail to agree on an appointing authority, Article 7.2(b) requires the Secretary-General of the Permanent Court of Arbitration at The Hague to designate an appointing authority. This appointing authority can then be requested by a party to appoint the second arbitrator. The use of the word 'request' indicates that there is no legal relation or obligation created by the UNCTIRAL Arbitration Rules between the party to the dispute and the appointing authority, and therefore no guarantee that the person so designated will agree to act.

In the second case, Article 6 of the UNCITRAL Arbitration Rules requires the appointing authority to use a 'list-procedure' unless that person decides that this process is not appropriate. Should this be the case, however, no guidance or provision is made for how the third arbitrator is to be appointed. The 'list-procedure' requires the appointing authority to provide each Party a list of three identical names. Each Party 'may' return the list with names they object to being removed from the list and those names not objected to being listed in order of preference. The appointing authority is then to select the arbitrator from the names 'approved on the lists returned to it and in accordance with the order of preference indicated by the parties'. Should all names on the list be rejected or the list not be returned to the appointing authority, then that person is given the discretion to appoint the third arbitrator, but again, this is not an obligation, leaving it open to the appointing authority to refuse to exercise that discretion.

In those FTA Investment Chapters that adopt the NAFTA-style approach to ISDS, each Party commits to appointing an arbitrator, and the third arbitrator is to be appointed by agreement between the disputing parties.[287] The ICSID Secretary-General is also designated as the appointing authority under all these FTAs and has also agreed to act as appointing authority for disputes under ICSID or UNCITRAL arbitration rules. Therefore, where either of the disputing parties fail to appoint their

286 ICSID Convention, Article 38.

287 See, e.g., the Canada–Chile FTA, Article G–24; Korea–Chile FTA, Article 10.27; and US–Chile FTA, Article 10.18.

own arbitrator, the ICSID Secretary-General is required to appoint these arbitrators using his or her discretion, but subject to the requirements of nationality, as outlined above, in UNCITRAL or ICSID.

This approach in FTA Investment Chapter ISDS provisions removes the potentially lengthy process under UNCITRAL for finding the appointing authority and uncertainty over whether that appointing authority will act to appoint arbitrators. It is also a departure from ICSID which designates the President of the World Bank as the appointing authority.[288]

One of the potential consequences of this departure from the ICSID approach is that whereas the President of the World Bank, pursuant to Article 40(1) of the ICSID Convention, is required to appoint arbitrators from the Panel of Arbitrators, the ICSID Secretary-General would appear free to appoint an arbitrator from outside the Panel.

As a result of this greater freedom granted to the ICSID Secretary-General to appoint arbitrators, some FTA Investment Chapter ISDS provisions also direct how the ICSID Secretary-General is to exercise their discretion to appoint the presiding arbitrator.[289] In these FTAs, the ICSID Secretary-General is to appoint the presiding arbitrator from a roster of thirty arbitrators, appointed by agreement between the FTA Parties. Should no arbitrator on this roster be available to serve, the ICSID Secretary-General has the authority to appoint arbitrators from the ICSID Panel of Arbitrators.

In contrast, other FTAs do not establish a roster of panellists and indeed do not provide any direction on how the ICSID Secretary-General is to exercise their power to appoint an arbitrator. Therefore, by default, the applicable arbitration rules under either ICSID or UNCITRAL will apply.[290]

Interestingly, the Japan–Singapore EPA, while content to largely rely on the provisions in the applicable arbitration rules for the appointment of arbitrators, contains limitations on how the Chairman under ICSID can exercise its authority to appoint arbitrators. This is achieved in Article 82.4(b) by conditioning each Party's consent to arbitration under ICSID on the Chairman allowing the disputing parties to indicate three nationalities whose appointment to a tribunal would be unacceptable to it, and by not appointing persons of these nationalities to a tribunal.

In the event that the Chairman acts inconsistently with this direction, then the Parties' consent to arbitration under ICSID only is vitiated; however, arbitration under the other arbitration rules listed in that FTA, namely UNCITRAL, is able to proceed. This approach therefore seeks to incorporate the UNCITRAL 'list-procedure' for selecting arbitrators under ICSID.

288 ICSID Convention, Article 37(2)(b).
289 See, e.g., Canada–Chile FTA, Article G–25; and Korea–Chile FTA, Article 10.28.
290 See, e.g., US–Chile FTA, Article 10.18.

C. Consolidation

Some FTAs now provide for the consolidation of different investment disputes under the same agreement regarding the same measure.[291] There is no provision for the consolidation of investment disputes under either ICSID or UNCITRAL, and therefore it is only possible where provided for by the ISDS provisions in the FTA.

The NAFTA-style ISDS provisions usually include consolidation provisions. For example the US–Chile FTA allows for consolidation '[w]here two or more claims have been submitted separately to arbitration under Article 10.15(1) and the claims have a question of law or fact in common and arise out of the same events or circumstances'.[292]

These consolidation provisions usually require a party to request a consolidation of claims, after which a third tribunal is established to consider the request and to either assume jurisdiction and to hear and determine together all the claims in the request, to determine part of a claim that will assist in the resolution of the other claims, or to instruct one of the original tribunals to assume jurisdiction and hear and determine all of the claims.

D. Transparency of arbitral proceedings

There are a number of different approaches to the transparency and openness of tribunals under the ISDS provisions in FTA Investment Chapters. Whether an ISDS process is open and transparent is a function of the extent to which tribunal hearings are open to the public, and there is access of the public to documents in a dispute, including the tribunal's award.

One approach is not to address these issues of transparency and openness in the ISDS provisions, and instead, to rely on the procedures, where they exist, in the applicable arbitration rules. This is the approach taken in numerous FTAs, such as Korea–Singapore, India–Singapore CECA, Japan–Singapore EPA and the Thailand–Australia FTA.[293] Some FTAs allow either Party to the dispute to publish the award.[294]

With respect to the publication of tribunal awards, both UNCITRAL and ICSID require the consent of the Parties. However, under ICSID Rule 48(4), the centre will publish 'exerpts of the legal reasoning of the tribunal'. Some FTAs allow either Party to the dispute to publish the award. Further, neither ICSID nor UNCITRAL allow for non-parties to the dispute to attend hearings.

An alternative approach being taken in FTA Investment Chapter ISDS provisions, such as the US–Chile FTA, CAFTA–DR–US and NAFTA, is to include detailed

291 *Ibid*., Article 10.24; CAFTA–DR–US, Article 10.25; and US–Singapore FTA, Article 15.24.

292 US–Chile FTA, Article 10.24.

293 Korea–Singapore FTA, Article 10, Section C; India–Singapore CECA, Article 6.21; Japan–Singapore EPA, Article 82; and Thailand–Australia FTA, Article 917.

294 See Korea–Chile FTA, Article 10.41.4 and Annex 10.41.4.

obligations regarding the transparency and openness of tribunals that are significant departures from the limited transparency and openness that currently exists under ICSID or UNCITRAL.

These FTAs require the parties to the dispute to make all documents in an ISDS dispute to be made available to the public, subject to a right to remove confidential information. All hearings of the tribunal are to be open to the public, with provision for closing these hearings for presentation of confidential information.

E. Amicus *briefs*

Those FTAs Investment Chapters ISDS provisions that emphasise the transparency and openness of the ISDS process also tend to expressly include a right for a tribunal to accept amicus briefs. This approach is also consistent with how tribunals have understood the scope of their power under both the UNCITRAL arbitration rules and ICSID arbitration rules. For instance, the tribunals in *Methanex* and *UPS*, constituted under the UNCITRAL Arbitration Rules, interpreted Article 15.1 as providing them with the procedural power to accept amicus briefs.[295] However, they also made it clear that receipt of amicus does not confer rights, procedural or substantive, on the persons submitting the amicus briefs. The tribunals also noted that in deciding whether to accept or reject amicus briefs, they would consider whether the substantive matters in the dispute had a public interest dimension.

Similarly, the tribunal in *Vivendi Universal, S.A.* v. *The Argentine Republic*, constituted under the ICSID Convention, found that it has the power to receive amicus briefs pursuant to ICSID Convention Article 44.[296] The tribunal also noted that in determining whether to accept amicus, the tribunal shall consider the appropriateness of the subject matter as a basis for amicus submissions, whether the case involves matters of significant public interest, and that the tribunal will only accept amicus from persons who establish that they have the expertise, experience and independence to be of assistance. Similar to the *Methanex* tribunal, the tribunal in *Vivendi* noted that it would not accept amicus on jurisdictional issues.

VI. The architecture of FTA Investment Chapters

This Part outlines the different ways that States can make market access commitments to their FTA Investment Chapter commitments and considers the arguments for and against each approach.

295 See *Methanex*, para. 47; and *UPS* v. *Canada*, Decision of the Tribunal on Petitions for Intervention and Participation as Amicus Curiae (17 October 2001), para. 67.

296 *Aguas Argentinas, S.A., Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A.* v. *The Argentine Republic* ('*Vivendi*'), ICSID Case No. ARB/03/19, Order in Response to a Petition for Transparency and Participation as Amicus Curiae (12 February 2007), para. 14.

A. Investment liberalisation – Negative or positive list

All FTA Investment Chapters include schedules wherein parties make their market access commitments to which the substantive commitments in the investment chapter apply. There are two main approaches for listing market access commitments in an FTA, namely through use of a positive or a negative list of commitments.

The positive list is a GATS-style approach, whereby member States list those sectors which they are prepared to subject to the FTA Investment Chapter commitments.[297] There are a number of FTAs that have adopted a positive list approach to scheduling commitments on investment, such as the Thailand–Australia FTA and the Japan–Singapore EPA.[298]

In contrast, under the negative list approach to scheduling FTA Investment Chapter commitments, all measures affecting investment in all sectors of the economy are required to be in conformity with the FTA Investment Chapter unless otherwise specified in a list of reservations to the FTA. Numerous FTA Investment Chapters have adopted the negative list approach to scheduling commitments, including AUSFTA, Canada–Chile, Korea–Singapore and CAFTA–DR–US.[299]

The negative list approach also normally includes two lists or annexes. Under Annex I, States list those non-conforming measures that they agree not to make any more non-conforming or restrictive. This is often referred to as a standstill commitment. Some FTA Investment Chapters, such as Korea–Singapore, Canada–Chile, and the Japan–Singapore EPA, also subject measures listed in Annex I to a 'ratchet mechanism', whereby any future amendment to a measure in that Annex that brings it into greater conformity with the FTA automatically becomes an international commitment or binding. The effect being that the measure cannot then be returned to its original non-conforming state without being in breach of the FTA.

In Annex II, States list those sectors with non-conforming measures they may wish to maintain or make more restrictive in the future. Annex II can also be used by a State to list those sectors in which a State desires the flexibility to introduce new measures which may not conform to their FTA commitments.

1. Positive list versus the negative list

In theory, the same level of liberalisation is achievable under either a positive or negative list approach to the scheduling of commitments. Under a positive list

297 Note that the GATS is a positive list for the national treatment and market access commitments, but that it adopts a negative list approach for the MFN commitment.

298 India–Singapore CECA, Article 6.16, Annexes 6A and 6B; and Japan–Singapore EPA, Article 76, Annexes VA and VB. The Thailand–Australia FTA uses a hybrid approach, whereby a positive list is used to make market access commitments to the pre-establishment NT commitment (see Article 904), and a negative list is used to make market access commitments to the post-establishment NT commitment (see Article 907).

299 AUSFTA, Article 11.13, Annexes I and II; Canada–Chile FTA, Article G–08, Annexes I and II; Korea–Singapore FTA, Article 10.9, Annexes I and II; and CAFTA–DR–US, Article 10.13, Annexes I and II.

approach, the schedule reflects those sectors in which commitments (with their limitations) are taken, and by extension it can be assumed that those sectors without commitments contain a State's non-conforming measures. Under a negative list approach, those non-conforming measures are listed in either Annex I or Annex II, and there is a legal obligation that all other measures not listed are consistent with the FTA Investment Chapter commitments.

However, empirical evidence suggests that states that use a negative list approach are more likely to make more extensive commitments with less carve-outs than under a GATS style positive list approach.[300] In addition, under a negative list approach, unless provision is made in Annex II to the FTA Investment Chapter, new investment regulation is automatically bound by the FTA Investment Chapter commitments.

Significant from the perspective of increasing investor confidence and certainty, a negative list also provides greater transparency because all relevant investment restrictions are contained in the reservations. This is in contrast to the positive list approach, which only shows investors those sectors where commitments are taken, but does not reveal the range of non-conforming measures that remain. Further, where a State, in order to retain policy flexibility, chooses not to make a treaty level commitment by binding a measure, there may be measures that are consistent with its FTA Investment Chapter commitments that are not included in a positive list.

States, however, may prefer a positive list approach due to the administrative costs associated with preparing a negative list. Because under a negative list all measures are bound unless listed, States need to do a stock-take of all measures and assess those measures conformity with the investment (and services) chapter. Where the measures are not in conformity a further decision needs to be taken whether to list that measure as a standstill commitment in Annex I, or when flexibility to increase the non-conformity of the measure is required, in Annex II.

In contrast, a positive list approach only requires States to consult with affected stakeholders. In most cases, many of these consultations may have taken place in the GATS context, and therefore States only have to consult with those stakeholders where GATS (mode 3)-plus and investment commitments in the non-services sectors are being made.

B. Investment in services – the investment or services chapter?

In a number of FTAs, the Services Chapter also contains important rules on investment. This will depend on whether the provision of a service through a commercial presence, or mode 3 in WTO speak, is included within the FTA's Services or Investment Chapter.

300 WTO Economic Research and Statistics Division, 'Services Liberalization in the New Generation of Preferential Trade Agreements (PTAs): How Much Further than the GATS?', Staff Working Paper ERSD-2006–07 (September 2006), at p. 55.

FTAs such as Japan–Singapore, Thailand–Australia, EU–Chile and India–Singapore all include mode 3 provision of service in the Services Chapters.[301] In contrast, FTAs such as AUSFTA, CAFTA–DR–US , Korea–Chile, US–Singapore, and Korea–Singapore, do not include mode 3 in the Services Chapter, with the result that these types of investments are captured by the broad definition of an 'investment' in the Investment Chapter.[302]

VII. Prospects for FTA Investment Chapters

Looking forward, the trend towards comprehensive investment provisions as part of bilateral and regional FTAs will continue. This reflects an appreciation of the synergies gained from a comprehensive regulatory approach to trade and investment and is consistent with the economic literature that shows trade and investment not necessarily as substitutes, but also as complements.[303]

The use of increasingly complex and comprehensive investment provisions in FTAs is nevertheless going to raise a number of challenges for States. In particular, a number of specific investment provisions are, and will remain, controversial.

One of these is the commitment on expropriation and specifically the meaning of indirect expropriation. As traditionally capital exporting States increasingly become defendants, either in State-to-State, though more often in investor-State arbitrations, the need to balance investment protection with ensuring adequate policy space for governments to regulate, will become increasingly important.

As discussed above, a number of FTAs, such as AUSFTA, US–Chile FTA and the India–Singapore CECA, include detailed provisions on what constitutes indirect expropriation.[304] These expropriation provisions were initiated by the US in the FTAs it entered into after NAFTA and can therefore be understood as a response to concerns that legitimate government regulation was being challenged as inconsistent with the NAFTA expropriation commitment. In this regard, it is interesting to note that expropriation claims under NAFTA against the US involved claims of indirect expropriation. These concerns over the proper scope of expropriation provisions are not necessarily only a developed country issue. Therefore, to the extent that these provisions on indirect expropriation strike the appropriate balance between the

301 Japan–Singapore EPA, Article 58; Thailand–Australia FTA, Article 802; EU–Chile AA, Article 96; and India–Singapore CECA, Article 7.1.

302 AUSFTA, Article 10.14; CAFTA–DR–US, Article 11.14; Korea–Chile FTA, Article 11.1; US–Singapore FTA, Article 8.1; and Korea–Singapore FTA, Article 9.1.

303 See OECD, 'Linkages Between Foreign Direct Investment, Trade and Trade Policy: An Economic Analysis with Application to the Food Service in OECD Countries and Case Studies in Ghana, Mozambique, Tunisia and Uganda', OECD Trade Policy Working Paper No. 50 (2 March 2007), at p. 19; and UNCTAD, *Trade and Development Report 2006* (New York and Geneva: UN, 2006), at pp. 157–8; see generally UNCTAD, *World Investment Report 1996: Investment, Trade and International Policy Arrangements* (New York and Geneva: UN, 1996).

304 AUSFTA, Annex 11–B; US–Chile FTA, Annex 10-D; and India–Singapore CECA, Annex 3.

right of Governments to regulate and the obligation to compensate investors for an expropriation, it is likely that such provisions will become increasingly prevalent in future FTAs.

Similarly, the NAFTA Interpretative Note regarding the fair and equitable treatment standard also reflects the NAFTA Parties experience being the defendant in investor-state dispute settlement action. The controversy over these provisions are similar to those raised with regard to the expropriation commitment, in that they are fundamentally about the appropriate balance between investment protection on the one hand and the ability of governments to regulate, on the other hand.

This growing awareness of the costs and benefits of strong investment protection and the political issues it raises for States when they are the defendants in ISDS arbitration begs the question whether future investment provisions will have a greater emphasis on investment liberalisation instead of investment protection. If we assume that the era of ideological opposition to foreign investment is largely over, and instead, the developmental benefits of foreign investment are now widely understood, it seems reasonable to expect that investment provisions in FTAs will increasingly focus on rights of establishment of foreign investment and become less concerned with their protection once the investment has occurred.[305]

Another potential development is negotiations on investment in the WTO. Some commentators have argued that Doha will be the last comprehensive multilateral trade round.[306] However, should investment be included within the WTO, a range of consequences for the future of FTA Investment Chapters present themselves. In the case that an investment agreement in the WTO included commitments as comprehensive as those in FTAs such as US–Chile, then Investment Chapters may become less likely in FTAs, or, FTA Investment Chapters will become similar to FTA SPS and TBT Chapters, whereby the Parties largely use them to reaffirm their WTO commitments.[307] However, should an investment agreement in the WTO represent the lowest common denominator, then FTA Investment Chapters will be likely to continue to provide a forum where States can go further than their WTO commitments.

The proliferation of different investment provisions in FTAs could, however, be a hurdle to multilateral investment negotiations. This is because States may seek to replicate their FTA investment commitments in a multilateral investment agreement, thereby making consensus on multilateral investment rules increasingly difficult.

Nevertheless, it is suggested that the increase in investment provisions in FTAs may themselves generate, over time, a number of forces towards developing a multilateral investment agreement at the WTO. One of these is what is often referred to as the 'spaghetti bowl' effect of FTAs, the potential for one country being bound

305 See also Kurtz, above n. 19, at 780.

306 Daniel K. Tarullo, 'The End of the Big Trade Deal: Why Doha Will Be the Last of the Grand Multilateral Trade Negotiations', *The International Economy*, 22 June 2006, p. 46.

307 See John Whalley, 'Recent Regional Agreements: Why So Many, Why So Much Variance in Form, Why Coming So Fast, and Where Are They Headed?', CESifo Working Paper No. 1790 (August 2006), at p. 26.

by a number of different investment rules.[308] In a globalised world where multinational enterprises disaggregate their production processes amongst many different countries, a spaghetti bowl of investment rules will cause increased transaction costs, possibly enough to create an important constituency in favour of a multilateral agreement on investment. However, where a multilateral agreement on investment departed from a State's investment commitments under an FTA, particularly if it represented a lowest common denominator, it may enhance the spaghetti bowl effect as States assumed investment treaty commitments at both the multilateral and the bilateral level.

Secondly, as investor-State dispute settlement provisions become a common part of FTA Investment Chapters, the potential for conflicting decisions will increasingly undermine, rather than enhance, the certainty and predictability that these provisions seek to create.[309] Consistency of arbitral decisions on investment could be addressed by establishing an appellate mechanism, something the Parties to CAFTA–DR–US have already agreed to do.[310] The desire for coherence amongst investment disputes is also likely to lend support for coherent investment rules in the form of a multilateral agreement on investment.

308 See generally Joost Pauwelyn, 'Adding Sweeteners to Softwood Lumber: The WTO–NAFTA ''Spaghetti Bowl'' is Cooking' (2006) 9(1) *Journal of International Economic Law* 197–206.

309 International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, Report of the Study Group (finalised by Martti Koskenniemi), UN Doc. A/CN.4/L.682 (4 April 2006), para. 419.

310 CAFTA–DR–US, Annex 10–F; the Parties to the US–Singapore FTA Article 15.26 and the Exchange of Letters on an Appellate Mechanism have agreed to consider within three years of entry into force of the FTA whether to establish an appellate mechanism to review ISDS rewards; see generally Susan D. Franck, 'The Nature and Enforcement of Investor Rights under Investment Treaties: Do Investment Treaties have a Bright Future?' (2005) 12(1) *University of California Davis Journal Of International Law & Policy* 47–100, at 62–6, for an outline of the implications of inconsistent decisions for investment treaty arbitration.

10

Government procurement

ARWEL DAVIES

I. Introduction

Public procurement is the activity whereby public entities contract with external private providers for the supply of the goods and services they require to carry out their functions. The overwhelming majority of bilateral and regional preferential-trade agreements (PTAs) seek to regulate this activity, or at least set out a commitment to do so. Of the seventy-seven or so agreements that have entered into force since January 2000,[1] only eleven make no reference to procurement. Of the remaining sixty-six agreements, forty-two recognise the liberalisation of procurement markets, and the need to develop procurement disciplines, as objectives. A further six agreements go further than this in that they presently seek to regulate procurement with the use of general principles.[2] The remaining eighteen agreements can be described as fully fledged systems of international regulation in the sense that general principles are supplemented with detailed rules on contract award procedures.[3]

Part II of this chapter discusses why procurement is subject to international regulation. At a certain level, the rationale for international regulation can be easily explained and understood. Discrimination against foreign suppliers in procurement markets can amount to a significant barrier to trade. International regulation therefore seeks to address distortions in the conditions of competition between domestic and foreign suppliers which can be caused by 'buy-national' tendencies and measures.

Beyond this explanation however, explaining the rationale for international regulation, and its relationship with national regulation, throws up some challenging conceptual issues which can be introduced as follows. Disciplines of non-discrimination serve the same purpose in the procurement context as they do in any other trade context. One way to put it is that non-discrimination facilitates the

1 The figures are drawn from the table of bilateral and regional trade agreements notified to the WTO available on www.worldtradelaw.net as of February 2007.

2 Examples are Chapter 11 of the Japan–Mexico Economic Partnership Agreement (Japan–Mexico EPA) and Part 6 of the Central America–Panama Free Trade Agreement (El Salvador–Panama).

3 Examples are Chapter 9 of the Central America–Dominican Republic–United States Free Trade Agreement (CAFTA–DR–US) and Title IV of the European Union–Chile Association Agreement (EU–Chile AA).

materialisation of the benefits of competition in the market place. However, there is room to question whether, in the procurement context, the identity of the purchaser as a public body not directly subject to market forces means that non-discrimination might not, on its own, be sufficient to achieve its intended end. While private purchasers subject to market forces will tend to purchase the most suitable goods and services at the lowest available price, the same supposition does not apply as immediately to public purchasers not directly subject to market forces. The question is, therefore, whether international rules need to be concerned not only with non-discrimination, but also with value for money – something which is generally regarded as an objective of only national regulation. It is argued that the objectives of international and national procurement regulation cannot be so conveniently distinguished and compartmentalised. Indeed, there is evidence that some international rules are concerned with value for money.

Part II further explains these thoughts, and also discusses their practical implications. For example, the question of exactly what international regulation is for clearly has a bearing on how the rules should be interpreted. One of the suggestions made is that the extent to which international procurement rules should be interpreted as concerned with value for money can be linked to the level of integration between states envisaged by the overall set of rules in question. There is a difference between the interpretation which is required to promote trade liberalisation, and that which is required in order to create a single market. It follows that similarly worded provisions contained in different sets of international rules ought not necessarily to be interpreted in the same way.

Part III provides an impression of the content of international procurement rules. A striking observation about the 66 PTAs which have some procurement content is that twenty-eight expressly establish some kind of link with the principal international instrument in this area – the WTO Agreement on Government Procurement (GPA).[4] This link takes one of three forms. In order of preponderance, either the Parties set out a commitment to become GPA signatories,[5] or one or more of the Parties to the agreement are already GPA signatories,[6] or the agreement envisages that future developments will be informed by WTO developments.[7] A further ten agreements set out rules which are either identical to, or very closely

4 This plurilateral agreement is contained in Annex 4(b) of the WTO Agreement.

5 A total of eighteen agreements can be placed in this category including the seven bilateral agreements entered into between Albania and its trading partners and the four bilateral agreements entered into between Bulgaria and it trading partners. Croatia and Jordan have also committed to joining the GPA in their agreements with the remaining European Free Trade Area (EFTA) states as have Macedonia and Bosnia and Herzegovina in their bilateral agreement.

6 For example, the remaining EFTA states being Iceland, Liechtenstein, Norway and Switzerland are all GPA members. The EFTA Agreements with Bulgaria and Croatia envisage that these states will endeavour to join the GPA.

7 For example, Article 15:3 of the EFTA–Croatia PTA provides that rules based on the GPA will be elaborated if Croatia has not acceded to the GPA by 1 January 2004; an accession which has yet to occur.

resemble those contained in the GPA.[8] This leaves twenty-eight agreements which have some procurement content but do not have an explicit or implicit link to the WTO rules. Most of these remaining agreements presently go no further than recognising the liberalisation of procurement markets as an objective. Only a small proportion of the remaining twenty-eight agreements envisage a form of regulation somewhat different to the WTO approach. This applies to the agreements which commit to implementing the APEC Non-Binding Principles on Government Procurement.[9]

It is therefore clear that the GPA has had, and will very probably continue to have, a dominant influence on the development of procurement disciplines in PTAs. The GPA's influence on the development of procurement disciplines at the bilateral and regional levels is well deserved by reason of the richness and duration of its negotiating history.[10] This influence explains the approach taken in Part III which is primarily to provide an impression of how the GPA seeks to promote the liberalisation of procurement markets. Frequent comparisons are however made with the rules in various PTAs to the extent that they materially differ from, or supplement, the GPA. The approach adopted has the advantage that some comment will be provided on the 'single revised draft text' of the GPA which will enter into force at some point in 2008.[11] The mandate for the negotiations which led to this revised text was provided by Article XXIV:7 of the Uruguay Round GPA. This provision required the Parties to undertake negotiations 'with a view to improving the Agreement and achieving the greatest possible extension of its coverage among all Parties' and eliminating any remaining discriminatory measures and practices. The discussion of some of the improvements, missed opportunities and drafting errors here will be of interest to those responsible for developing the procurement content of PTAs. The revised text will be referred to as the GPA 2008, while the outgoing version will be referred to as the GPA 1994. References to the GPA can be taken to indicate both versions.

Part IV questions whether the GPA's influence on the development of procurement disciplines in PTAs should be welcomed, or regarded as a cause for concern.

8 Agreements in this category include those between the CAFTA–DR–US; EU–Chile; EFTA–Chile; Japan–Mexico; US–Australia; and US–Morocco.

9 This applies to the agreements between Korea–Singapore; New Zealand–Singapore; New Zealand–Thailand; and US–Singapore.

10 On the negotiating history see, Annet Blank and Gabrielle Marceau, 'The History of the Government Procurement Negotiations since 1945' (1996) 5 *Public Procurement Law Review* 77–159; and Arie Reich, *International Public Procurement Law: The Evolution of International Regimes on Public Purchasing* (London: Kluwer Law International, 1999), Chapters III, V and X.

11 GPA/W/297, 11 December 2006. The 2005–2006 report of the Committee on Government Procurement notes that the revised text is provisional in that it is subject to the outcome of continuing negotiations on coverage which ought to be completed during 2008. GPA/89 of 11 December 2006.

II. Why is public procurement subject to international regulation?

The range of goods and services purchased by governments to carry out their functions is of course vast, there being a near complete overlap between purchases by public entities and private firms and consumers, as well as goods which can only be procured by central government such as hard defence materials. It has been estimated that, in developed countries, government procurement accounts for around 7–14 per cent of Gross Domestic Product, depending on such factors as whether utilities and military procurement are taken into account. These figures may be higher for developing countries.[12] To the extent that public entities and other entities subject to their influence succumb to the tendency to 'buy national' and discriminate against foreign suppliers, procurement activities amount to a highly significant non-tariff barrier to trade. The reference here to entities subject to government influence implicates entities providing utility functions such as the generation and supply of energy and public transport services. These entities may be subject to the same legal structures as private companies, but are also subject to government ownership or control. International rules commonly provide for the withdrawal of such entities from coverage if government control or influence over them is eliminated.[13]

There is significant evidence that discrimination in public procurement is common place. A study of a number of EU Member States by Trionfetti compared the import-penetration rate in government markets with that of comparable private markets and found that this rate was consistently around one-third lower in government markets.[14] Bearing in mind that this study was conducted in the context of a sophisticated system of procurement regulation, it is plausible that the disparity in import-penetration rates may be higher for countries whose efforts to liberalise procurement markets are at an earlier stage of development.

A. Non-discrimination: National treatment or most-favoured-nation treatment or both?

When procurement rules apply as between more than two Parties, the general principles dealing with non-discrimination usually set out both national treatment and most-favoured-nation (MFN) treatment type obligations. Thus the GPA and the North American Free Trade Agreement (NAFTA) rules require in effect that

12 See Sue Arrowsmith, *Government Procurement in the WTO* (The Hague: Kluwer Law International, 2003), at p. 3 and studies cited therein.

13 It is notable that the GPA 2008 envisages the adoption by the Committee on Government Procurement of indicative criteria that demonstrate the effective elimination of control or influence. See GPA 2008, Article XIX:8(b).

14 Federico Trionfetti, 'Discriminatory Procurement and International Trade' (2000) 23(1) *The World Economy* 57–76, at 61–4.

suppliers from all Parties be provided with treatment no less favourable than provided to both national suppliers, and the suppliers of any other Party. The MFN treatment obligations here are qualified in nature since the question is whether favourable treatment has been given to any other Party, rather than whether it has been given to a supplier of any other country whether or nor a Party to the agreement.[15]

In contrast, bilateral PTAs tend to set out only a national treatment obligation. As only the relative treatment of domestic suppliers and foreign suppliers from a particular Party is in question, a qualified MFN treatment obligation would not add anything. The opposite approach however applies in a number of bilateral agreements, most notably between Turkey and its trading partners and Albania and its trading partners. For example, Article 23(1) of the Albania–Bosnia and Herzegovina Free Trade Agreement envisages liberalisation of procurement markets as an objective. This is not yet backed up by a national treatment obligation, but a full MFN treatment obligation is provided for in Article 23(2):

> The Contracting Parties will progressively develop their respective rules, conditions and practices on government procurement and shall grant suppliers of the other contracting party access to contract award procedures on their respective public procurement markets not less favourable than that accorded to companies of any third country.

The probable motivation for this approach is that MFN treatment alone amounts to a dormant commitment, which is only activated in the event of favourable treatment being granted to a third country.

The most important point about national treatment and MFN treatment in the procurement context is that these obligations do not usually apply to the question of whether foreign suppliers can participate in any particular contract award. Coverage negotiations are usually conducted on the basis of reciprocity which involves individual states granting access to their procurement markets only to the extent that other states grant comparable or equivalent access.[16] Foreign suppliers are therefore only entitled to national treatment and MFN treatment provided they are entitled to participate in the contract award. This question can be answered by consulting the coverage Annexes of individual Parties. In practice, bilateral negotiations result in the universal coverage of some contracts. This is usually the position for central government contracts for the supply of goods. However, as we

15 This observation probably explains why in both the GPA and the NAFTA Articles III and 1003 respectively refer to *National Treatment and Non-discrimination* with no reference to MFN.

16 Thus the right of a foreign supplier to bid for United States (US) services contracts which are in principle covered by the GPA depends on whether the foreign supplier's own government has listed the same service in its coverage annexes. This is clear from the US Appendix 1 to the GPA, para. 8 of the General Notes. The Appendix 1 of each GPA Party can be viewed on the WTO's web pages at www.wto.org/english/tratop_e/gproc_e/loose_e.htm.

move towards sub-central public entities and further still towards regulated utilities, and where the subject matter of the contract is services or construction services as opposed to goods, the absence of MFN treatment results in increasingly uneven coverage.

B. The relationship between non-discrimination and value for money

Value for money is an imprecise term, but can be taken to refer to the avoidance of unnecessary expenditure which might be incurred by the failure of the procurement process to identify the most suitable goods and services required at the lowest available price. There is a view that it is an understandable mistake to think of international rules as being concerned with value for money.[17] The mistake occurs because national and international rules strongly resemble each other, in that competitive tendering procedures are commonly envisaged, and because value for money is always at least an important concern of national rules and frequently the overwhelming concern. It has been argued however, that it does not follow that international rules are therefore concerned with value for money. The position is merely that the same rules are suitable both to make discrimination more difficult and to enhance value for money.

Arrowsmith finds evidence for this position in the observation that international rules do not reproduce national rules which are plainly concerned with ensuring value for money. Thus, national rules tend to require the financial and technical capacity of suppliers to perform contracts to *actually* be ascertained, while international rules only require the absence of discrimination in any verification process which *does* occur.[18] International rules are not therefore directly concerned with objectives such as 'value for money through an efficient process' and 'integrity etc. but only with removing trade barriers'.[19] In a similar vein, Trepte comments that, '[T]he focus of the international systems is limited primarily to securing non-discriminatory and reciprocal access to the procurement markets of their members. To the extent that the procedures adopted reflect those which already existed in the national systems of their membership, those systems will "fortuitously" promote economic efficiency or, at least, not impede it'.[20]

The difficulty with such statements is that they might unintentionally lead some to form the view that non-discrimination is an end in itself when it is more properly regarded as an instrument of trade liberalisation. In the procurement

17 Arrowsmith, above n. 12, at pp. 172–4.

18 Sue Arrowsmith, John Linarelli and Don Wallace Jr, *Regulating Public Procurement National and International Perspectives* (The Hague: Kluwer Law International, 2000), at p. 234.

19 Sue Arrowsmith, 'Reviewing the GPA: The Role and Development of the Plurilateral Agreement After Doha' (2002) 5(4) *Journal of International Economic Law* 761–90, at 766.

20 Peter-Armin Trepte, *Regulating Procurement: Understanding the Ends and Means of Public Procurement Regulation* (Oxford: Oxford University Press, 2004), at p. 284.

context, as indeed in all trade contexts, non-discrimination is intended to facilitate the materialisation of the benefits of competition in the market place. Non-discrimination goes some way to creating the environment in which these benefits can be realised by broadening the pool of suppliers from which public and private purchasers can choose. However, because private firms are directly subject to market forces, it can reasonably be supposed that, when they make purchasing decisions, they favour the lowest price goods and services which can fulfil their requirements regardless of the origin and nationality of these goods and services. This behaviour is indispensable in order for non-discrimination to achieve its primary end.

The assumption which applies to private purchasers does not necessarily hold true for public purchasers. The less direct pressure of market forces means that they might be more inclined towards inefficiency.[21] This is a plausible deduction from Trionfetti's findings[22] although it is important to bear in mind a point made by Linarelli that, '... in the right circumstances, government officials have reputational, career and programmatic incentives to be efficient'.[23]

Once the primary end of non-discrimination is brought out into the open, the compartmentalisation of the objectives of national and international regulation becomes problematic. The questions which become apparent are whether international regulation is, and ought to be, limited to the removal of discrimination, or whether the achievement of value for money might also be a concern.

To raise these questions might frequently be viewed as unnecessary since a failure to purchase on a value for money basis will often involve discrimination. This is particularly the position for states which use procurement as an instrument for the pursuit of non-trade/secondary policies of an industrial or social character – something which is common among developing countries and which also reflects the identity of the purchaser as a public body.[24] Such policies frequently involve

21 Trepte points out that there is little empirical evidence which demonstrates that public procurement is conducted on a less efficient basis than private firms operating in a competitive market. He nevertheless concludes a careful analysis in the following terms. 'The tendency of the public purchaser is towards inefficiency. It need not always be so and there is no guarantee that private companies are always more efficient. However, the position of the agent [the bureaucrat conducting the procurement] vis-à-vis his principal [the government] is such that he will have no direct interest in the outcome of the procurement in terms of "profitability" [the need to save money on one transaction in order to be able to carry out further transactions in the public good].': Trepte, *ibid.*, at p. 119.

22 Trionfetti notes that the expenditure of households or firms 'is driven by profit and utility maximization and, likely, is not affected by any sort of discriminatory behaviour': Trionfetti, above n. 14.

23 John Linarelli, 'The WTO Agreement on Government Procurement and the UNCITRAL Model Procurement Law: A View From Outside the Region' (2006) 1 *Asian Journal of WTO and Health Law and Policy* 61–84, at 69.

24 On the instrumental uses of the procurement function see, Christopher McCrudden, *Buying Social Justice: Equality, Government Procurement, & Legal Change* (Oxford: Oxford University Press, 2007); Christopher McCrudden, 'International Economic Law and the Pursuit of Human Rights: A Framework for Discussion of the Legality of "Selective Purchasing" Laws Under the WTO Government Procurement Agreement' (1999) 2(1) *Journal of International Economic Law* 3–48; and Arrowsmith, above n. 12, Chapter 13.

preferences for local suppliers and, therefore, entail both discrimination and the possibility of unnecessary expenditure. However, there are at least two reasons why the relationship between non-discrimination and value for money is one of significant practical importance.

First, preferred procurement procedures might not involve discrimination, but might nonetheless be less likely than other available procedures to result in the best value for money.[25] States can reduce the level of discretion available to procurement officials to limit the scope for corruption. The same confinement of discretion also makes discrimination more difficult. If the limit of international rules is to secure the absence of discrimination, then the national choice of procedure is laudable. In contrast, if international rules are concerned with value for money, there is scope for courts, or other review bodies, to question the use of these preferred procedures.

The second reason is the mirror image of the first. Some states might wish to grant very broad discretion to procuring entities in order to enhance value for money. For these states, the need to follow procedural rules which constrain discretion to make discrimination more difficult might be seen as impeding value for money. This is especially the position for states wishing to experiment with new methods of procurement which are difficult to reconcile with a particular (and possibly outmoded) conception of the procurement process. Because of developments at the national level in this direction, there is an emerging debate over the extent to which general principles in international rules need to be supplemented with detailed procedural rules.[26] There would seem to be less scope for objection to scaling back on regulation by detailed rules if the connection between non-discrimination and value for money is accepted, and openly acknowledged. Some attention is therefore given below to the positive and normative dimensions of what is likely to become an important debate. The intention is to introduce some issues which will be taken up more fully in future work.

European regulation can arguably be categorised as concerned with value for money as a result of the European Commission's position, which seems to be reflected in European Court of Justice (ECJ) reasoning. A 2001 Commission Communication states that, '[P]ublic procurement policy aims at contributing to the realization of the single Market by the creation of competition necessary for the non-discriminatory award of public contracts and the *rational allocation of public money through the choice of the best offer presented*' (emphasis added).[27] This appears not to have been an isolated *faux pas* since the Commission's internal market web-pages presently refer to EU public procurement law as aiming to '... increase

25 This point is exemplified by the *Sintesi* case discussed below. Case C-247/02, *Sintesi SpA* v. *Autorità per law Viglinaza sui Lavori Pubblici* [2004] ECR I-09214.

26 See the discussion in section IV.

27 Commission Interpretative Communication on the Community law applicable to public procurement and the possibilities for integrating environmental considerations into public procurement: Brussels, 4.7.2001 COM(2001) 274 Final, at p. 4.

competition and transparency in order to create opportunities for all EU businesses, better value and higher quality services for tax payers'.[28] Also notable is that Recital 46 of the new public sector Directive[29] provides that, '[W]here the contracting authorities choose to award a contract to the most economically advantageous tender, they shall assess the tenders in order to determine which one offers the *best value for money*'. This phrase did not feature in the outgoing public sector directives. However, this did not prevent the ECJ from finding that an objective of European regulation is to increase the likelihood that the best tender is accepted.

The *Sintesi* case[30] involved the construction of an underground car park in the historical centre of the City of Brescia. As is typical, Article 30(1) of the Community Directive sets out two approaches to contract award criteria in the following terms.

> The criteria on which *the contracting authorities* shall base the award of contracts shall be:
>
> (a) either the lowest price only;
> (b) or, when the award is made to the most economically advantageous tender, various criteria according to the contract: e.g. price, period for completion, running costs, profitability, technical merit.[31] (Emphasis added.)

The question referred by the national court was whether this provision precludes national rules under which contracting authorities are required to employ only the lowest-price criterion. The Italian government claimed that this legislative measure was adopted, '. . . to combat corruption in the public works contracts by eliminating the administration's discretion in awarding contracts and by adopting transparent procedures apt to ensure free competition'.[32]

It is useful to first note the narrow basis on which the case could have been decided. This emerges clearly from the Opinion of Advocate General Stix-Hackl[33] and is based upon a literal interpretation of Article 30(1). It was found that the provision imposes an express obligation on contracting authorities rather than on member States. '. . . [T]he requirement that only one of the two available criteria for the award of contracts be applied also includes the power of the contracting authority to choose one of the two. The contracting authority loses this power in so far as 'its' member State limits this choice . . .'[34] This literal interpretation was reinforced by the observation that the Directives do sometimes permit member States to constrain the discretion of contracting authorities. Article 30(1) was not

28 See http://ec.europa.eu/internal_market/publicprocurement/remedies/remedies_en.htm (visited 10 November 2006).

29 Directive 2004/18/EC ([2004] OJ L134/1). 30 Above n. 25.

31 Directive 93/37/EEC ([1992] O.J. L199/54), Article 30(1). These alternative award criteria are preserved in the current public sector directive, albeit that 'the lowest price only' now features as the second basis for award, and the list of examples of considerations relevant to 'most economically advantageous' has been extended, most notably to include 'environmental characteristics': Directive 2004/18/EC ([2004] OJ L134/1), Article 53.

32 The *Sintesi* case, para. 27. 33 Delivered on 1 July 2004. 34 *Ibid.*, at paras. 54–5.

such an example. The Advocate General also went beyond this textual approach noting that, '[A]spects relating to competition may also be relied on to show that member States do not have the power to lay down the criterion for the award of contracts. For example, laying down such a criterion restricts the contracting authorities' freedom to choose the criterion which is most appropriate for ensuring free competition in a specific procedure'.[35]

Before the ECJ, it is interesting to note the Commission's position, which (despite the manner in which the Commission has described its views elsewhere) corresponded with that of the Italian, Greek and Austrian governments. The Commission considered that there was no reason to prevent national legislatures from mandating the use of a particular award criterion. Both overall award criteria could equally 'ensure healthy competition between undertakings' provided they are 'clearly stated in the contract notice and applied objectively and without discrimination'.[36] These passages seem to identify the limits of Community regulation. It can be inferred from them that, provided there is free-competition, transparency and non-discrimination, member States are free to limit the discretion of contracting authorities. They are free, in other words, to decide where the balance lies between anti-corruption and value for money.

The literal interpretation set out by the Advocate General is notably absent from the ECJ's brief judgment. Rather, the reasoning is based on a development of the Advocate General's views about competition. The Court first noted that the purpose of the Directive according to its 10th recital is to 'develop effective competition in the field of public contracts'. It is worth setting out the two key paragraphs which followed:

> 39 A national provision, such as that at issue in the main proceedings, which restricts the contracting authorities' freedom of choice, in the context of open or restricted tendering procedures, by requiring that the lowest price be used as the sole criterion for the award of the contract, does not prevent those authorities from comparing the different tenders and from accepting the best one on the basis of an objective criterion fixed in advance and specifically included among those set out in Article 30(1) of the Directive.
>
> 40 However, the abstract and general fixing by the national legislature of a single criterion for the award of public works contracts deprives the contracting authorities of the possibility of taking into consideration the nature and specific characteristics of such contracts, taken in isolation, by choosing for each of them the criterion most likely to ensure free competition and thus to ensure that the best tender will be accepted.

In paragraph 39, the Court agrees with the Commission that the national provision is unproblematic in respect of transparency and non-discrimination. There is also competition because contracting authorities can compare different tenders.

35 *Ibid.*, at para. 62. 36 The *Sintesi* case, paras. 32–4.

However, paragraph 40 then indicates that free competition requires that contracting authorities have the discretion to specify award criteria which reflect the characteristics of individual contracts. The suggestion, perhaps, is that free competition has a qualitative dimension. The identity of interested firms might have been different under the lowest price criterion. Firms whose costs are higher by reason, for example, of the use of higher quality construction materials, might have been put off participating, thereby making it less likely that the best tender will be accepted.

The view of the concept of free competition taken by the Advocate General and the Court blurs the boundary between the limits of Community regulation, and the objectives of national regulation. In this area, member States do not have the ability to decide where the balance lies between the need to limit discretion in the interests of anti-corruption and value for money. The Court considers that contracting authorities are in the better to position to decide upon this balance, even if member States are concerned about the possibility of corruption on the part of their contracting authorities. At one level, however, the decision ought not to be criticised. The approach taken need not have proceeded beyond the textual analysis set out by the Advocate General since the language of the provision is clear. As the choice is for contracting authorities and not for member States, any criticism should be directed towards the Community legislature.

Whatever view is taken of the merits of the case, it seems clear that the absence of discrimination is necessary, but not sufficient, to secure the type of competition which the Advocate General and Court have in mind. Free competition not only requires that suppliers are competing on a level playing field, but also that they are competing using criteria which, in the opinion of the contracting authority (but not the member State), make it most likely that the best tender will emerge.

It is interesting to pose the question of what would happen if a national law of the same kind were challenged in proceedings relating to the GPA or a PTA. Most international rules, including the GPA, contain provisions which very closely resemble Article 30(1) of the Community Directive. In particular, the choice between the two overall award criteria is specified as being for the procuring entity rather than for the Party.[37] The type of textual analysis undertaken by the Advocate General would therefore be equally relevant here. However, it is submitted that an analysis of the relevant provisions in their context ought to produce a different result. Two statements in the Preamble of the GPA 2008 are particularly relevant. The first recognises that 'the procedural commitments under this Agreement should be sufficiently flexible to accommodate the specific circumstances of each Party'. Also recognised is the importance of 'carrying out procurements in a transparent and impartial manner, and of avoiding conflicts of interest and corrupt practices'. These are apposite statements when it is recalled that a reason for the use of the

37 See, e.g., GPA 2008, Article XV:5, and the Australia–United States Free Trade Agreement (AUSFTA), Article 15.9.6.

lowest price criterion (just as in *Sintesi*) is that the discretionary element, and therefore the opportunity for corrupt practices, is reduced.

Quite apart from any textual analysis, care must be exercised when drawing comparisons between European regulation directed at the achievement of a single market, and international regulation aimed only at trade liberalisation. In the European context, there would seem to be more permissible scope for interpreting the rules in a manner which makes it more likely that they will contribute towards their ultimate end. There is less scope for objection, in other words, to a blurred boundary between Community and national regulation. In contrast, in the GPA and PTA contexts, the case for interpreting the rules with their ultimate end in mind, rather than interpreting them as concerned only with non-discrimination, is not nearly as compelling. The view expressed here might be seen as undermining the position that all rules which require non-discrimination share a common end and that this end cannot be achieved without value for money purchasing at the national level. However, it is acceptable, in my view, to identify something as the ultimate end of a set of rules, without also having to establish that the rules should be interpreted so as to make it as likely as possible that this end will be achieved. It is a question of identifying the point at which the baton should be handed to national regulators. The transition should plausibly be earlier in the context of trade liberalisation than in the context of creating a single market.

Moving away from the European context, it is notable that the connection between non-discrimination and value for money is sometimes made explicit. This is most significantly the position in the context of the Asia-Pacific Co-operation forum (APEC) Non-Binding Principles of Government Procurement.[38] The drafting of these Principles was completed in 1999 pursuant to the Osaka Action Agenda which committed the members to 'develop a common understanding on government procurement policies and systems . . .', and, 'achieve liberalization of government procurement markets throughout the Asia-Pacific region . . .' The principles identified by the APEC Government Procurement Experts Group are transparency, value for money, open and effective competition, fair dealing, accountability and due process, and non-discrimination. Principle 16 provides that, '. . . government procurement practices and procedures should be directed to achieving the best available value for money in the acquisition of goods and services to deliver, or support delivery of, government programmes'. Principles 17 resonates with the policy underlying the *Sintesi* decision, since it emphasises that, '[T]he test for best available value for money is a comparison of relevant benefits and costs on a whole of life basis. Purchase price alone is not an adequate indicator of total relevant costs'.

More tellingly is the clear connection between non-discrimination and value for money set out in Principle 70: 'The use of discriminatory practices in government

38 The Principles themselves as well as related information can be viewed at www.apec.org/apec/apec_groups/committees/committee_on_trade/government_procurement.html.

procurement undermines the competitive process and thus the ability of member governments to achieve the best possible value for money outcomes'. These Principles differ in their status from those usually contained in international agreements in the sense that they are non-binding. However, the Principles also reflect the 'common understanding' of the APEC Members. Also notable is that these Members have re-affirmed their commitment to the Principles in several instances in which APEC members have entered into bilateral agreements. For example, one of the General Principles in the New Zealand–Singapore Closer Economic Partnership Agreement (NZ–Singapore CEPA) requires the Parties to, 'use value for money as the primary determinant in all procurement decisions'.[39] A feature of this agreement which lends support to the idea explained above, is that the purpose of the procurement rules in this PTA is 'to establish a single New Zealand–Singapore government procurement market'.[40]

In sum, it has been argued that international rules which explicitly envisage value for money as an objective, and those which do not, share a common end. This end is to facilitate the materialisation of the benefits of competition in the market place. Put another way, international rules which envisage non-discrimination cannot achieve their primary end without value for money purchasing at the national level. These points apply whether the purchaser is a public or a private body, but take on a special significance in the public sphere because of the relative absence of market forces. Interesting questions are raised about the extent to which international rules should be interpreted as going beyond non-discrimination and about who is in the best position to decide upon which procedures are most likely to maximise value for money.

III. The typical content of procurement disciplines in PTAs

As noted above, the material here relates primarily to the GPA, with reference to the rules in various PTAs to the extent that they materially differ from, or supplement, those in the GPA. The rules described are those which apply to covered contracts. For various reasons, international rules do not apply to all contracts. As already noted, coverage is frequently limited by reciprocity considerations. It is also usual for international rules to specify financial thresholds which are intended to identify contracts of cross-border interest.[41]

39 NZ–Singapore CEPA, Article 49. 40 *Ibid.*, Article 46(1).

41 The GPA financial thresholds are indicated in the Appendix I of each Party. For central government entities, the thresholds for supplies and services are generally set at SDR 130,000 (approximately USD $196,000) and at SDR 5m for construction services. Thresholds vary considerably at the sub-central level particularly for construction services. The US threshold at sub-central level for construction services is SDR 5m, but it is 15m for Korea. In the AUSFTA, the threshold for central government goods and services contracts is AUD$81,800. The same threshold at the regional level is AUD$666,000.

A. Methods of procurement

The GPA envisages three procurement methods: open, selected and limited tendering procedures. Under the open procedure, all interested suppliers can tender whereas, under the selected procedure, only invited suppliers can tender.[42] No preference is expressed as between open and selected procedures so that states are free to preserve or adopt their own rules on this matter. In contrast to open and selected procedures, limited tendering is a non-competitive process under which the entity contacts suppliers individually. This procedure can only be used on the grounds specified in Article XV of the GPA 1994. Examples include '. . . extreme urgency brought about by events unforeseeable by the entity' and '. . . purchases made under exceptionally advantageous conditions which only arise in the very short term . . . [such as] disposal of assets of businesses in liquidation or receivership'.

Of the PTAs which set out detailed rules on tendering methods most are virtually identical to the GPA while none are materially different.[43]

B. The invitation to participate

Article XI(1) of the GPA 1994 requires the publication of an '. . . invitation to participate for all cases of intended procurement, except as otherwise provided for in Article XV (limited tendering)'. Beyond this simple statement, Article XI continues to set out a complicated structure for different types of invitation to participate, in particular by using similar terms (the 'notice of proposed procurement' and the 'notice of planned procurement') to refer to different types of invitations. The key point however is that less flexibility is provided to Annex 1 entities (central government entities) than Annexes 2 and 3 entities (respectively sub-central government entities and 'other entities' in practice in the utilities sectors). The explanation for this is that, if there are central government tendencies or policies to buy national, their influence diminishes as we move away from the central government level. Some commentators are sceptical about whether this rationale is sufficiently compelling to deprive Annex 1 entities of what amounts to a modest amount of increased flexibility. According to this view, the reduced cost of operating more flexible procedures would not come at the expense of transparency, competition and any increased risk of discrimination, so that the same flexibility should be available to all entities.[44]

42 GPA 1994, Article VII(3).

43 An apparent difference can be found in the CAFTA–DR–US in that selected tendering is not expressly envisaged. However the definition of open tendering, as 'any type of procurement method . . . except direct purchasing' makes it clear that selected tendering is regarded as a type of open tendering. Direct purchasing in this Agreement (see Article 9.9.2) corresponds with limited tendering under the GPA and the language of GPA Article XV is used to establish when direct purchasing is permissible.

44 Arrowsmith, above n. 12, at p. 189.

All entities can use a notice of proposed procurement as the invitation to participate. Article IX(6) of the GPA 1994 sets out what must be contained in this notice. Information must, for example, be provided about the nature and quantity of the products or services required. Where there are to be recurring contracts, an estimate should, if possible, be provided of the timing of the subsequent tender notices. Suppliers must also be informed of whether 'the procedure is open or selective or will involve negotiation' and of 'the address and final date for submitting an application to be invited to tender or for qualifying for suppliers' lists, or for receiving tenders, as well as the language or languages in which they must be submitted'.[45] The reference here to language is significant since it is clearly the position that entities are permitted to require that tenders are submitted in the national language, and, therefore, to allocate any translation costs to foreign suppliers. It follows that such a rule is not to be regarded as conferring less favourable treatment on foreign suppliers contrary to Article III(1)(a). This is an example of the GPA recognising that there is a balance to be achieved between non-discrimination and the efficiency of the procurement process itself.

Annexes 2 and 3 entities can, in addition to the notice of proposed procurement, issue the invitation to participate via a notice of planned procurement or a notice regarding a qualification system.[46] The notice of planned procurement is intended to give an impression of the procurement plans for each fiscal year, and requires less information to be provided than the notice of proposed procurement. It must, as a minimum include information relating to 'the subject matter of the contract; 'the time-limits set for the submission of tenders or an application to be invited to tender' and 'a statement that interested suppliers should express their interest in the procurement to the entity'. Annexes 2 and 3 entities which use the notice of planned procurement can then avoid having to publish notices of proposed procurement for individual requirements. They may instead notify these individual requirements only to suppliers who have expressed interest in the notice of planned procurement.

The third method of providing the invitation to participate, being the notice regarding a qualification system, is also available only to Annexes 2 and 3 entities. A general obligation must first be fulfilled which applies whether or not the notice of the qualification system is being used as an invitation to participate. This general obligation applies, '[I]n the case of selective tendering procedures, [for] entities maintaining permanent lists of qualified suppliers'.[47] The obligation is to publish annually a notice detailing the lists which are maintained, the products and services covered by the lists, the conditions for inscription of the lists and their period of validity. Where the publication of this information is used as the invitation to

45 Article IX(6)(d). 46 Article IX(3).

47 Article IX:9. It follows from this provision that the notice regarding a qualification system cannot be used as the invitation to participate when the open procedure is used.

participate, the notice must in addition contain 'a statement that the notice constitutes an invitation to participate'.[48]

The increased flexibility here means that Annexes 2 and 3 entities can dispense with the need to publish notices of proposed procurement for individual procurements provided there is a valid list in operation. When individual needs arise, entities can permissibly contact only the suppliers on the list. However, it is also important to note that access to the list must be kept open at all times and all entities must include qualified suppliers on the lists within a reasonably short time. This seems to be reasonably clear from Article VIII(e) which provides that if an unqualified supplier requests participation in an intended procurement after the publication of the invitation to participate, 'the entity shall promptly start procedures for qualification'. When this provision is considered, it becomes clear that Annexes 2 and 3 entities do not have very much more flexibility than Annex 1 entities.

There are some positive developments in the GPA 2008 with regard to the invitation to participate, but no changes of any great substance. In terms of terminology, the phrase 'notice of intended procurement' replaces both the 'invitation to participate' and the 'notice of proposed procurement'. This removes the potential confusion caused by the use of notices of proposed and planned procurement. The notice of planned procurement is preserved. Beyond this, however, the points made above apply equally to the revised text. Annexes 2 and 3 entities have modestly more flexibility than Annex 1 entities. In this respect, the GPA differs from some recently concluded PTAs. For example, in the Australia–United States Free Trade Agreement (AUSFTA), even though the procurement rules here apply to central and regional government entities and government enterprises, the rules apply in the same way to all entities. There is therefore no question of some entities having more flexibility than others. It can be supposed that the prevailing view in the GPA 2008 negotiations must have been that unifying the procedures for all entities would have presented too great a risk to transparency and competition.

C. Conditions for participation/qualification/supplier lists

At some point before a contract is awarded, the entity will need to ensure that suppliers have the basic attributes which will enable them to perform the contract. The GPA refers to the permissible criteria for assessing basic attributes as conditions for participation. These conditions are verified in qualification procedures. Sometimes all aspects of these procedures will be conducted on an ad hoc basis for individual procurements. The cost inherent in repeating the same procedures can also however be reduced by inviting suppliers to join a permanent list of

48 Article IX:9(d) and (e).

qualified suppliers (referred to as a multi-use list[49] in the GPA 2008 and the AUSFTA).

When the open procedure is used, entities are not permitted to impose any conditions for participation or operate any kind of qualification system before tenders are submitted. This follows from the definition of the open procedure under which 'all interested suppliers may submit a tender'.[50] The process of verifying whether suppliers meet the conditions for participation can only therefore commence after the expiry of the time for receipt of tenders. There is much greater flexibility with the selective procedure to the extent that the qualification process may be conducted even before the precise procurement requirement is known by inviting suppliers to apply for inclusion on lists.

Apart from repeating the prohibition on discrimination in Article III, the key obligation in Article VIII(b) with regard to conditions for participation is that they should be, 'limited to those which are essential to ensure the firm's capability to fulfil the contract in question'. Examples of permissible criteria are those relating to the 'financial, commercial and technical capacity of suppliers'. Thus a minimum annual turnover and a requirement of having previously performed comparable contracts might be specified. When the selective procedure is used, and when the application of such criteria does not sufficiently whittle down the field, it would be permissible for the entity to select the suppliers with, for example, the most experience of performing comparable contracts, provided that no preference is given to suppliers with experience of performing comparable contracts in the entity's own territory. Article VIII(c) of the GPA 2008 now provides this as an example of an impermissible discriminatory approach.

As for the question of how many suppliers should be invited to tender, Article X(1) refers to the need to 'ensure optimum effective international competition under selective tendering procedures'. This should result in the invitation of tenders from 'the maximum number of domestic suppliers and suppliers of other Parties, consistent with the efficient operation of the procurement system'. These provisions have been omitted from the GPA 2008 giving the impression that it is very much a matter for individual Parties or entities to decide on the point at which increased competition is likely to be outweighed by the cost of evaluating tenders.

There is uncertainty over whether the application of conditions for participation can result in the exclusion of firms which, in general terms, lack integrity but which are capable of fulfilling the contract. The relevant provisions set out below are representative of those generally found in PTAs.

49 Article I(i) of the GPA 2008 and Article 15.15 of the AUSFTA define a multi-use list as 'a list of suppliers that a procuring entity has determined satisfy the conditions for participation in that list, and that the procuring entity intends to use more than once'.

50 GPA 1994, Article VII:3(a). The same definition is used, for example, in AUSFTA, Article 15.15.8.

GPA 1994

Article VIII(b): any conditions for participation in tendering procedures shall be limited to those which are essential to ensure the firm's capability to fulfil the contract in question . . .

Article VIII(h): nothing in subparagraphs (a) through (g) shall preclude the exclusion of any supplier on grounds such as bankruptcy or false declarations . . .

AUSFTA

Article 15.7.2: In assessing whether a supplier satisfies the conditions for participation, a procuring entity:

(a) shall evaluate the financial, commercial, and technical abilities of a supplier on the basis of the supplier's business activities both inside and outside the territory of the Party of the procuring entity . . .

Article 15.7.3: Nothing in this Article shall preclude the exclusion of a supplier on grounds such as:

(a) bankruptcy;
(b) false declaration; or
(c) significant deficiencies in performance of any substantive requirement or obligation under a prior contract.

GPA 2008

Article VIII(1): A procuring entity shall limit any conditions for participation in a procurement to those that are essential to ensure that a supplier has the legal, commercial, technical, and financial abilities to undertake the relevant procurement.

Article VIII(3): Where there is supporting evidence, a Party, including its procuring entities, may exclude a supplier on grounds such as:

(a) bankruptcy;
(b) false declarations;
(c) significant or persistent deficiencies in performance of any substantive requirement or obligation under a prior contract or contracts;
(d) final judgments in respect of serious crimes or other serious offences;
(e) professional misconduct or acts or omissions that adversely reflect upon the commercial integrity of the supplier; or
(f) failure to pay taxes.

The question is whether suppliers can be excluded on grounds such as bankruptcy or false declarations even if their capability to fulfil the contract is not affected. Bankruptcy might well prevent suppliers from fulfilling the contract. However, the same cannot be said of false declarations or analogous grounds such as convictions for equal opportunities or environmental legislation unless the national penalty involves

preventing firms found to have committed these misdemeanours from participating in government contracts. A possible view is that attention should be given to the fact that, in the GPA 1994, Article VIII(h) is clearly set up as an exception to Article VIII(b). This makes it possible to interpret paragraph (h) as permitting entities to exclude suppliers whose integrity can be objectively questioned even if these suppliers are fully capable of performing the contract. Convictions for breach of equal opportunities legislation ought therefore to suffice even if suppliers are not consequently prevented under national law from participating in government contracts. The same analysis applies to the AUSFTA, again, because the second provision is clearly set up as an exception to the first provisions.

Under the GPA 2008, Article VIII(3) is not set up as an exception to Article VIII (1). Thus it is possible to take the view that anything done under paragraph 3 must be consistent with paragraph 1. It would follow for example, that a supplier can only be excluded on the basis of final judgments in respect of serious crimes if, under national law, the supplier is thereby deprived of the legal ability to undertake the relevant procurement. It is submitted, however, that this is not the preferred interpretation since exclusion depends on the rather arbitrary factor of whether this is required or permitted under national law. The view that paragraph 1 constrains discretion under paragraph 3 is also weakened by the introduction of the safeguard in paragraph 3, in the form of the need for 'supporting evidence'. It is improbable that the intention of the Parties was to permit exclusion under paragraph 3 where there is supporting evidence, but only if this happens to be a sanction envisaged by national law. The better interpretation is therefore that, in all three sets of rules above, the two provisions operate independently of each other so that suppliers can be excluded on such grounds as those listed, even if they are fully capable of undertaking the procurement. The second provision in all three sets of rules can therefore be regarded as a *lex specialis*.

D. Time limits for award procedures

The purpose of time limits is to give foreign suppliers adequate opportunity to overcome their potential lack of familiarity with foreign procurement procedures, while also recognising that entities need to progress procurement procedures with reasonable speed. Article XI of the GPA 1994 regulates times limits with both general and specific obligations. The general obligation requires time limits to be 'adequate to allow suppliers of other Parties as well as domestic suppliers to prepare and submit tenders before the closing of the tendering procedures'. An indication of relevant factors is provided which include the 'complexity of the procurement' and the 'extent of subcontracting anticipated'.[51] Entities are required to take such considerations into account to the extent that they are 'consistent with their own reasonable needs'.

51 Article XI:1(a).

Article XI:2 then proceeds to set out minimum periods for two stages in the procurement process. If the selected procedure is used, suppliers must be given no less than twenty-five days to submit an application to be invited to tender. This twenty-five-day period commences with the publication of the invitation to participate. Entities will then select some or all of the interested suppliers to submit tenders. No less than forty days must elapse between the invitation to tender and the submission of tenders. In contrast, if the open procedure is used, the initial twenty-five-day period does not apply since all suppliers have the opportunity to submit tenders. Suppliers here must also be given forty days to submit tenders and this period runs from the publication of the invitation to participate.

These periods can be reduced in various circumstances. For example, 'a state of urgency duly substantiated by the entity renders impracticable the periods in question', both the twenty-five and forty-day periods can be reduced to not less than ten days each.[52] Article XI:3(d) also provides increased flexibility for Annexes 2 and 3 entities only. When these entities use 'selective procedures involving the use of a permanent list of qualified suppliers', the period for receipt of tenders can 'be fixed by mutual agreement between the entity and the selected suppliers'. Even without agreement entities can fix periods which are long enough to enable responsive tendering. These periods cannot be less than ten days.

The GPA 2008 largely reproduces the time limits in the existing GPA. It is regrettable that the increased flexibility for Annexes 2 and 3 entities has not been extended to Annex 1 entities. A further missed opportunity is that no clarification is provided on how the deadlines apply to iterative/repetitive procedures involving more than one round of tendering for a single requirement.[53] Therefore, there is continuing uncertainty on whether the tender submission periods are applicable to each round of tendering.[54] A significant modernisation, however, is that electronic forms of communication are now envisaged. This was an area in which the GPA had fallen behind some PTAs.[55] The new text provides for a reduction in the time limit for submitting tenders of five days where the notice of intended procurement is published by electronic means. Further reductions of five days each are permitted if tender documentation is made available electronically from the date of publication of the notice of intended procurement and if tenders can be received electronically.[56]

52 Article XI:3(c). The same language is used, for example, in the Mexico–Israel Free Trade Agreement, Article 6.11.4(c).

53 As will be seen below however, iterative tendering which occurs during an electronic auction is now envisaged by the GPA 2008.

54 It has been suggested that the general obligation to provide for 'adequate' time limits for the preparation and submission of tenders is applicable to each stage of a multi-stage process and that more time is generally required at the first stage so that the time limits would thereafter be progressively reduced. Arrowsmith, above n. 12, at pp. 200–1.

55 For example, Article 15.5.4 of the AUSFTA provides for a modest reduction in the time limit for tender submission when the notice of intended procurement is published in an electronic medium.

56 Article XI:5.

In total therefore, use of electronic means of communication can result in the deadline for receipt of tenders being reduced from forty to twenty-five days from the date the entity notifies suppliers that they will be invited to submit tenders.

Article XI:6 regulates the situation where both electronic means are used, and another ground for reduction of the time limit is present, such as the publication of a notice of planned procurement. It is provided that this, 'shall in no case result in the reduction of the time-period for tendering set out in paragraph 3 [40 days] to less than 10 days *from the date on which the notice of intended procurement is published*' (emphasis added). There is a slight drafting error here since the provision only makes sense if open tendering is used. If selective tendering is used, the notice of intended procurement will be followed by requests to participate from suppliers and then the invitation to submit tenders from the entity. The lapse of time between the notice of intended procurement and the invitation to submit tenders will normally be significantly greater than ten days. Under the wording presently used, entities could therefore set a period for tender submission of less than ten days from the invitation to submit tenders. This anomaly would be removed by the deletion of the emphasised words. Paragraph 3 sets out when the time period should commence in both open and selective procedures and the reference to paragraph 3 in paragraph 6 incorporates this difference.

E. Awarding of contracts

Both the 1994 and 2007 texts specify that tenders '. . . must at the time of opening, conform to the essential requirements of the notices or tender documentation and be from a supplier which complies with the conditions for participation'.[57] The GPA 1994 then requires that the award be made to the tenderer determined to be 'fully capable of undertaking the contract and whose tender . . . is either the lowest tender or the tender which in terms of the specific evaluation criteria set forth in the notices or tender documentation is determined to be the most advantageous'. The 2007 text also sets out these two award criteria albeit that 'the most advantageous tender' now appears as the first criterion.

1. The most advantageous tender

Parties have broad discretion over the content of specific evaluation criteria under the overall criterion of 'most advantageous tender'. Article XII:2(h) of the GPA 1994 requires that the tender documentation must set out 'the criteria for awarding the contract, including any factors other than price that are to be considered in the evaluation of tenders'. The equivalent provision in the GPA 2008 has been somewhat

57 GPA 1994, Article XIII:4(a); and revised GPA 2008, Article XV:4. The same language is used, for example, in Mexico–Israel PTA, Article 6.13.4; EU–Chile AA, Article 153:1; and AUSFTA, Article 15.9.5.

expanded. Article X:9 provides that '[T]he evaluation criteria ... may include, among others, price and other cost factors, quality, technical merit, environmental characteristics, and terms of delivery'.

The inclusion of 'environmental characteristics' on this illustrative list raises the question of whether such characteristics can only permissibly relate to the products or services themselves (for example, requirements that any materials used are recyclable) or also to the supplier's production methods (for example, relating to its emissions standards). When the provisions above are read in context, it is revealed that the latter and broader approach is to be preferred. Article VI:1 of the GPA 1994 envisages that technical specifications can relate to 'the characteristics of the products or services to be procured ... or *the processes and methods for their production* ...' (emphasis added).[58] The GPA 2008 also introduces a new provision under which, '[F]or greater certainty, a Party, including its procuring entities, may, in accordance with this Article, prepare, adopt, or apply technical specifications to promote the conservation of natural resources or protect the environment'.[59] The utility of these provisions would be reduced if production methods cannot be considered at the award stage. It is therefore submitted that it would be permissible to rank tenders partly on the basis of the extent to which the suppliers improve upon international standards on emissions.

2. Ranking of evaluation criteria

Unlike the GPA 1994, the GPA 2008 requires the tender documentation to indicate the 'relative importance' of 'all the evaluation criteria'.[60] This new obligation can be seen as supporting both non-discrimination and value for money. As the evaluation criteria must be ranked and published in tender documentation, the opportunity for tacitly communicating the ranking only to a favoured supplier is removed. Value for money is also enhanced as suppliers have a better understanding of what is required. The ranking requirement would seem to be flexible and would probably be satisfied by a list of evaluation criteria in order of importance. It would certainly be satisfied by providing approximate percentage values for all the criteria.

However, if an electronic auction is used, entities will in practice be required to give an exact percentage weighting or value to all evaluation criteria. This does not have to be included in the tender documentation. Rather, Article XIV(a) effectively requires the precise weightings to be communicated before the auction commences as part of the 'mathematical formula' referred to in this provision.

3. Electronic auctions

A possible alternative to opening confidential tenders and awarding the contract to the best tender is to conduct an electronic auction. The auction phase of the award

58 In the GPA 2008, the same language is used to define the term 'technical specification' in Article I(t).
59 GPA 2008, Article X:6. 60 Article X:7(c).

procedure involves the participants having the opportunity to improve their tenders which are then continuously re-ranked by electronic means. Electronic auctions can enhance value for money since suppliers have an incentive to improve tenders. Transparency is also enhanced, particularly if participants have information on the characteristics of other tenders, as well as the ranked position of their own tender, during the auction.

Unlike the GPA 1994 and PTAs with a procurement dimension, the GPA 2008 makes express provision for electronic auctions. Article I(e) defines them as an 'iterative process[61] that involves the use of electronic means for the presentation by suppliers of either new prices, or new values for quantifiable non-price elements of the tender related to the evaluation criteria, or both, resulting in a ranking or re-ranking of tenders'.

Article XIV deals with auctions in the following terms:

> Where a procuring entity intends to conduct a covered procurement using an electronic auction, the entity shall provide each participant, before commencing the electronic auction, with:
>
> (a) the automatic evaluation method, including the mathematical formula, that is based on the evaluation criteria set out in the tender documentation and that will be used in the automatic ranking or re-ranking during the auction;
> (b) the results of any initial evaluation of the elements of its tender where the contract is to be awarded on the basis of the most advantageous tender; and
> (c) any other relevant information relating to the conduct of the auction.[62]

The reference to '. . . any initial evaluation' in paragraph (b), indicates that an initial evaluation of tenders prior to the auction is not mandated. The obligation is rather that the result of any initial evaluation which *is* conducted must be communicated before the auction phase. This is in sharp contrast to the new EU public sector directive which requires that, where the most economically advantageous award criterion is used, the invitation to participate in the auction be accompanied by the 'outcome of a full evaluation of the relevant tenderer'.[63] However, this difference is unlikely to have very much impact. Where the overall award criterion is the most advantageous tender, an 'initial evaluation' would at least sometimes, if not usually, occur in practice for the following reasons.

Paragraph (a) refers to 'the automatic evaluation method' and the 'automatic ranking or re-ranking during the auction'. The need for automation rules out any intervention and exercise of subjective judgement by the entity during the auction. It follows that the non-price factors which can be improved upon during the auction

61 Article 1(7) of the new EU public sector directive (above n. 29) uses the phrase 'repetitive process'.

62 No guidance is provided on what this other relevant information might be although it could most obviously relate to when and how the auction will end.

63 Article 54(5) of the new EU public sector directive (above n. 29). The reference in this provision to 'tenderer' is an error, the correct term being 'tender'.

must be 'quantifiable' and capable of being expressed in 'figures and percentages'. These expressions are from the new EU public sector directive,[64] but they are also implicit GPA requirements because of the limits of what can be automatically evaluated via electronic means. Many non-price factors are capable of being automatically evaluated. For example, an aspect of quality might be service intervals for a machine. It could be specified that for every extra month of operation beyond one year during which the machine does not require a service, the entity will pay an extra £100. However, the entity might also choose to undertake an initial evaluation of this factor, and other non-price factors even though they are capable of automatic evaluation. Indeed, it is common for all non-price factors to be evaluated before the auction and for price alone to be subjected to the auction. It is also the position that some non-price factors are not capable of automatic evaluation. It would not be possible, for example, to improve the artistic merit of the construction to be delivered during the auction, since the question of how many points to allocate here necessitates the exercise of human judgement.[65] It can therefore be seen how the obligation to disclose the 'results of any initial evaluation' might frequently be triggered.

A possible means of avoiding the obligation might be for the entity to evaluate non-price factors excluded from the auction only after the conclusion of the auction. This practice is probably not permitted. The auction must result in a 'ranking or re-ranking of tenders'. The most natural interpretation of this requirement is that participants must know during the auction whether their tender is the winning tender, and must know at the end of the auction whether their tender has won. If this is the position, then the ranking must be based both on the factors which can be revised during the auction, and those that have been fixed and inputted after the initial evaluation, but before the commencement of the auction. This would enhance both transparency and the incentive to improve tenders.

It is also clear from the wording of Article XIV that 'each participant' is only entitled to receive information about 'the results of any initial evaluation of the elements of *its tender*'. There is therefore no obligation to disclose to participants how their tenders relate to other tenders. However, such disclosure is probably also not prohibited provided it occurs in a transparent and non-discriminatory manner. This would involve the ranking after the initial evaluation being made available to all participants.[66]

64 Article 54:3(a).

65 Sue Arrowsmith, *The Law of Public and Utilities Procurement*, 2nd edn (London: Sweet & Maxwell, 2005), at p. 1202.

66 Some doubt on this point is created by the need to guarantee the confidentiality of tenders under GPA 2008 Article XV:2. This safeguard probably does not apply to any part of an award procedure which culminates in an electronic auction. This interpretation seems to be confirmed by GPA 1994 Article XIV:3 which supplements the need to treat tenders in confidence with a prohibition against providing '. . . information intended to assist particular participants to bring their tenders up to the level of other participants'. This, of course, is the entire rationale for the electronic auction so that the key requirements here are transparency and non-discrimination.

F. Exceptions provisions

As in all areas of trade regulation, there is a balance to be achieved between trade liberalisation and allowing states to pursue legitimate non-trade objectives. Most PTAs set out the exceptions provision contained in the GPA which in turn corresponds largely with Article XX of the GATT.

> **GPA 2008 Article III:2**
>
> Subject to the requirement that such measures are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between Parties where the same conditions prevail or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent any Party from imposing or enforcing measures:
>
> (a) necessary to protect public morals, order, or safety;
> (b) necessary to protect human, animal or plant life or health;
> (c) necessary to protect intellectual property; or
> (d) relating to goods or services or persons with disabilities, philanthropic institutions, or prison labour.

It has been suggested that some human rights oriented policies might fall under paragraph (a).[67] The debate here was triggered by legislation enacted by the Commonwealth of Massachusetts to forbid the award of government contracts to domestic and foreign firms having business links with Burma (Myanmar), on the basis that this state is considered to have a poor human rights record. The European Communities (EC) and Japan requested a WTO panel to examine the compatibility of this legislation with the GPA 1994 and a panel was established on 21 October 1998.[68] This might have been a highly significant case in terms of providing guidance on the meaning of several GPA 1994 provisions, including Articles VIII(b) (now VIII:1 and 2 of the GPA 2008) and XIII:4(b) (now XV:5 of the GPA 2008). Had a violation of these provisions been established, it is reasonable to suppose that the scope for justifying the legislation under the 'public morals, order or safety' exception would have been considered. However, panel proceedings were suspended in February 1999, and the complaint was later allowed to lapse.[69]

Notwithstanding the possible scope of the public morals exception, none of the other grounds would seem to permit Parties to provisionally justify the use of

67 See McCrudden, 'International Economic Law and the Pursuit of Human Rights', above n. 24, at 38–42.

68 Request for Establishment of a Panel by the European Communities, *US–Government Procurement*, WT/DS88/3 (9 September 1998).

69 The WTO proceedings were allowed to lapse because the constitutionality of the Massachusetts Burma law was successfully challenged by a non-profit corporation, 34 members of which had been placed on a restricted purchase list to indicate their business involvement in Burma. The main basis for the Supreme Court decision was that the state legislation was an obstacle to the achievement of Congress's objectives under a later federal statute dealing with sanctions against Burma. *Crosby* v. *National Foreign Trade Council* 120 SCt 2288 (2000).

procurement for the pursuit of industrial and social policies such as preferences for domestic infant industries, or businesses owned by disadvantaged groups.[70] Only paragraph (d) is of limited relevance to social policies.

Until recently, this limited scope for justifying non-trade policies might have been explained on the basis that little attention was given to this question during the Uruguay Round negotiations. This is indicated by McCrudden's account of the GPA 1994 negotiations which indicates that discussions focused on derogations to remove certain policies form the GPA's reach, rather than requiring Parties to justify their secondary uses of procurement.[71] However, the GPA 2008 does not implement a reform proposal which might have facilitated the pursuit of secondary policies. This proposal is to require all secondary policies to be justified 'but to remove limitations on the possible *types* of public interest justification' along the lines of the WTO's Agreement on Technical Barriers to Trade (TBT).[72] On the assumption that this proposal was considered in the negotiations, it is interesting to speculate as to what might have led to its rejection. Part of the explanation might have been a lack of desire to facilitate the pursuit of secondary policies on the basis that this would undermine the pursuit of value for money and therefore the extent to which non-discrimination can achieve its primary end. Some parties might also have considered that implementing the proposal would have done more to undermine than facilitate the secondary uses of procurement. The practice at present is for secondary policies to be accommodated by derogations in coverage.[73] Policies can therefore operate even if they clearly or potentially breach procurement rules.[74] The thrust of the proposal is for this practice to be substituted by the exposure of secondary policies to a necessity requirement[75] and the chapeau. Given the strictness with which these

70 One of the matters discussed in the 1997 Green Paper on Public Sector Procurement Reform in South Africa is the need, '[t]o realise the potential of public sector procurement as an instrument of policy in the socio-economic transformation process': see www.info.gov.za/greenpapers/1997/ publicproc.htm at 3.1.2. For an analysis of subsequent legislative developments, see Phoebe Bolton, 'An Analysis of the Preferential Procurement Legislation in South Africa' (2007) *Public Procurement Law Review* 36–67. For an analysis of domestic preferences in Malaysia, see Christopher McCrudden and Stuart. G. Gross, 'WTO Government Procurement Rules and the Local Dynamics of Procurement Policies: A Malaysian Case Study' (2006) 17 (1) *European Journal of International Law* 151–85.

71 McCrudden, 'International Economic Law and the Pursuit of Human Rights', above n. 24, at 20–1.

72 Arrowsmith, above n. 19, at 782.

73 For example, in the context of the GPA, the General Notes to Canada's Appendix 1 provides that the Agreement does not apply to procurements in respect of set-asides for small and minority businesses.

74 Negotiating derogations are plausibly a preferable means of pursuing secondary policies than allowing them to be justified. As McCrudden explains, this is because negotiated concessions have to be 'paid' for with the other concessions: McCrudden, 'International Economic Law and the Pursuit of Human Rights', above n. 24, at 46. A point recently made by Linarelli seems to identify a possible problem with this view. Only states with a substantial import market in public procurement have the capacity to open large procurement markets while also keeping substantial markets closed. Larger developed economies are therefore likely to have a higher capacity than smaller developing economies to pay for derogations: Linarelli, above n. 23, at 79.

75 TBT Agreement Article 2.2 imposes a necessity requirement in the sense that 'technical regulations shall not be more trade-restrictive than necessary to fulfil a legitimate objective'.

requirements have been interpreted, at least by WTO panels and the Appellate Body, some parties might have preferred to retain the derogation route.

G. Domestic review procedures for supplier challenges

When suppliers consider that the GPA has not been properly implemented, or that it has been breached in the context of a particular award procedure, they can, independently of their governments, take advantage of the requirement to provide for national challenge procedures. Article XX:2 of the GPA 1994 provides that:

> [E]ach Party shall provide non-discriminatory, timely, transparent and effective procedures enabling suppliers to challenge alleged breaches of the Agreement[76] arising in the context of procurements in which they have, or have had, an interest.

This innovation stems from the inadequacy of the Dispute Settlement Understanding (DSU) in providing a meaningful solution where the complaint relates to a failure to follow the GPA in a particular award procedure. The timetable for resolving disputes under the DSU is understandably protracted[77] and there is no provision for interim remedies, such as the suspension of the award procedure, at the start of the dispute. Indeed there would be little point in providing for suspension, unless a panel could order the recommencement of the procedure in the event of a breach being confirmed. It is generally understood however that the standard recommendation under DSU Article 19 has only prospective effect.[78]

76 Cottier has interpreted the wording here as indicating that the GPA has direct effect in the sense that the national review body would be required to apply the GPA itself rather than national implementing measures in the event of a conflict. However it is now clear that the wording was not intended to indicate direct effect. GPA 2008 Article XVIII:1(b) provides that, 'where the supplier does not have a right to challenge a breach of the Agreement under the domestic law of a Party, [suppliers may challenge] a failure to comply with a Party's measures implementing this Agreement'. This confirms that direct effect is a matter for individual Parties. Where the supplier's complaint is that the GPA has not been properly implemented by a state which does not recognise the direct effect of the WTO Agreements, the appropriate course of action would be for the supplier to petition its government to institute intergovernmental proceedings under the Dispute Settlement Understanding: Thomas Cottier, 'A Theory of Direct Effect in Global Law', in Armin von Bogdandy, Petros C. Mavroidis and Yves Mény (eds.), *European Integration and International Co-ordination: Studies in Transnational Economic Law in Honour of Claus-Dieter Ehlermann* (The Hague: Kluwer Law International, 2002), pp. 99–123.

77 GPA 1994 Article XXII:6 provides that, '[e]very effort should be made to accelerate the proceedings to the greatest possible extent' and then recommends specific reduced deadlines. Interestingly, this provision has been jettisoned from the GPA 2008 which probably reflects the view that breaches of the GPA in the context of a particular award procedure can only realistically be challenged at the national level.

78 In the procurement context, the *Trondheim* case, which was decided under the Tokyo Round GPA, confirms that remedies following intergovernmental proceedings cannot have an impact on past conduct. Norway had failed to subject a covered contract to any kind of competitive award procedure in contravention of the GPA. By the time the case was heard the contract had been awarded to a Norwegian firm which had also completed performance. The panel declined to annul the contract and order the re-commencement of the award procedure on the basis that recommendations 'of this nature' did not form part of the 'customary practice' in GATT cases. The panel also considered that annulment of the contract would not have been appropriate in this case even if possible in principle in light of the impact on the

Article XX of the GPA 1994 goes some way to improving the position by setting out rules on the identity and attributes of the review body, and the remedies which it should have at its disposal. On these matters, GPA 2008 does not materially differ from GPA 1994 although there are significant differences as between PTAs.

GPA 1994 provides that, '[C]hallenges shall be heard by a court or by an impartial and independent review body with no interest in the outcome of the procurement and the members of which are secure from external influence during the term of appointment'.[79] Where complaints are heard by an independent body which is not a court, this body must either be subject to judicial review or have procedures which provide, *inter alia*, that 'participants can be heard before an opinion is given'; 'opinions or decisions are given in writing'; 'proceedings can take place in public' and that 'witnesses can be presented'.

On the identity and attributes of the review body, most PTAs contain identical or closely comparable provisions. The NAFTA rules provide the most notable exception in that the only requirement is that the review body should have 'no substantial interest in the outcome of procurements'.[80] It is also provided that entities should 'normally' follow the recommendations of the review body.[81] The GPA does not expressly provide that entities must follow review body recommendations. However this would seem to be implicit in the need to provide for access to courts or court-like procedures.

With regard to the remedies which the review body should have at its disposal, the GPA preserves considerable flexibility. The first principle is to provide for 'rapid interim measures to correct breaches of the Agreement and to preserve commercial opportunities'.[82] The rationale here is that if the procurement process is permitted to continue during the challenge procedures, the final remedy is unlikely to be very helpful in terms of encouraging suppliers to complain and deterring breaches. If the procurement process can be stopped at an early stage, it is likely that a breach could result in re-commencement being ordered. However, if a contract has been awarded or even performed, any remedy other than a declaration that a breach has occurred becomes unlikely, because of prejudice to the successful supplier and the public interest in the prompt delivery of government functions. The GPA leaves the question of interference with concluded and performed contracts to individual

successful tenderer and the waste of resources incurred through performing the contract twice. At the end of the case therefore the US as complainant was left with little more than the satisfaction of the panel's confirmation that a violation had occurred: see GATT Panel Report, *Norway–Trondheim Toll Ring*.

79 GPA 1994, Article XX:6. GPA 2008 expressly envisages that the challenge may initially be heard by a body other than an 'impartial administrative or judicial authority' provided the supplier can appeal the initial decision to such an impartial body. The complaint may therefore initially be heard by the entity which is the subject of the complaint (GPA 2008, Article XVIII:5).

80 NAFTA, Article 1017(g). 81 NAFTA, Article 1017(l).

82 GPA 1994, Article XX:7(a). The wording is improved in GPA 2008 to reflect the observation that interim measures do not themselves correct breaches of the Agreement, but rather preserve the opportunity to correct breaches.

Parties or entities. Some PTAs are stricter on this issue. For example, the CAFTA–DR–US requires that the review body be empowered to suspend 'the award of a contract or the performance of a contract already awarded'.[83]

The final remedies envisaged by the GPA are either, 'correction of the breach of the Agreement or compensation for the loss or damages suffered, which may be limited to costs for tender preparation and protest'. It has been argued that review bodies must have both remedies (correction and compensation) at their disposal on the basis that 'effective' challenge procedures are required by Article XX:2.[84] Correction might involve advertising a covered contract, or evaluating a wrongfully excluded tender properly submitted before the deadline. The review body might however be required to, or choose to, award-only compensation when the award procedure has reached a certain stage. The GPA clearly permits the compensation remedy to be very limited. There is nothing to prevent GPA Parties from awarding damages for lost profits, but it is notable that the Mexico–Israel Free Trade Agreement provides that compensation 'shall [rather than may] be limited to costs for tender preparation or protest'.[85]

A fundamentally different means of resolving disputes is set out in Article 54 of the NZ–Singapore CEPA, in that suppliers have considerably less direct control over the process. Supplier complaints are first heard by way of consultations between the aggrieved supplier and the procuring government body. If the complaint is not resolved at this level, it then takes on an intergovernmental character since the next stage is for the supplier to seek the assistance of its national 'designated body'.[86] The complaint may be 'processed informally' if this is deemed appropriate by the complainant and its national body.[87] No guidance is given on how the complaint might be informally processed although it is reasonable to suppose that the supplier's national body will enter into consultations with the procuring entity complained of. If the complaint is not resolved via informal means, the supplier's national body then notifies the complaint to its counterpart in the other Party 'for investigation of any alleged breach ... and for a report by it in writing'.[88] The intergovernmental character of the complaint is reinforced by Article 54:4 which effectively provides for the complaint to lapse if the response to the written report is satisfactory to the complaining supplier's national body. If the complaint does not lapse, the complaining supplier's national body may refer the matter to the Minister

83 Article 9.15.2. 84 Arrowsmith, above n. 12, at 400. 85 Article 6.17.7(c).

86 These bodies are the Ministry for Economic Development in New Zealand and the Ministry of Finance for Singapore.

87 Article 54:2.

88 Article 54:3. It is unclear from the wording which designated body must draft the written report. However, when paragraph 3 is read with paragraph 4, the impression created is that the report is drafted by the complaining supplier's national body. This is also the better interpretation as the supplier's national body can be expected to be more independent and impartial than its counterpart; a point which takes on extra significance where the counterpart happens to be the procuring entity complained of.

responsible for procurement in the other Party 'for further investigation and decision'.[89] Article 30:6 envisages a thirty-day period for resolving the dispute which runs from the date the supplier notifies the complaint to its national body. This period is sufficiently short for interim measures to operate in order to preserve opportunities, although these are not expressly required. Finally, if the dispute is not resolved within thirty days, it can be subject to strictly intergovernmental proceedings under Part 10 of the Agreement.

When compared to these arrangements, the GPA's national challenge procedures seem very sophisticated. Considered in isolation however, the GPA's minimum requirements arguably ought to have been strengthened by the GPA 2008 especially with regard to the possibility of damages for lost profits. However, the likely divergence of approaches in national legal systems to non-contractual damages for lost profits (which may or may not have accrued but for the breach) militates against agreement on general principles in this area. The possible alternative of liquidated damages can also be regarded as a reform too far bearing in mind that the GPA is already highly distinctive in requiring national challenge procedures. A final point here is that the GPA, and most PTAs, are founded on a national treatment principle. If national suppliers are able to claim lost profits, the same entitlement must probably be extended to foreign suppliers.

H. PTA content which does not feature in the GPA

There are very few examples of rules contained in PTAs which do not feature in the GPA. As discussed above,[90] a common feature of international procurement rules is the possibility of excluding suppliers on grounds which broadly relate to their lack of integrity, as evidenced by professional misconduct and failure to pay taxes. International rules do not, however, generally seek to address lack of integrity and corruption among procurement officials other than to the extent that transparent procedures make it more difficult to conceal both discrimination and corruption. Article 15:10 of the AUSFTA goes considerably further than most international rules in this respect.

> **Ensuring integrity in procurement practices**
>
> 1. Each Party shall ensure that criminal or administrative penalties exist to sanction:
>
> (a) a procurement official of that Party who solicits or accepts, directly or indirectly, any article of monetary value or other benefit, for that procurement official or for another person, in exchange for any act or omission in the performance of that procurement official's procurement functions;

89 Article 54:5. 90 See section IIIC.

(b) any person who offers or grants, directly or indirectly, to a procurement official of that Party, any article of monetary value or other benefit, for that procurement official or for another person, in exchange for any act or omission in the performance of his or her procurement functions; and
(c) any person intentionally offering, promising or giving any undue pecuniary or other advantage, whether directly or through intermediaries, to a foreign procurement official, for that foreign procurement official or a third party, in order that the foreign procurement official act or refrain from acting in relation to the performance of procurement duties, in order to obtain or retain business or other improper advantage.

IV. Appraising the impact of WTO rules on PTA procurement content

It can be questioned whether the influence of developments at the WTO level on the procurement content of PTAs is to be welcomed. Overall, it is submitted that the answer is yes, albeit that some concerns can be identified.

At an early stage in the development of international procurement regulation it was realised that general obligations of non-discrimination would need to be supplemented with minimum procedural obligations to tackle the widespread use of discriminatory practices as opposed to readily identifiable laws and measures.[91] There is now a view that the pendulum has swung too far in the direction of regulation by detailed rules. In particular, Arrowsmith's work calls for serious consideration to be given to a swing of the pendulum somewhat back towards regulation by general principles alone. Accepting this view would have clear implications for the future development of procurement disciplines in PTAs. It would follow that PTAs which presently do not set out detailed procedural rules should not be seen as inferior instruments, and ought not necessarily to pursue the objective of alignment with the GPA. This would apply particularly to the minority of PTAs which do not envisage this objective.[92] A number of reasons for regulation by general principles are reflected in this Chapter.

Some of the rules which have been preserved in the GPA 2008 arguably do not contribute towards the achievement of the Agreement's objectives enough to warrant their retention. It is difficult to see a convincing rationale for preventing central government (Annex 1) entities from using all types of invitation to participate. A simplification to make all forms of invitation available to all entities might have been a sensible development. There is a limit to how much weight can be

91 Blank and Marceau report that a consensus emerged on this point during an information gathering exercise on discriminatory measures and practices undertaken by the Trade Committee of the Organization for Economic Co-operation and Development in the early 1960s: Blank and Marceau, above n. 10.

92 Chapter 16 of the Chile–Costa Rica Free Trade Agreement exemplifies the approach of regulation through general principles which are not supplemented by detailed award procedure rules. There also does not appear to be any link with WTO developments.

attached to this example, however. The proposed simplification would surely have been considered in the negotiations leading to the GPA 2008. The prevailing view must have been this simplification would have adversely affected transparency and competition.

A second possible reason for regulation by general principles alone is that detailed rules have to continuously respond to changes in procurement methods at the national level, for example, to make use of electronic purchasing methods. There is a danger of the rules becoming ever more technical and difficult to apply particularly as it is inevitable that drafting errors creep in. It is possible that these problems are not sufficiently offset by any increased transparency achieved by detailed rules as opposed to general principles. The discussion above on time limits provides a case in point. The GPA 2008 has responded to the advent of electronic means of communication by specifying the extent to which deadlines can be reduced. This has resulted in the introduction of a small drafting error and, even before the rules were supplemented, it was questioned '. . . whether such detailed provisions are needed, and whether a simple rule that time limits must be adequate for suppliers to respond would not be satisfactory'.[93]

These are clearly not insurmountable problems, and the human urge to supplement general principles with specific rules is not something which can be easily suppressed. However, there is a third and more fundamental reason for a move away from the detailed regulation of award procedures. There are examples of developed country governments beginning to focus more on the outcome of the procurement process rather than the process itself. Such initiatives involve the exercise of broad discretion by entities as to how the procurement is conducted, coupled with audit mechanisms to assess the extent to which value for money has been achieved.[94] The exercise of this discretion for a covered contract would breach the GPA unless the preferred procedures happened to correspond with those of the GPA. Arrowsmith therefore suggests the possibility of Parties or entities having the 'choice between the traditional rule-based approach of the GPA or an approach based on principles backed up by additional enforcement measures'.[95]

93 Arrowsmith, above n. 12, at p. 421.

94 One of the leading examples of this approach is the UK's 'Best Value' regime which applies to local authorities and which was introduced by the Labour government partly in order to replace Compulsory Competitive Tendering. On the 'Best Value' regime, see Stephen Cirell and John Bennett, *Best Value Law and Practice* (London: Sweet & Maxwell, 1999). Best Value is itself presently the subject of legislative reform. It is interesting to note an observation recently made by Cirell and Bennett: 'Best Value did not succeed in delivering the outcomes planned by the Government. The reason for this may well be the way Best Value was introduced, meaning that a procedural "machinery" of Best Value grew up which distracted from the main aim'. This perhaps indicates that it is difficult to pin point when, and how, general principles should be supplemented with detailed guidance. See Stephen Cirell and John Bennet, 'Best Value, The White Paper and the New Local Government Bill' (15 February 2007), available at www.info.gov.za/greenpapers/1997/publicproc.htm (visited 27 February 2007).

95 Arrowsmith, above n. 12, at p. 437.

It will be necessary to think further about proposals of this kind if national experience with procurement methods involving the exercise of broad discretion grows. However, for the foreseeable future, moves back towards regulation by general principles alone can probably be regarded as a developed country perspective. Indeed, for a large proportion of developing countries, the GPA (and PTAs with procurement content which strongly resembles the GPA) might be seen as embodying too much flexibility and discretion, bearing in mind factors such as the present level of professionalisation of procurement officers. This sentiment is reflected in comments made in connection with the revision of the UNCITRAL Model Law on Procurement of Goods Construction and Services.[96] The need to take account of electronic auctions has been recognised here, just as is has been in the GPA context, but seems to have been regarded as presenting both threats and opportunities. The Secretariat has reported the view of delegates that, '. . . the Model Law had promoted so far traditional open tendering as a "gold standard", whose fundamental principles included prohibition of negotiations and a single opportunity for a supplier to submit its best tender, which were contradicted by the inherent features of electronic reverse auctions'.[97] Also noted is that electronic auctions, 'might be prone to elevated risks of corrupt practices through outsourcing decision-making beyond government, such as to third-party software and service providers'.[98]

This perspective could be regarded as casting doubt on the aspiration towards GPA membership expressed in many PTAs. Questions considered above again become relevant.[99] In implementing the GPA, how much leeway do Parties have in deciding where the balance lies between objectives such as value for money and the prevention of corruption? Is there a failure to implement the GPA where the choice between overall award criteria is made by the Party itself, rather than on a case-by-case basis by procuring entities? An answer to the second question has been provided by the European Court of Justice, although it has been argued that this answer should not be transposed to the GPA and PTA contexts. Even though the provisions at issue are closely comparable in their wording, regard should be had to the

96 The text of this Model Law is available at www.uncitral.org/uncitral/en/uncitral_texts/procurement_infrastructure/1994Model.html. The rationale for producing the Model Law on procurement was to address differences in national rules which might present unnecessary obstacles to international trade. The Model has not been examined in this Chapter because its content goes significantly beyond what is typically found in PTAs. It provides a useful starting point for states embarking on the task of developing national procurement rules. See Sue Arrowsmith, 'Public Procurement: An Appraisal of the UNCITRAL Model Law as a Global Standard' (2004) 53(1) *International and Comparative Law Quarterly* 17–46.

97 Report of Working Group I (Procurement) on the work of its ninth session A/CN.9/595, at para. 87. The preference for open tendering referred to in the quoted passage emerges most clearly from the Guide to Enactment which accompanies the Model Law. Paragraph 16 of its Introduction provides that some of the key features of tendering as provided for in the Model Law include: 'as a general rule, unrestricted solicitation of participation by suppliers or contractors'.

98 Report of Working Group I (Procurement) on the work of its tenth session A/CN.9/615, at para. 46.

99 See section IIB.

difference between what is required to create a single market, and what is required for the more modest objective of trade liberalisation.

Subject therefore to the need to think about a completely different approach to regulation to accommodate the practices of some developed countries, the GPA's influence on the development of PTAs can be welcomed. It embodies a particular conception of how the primary end of international regulation can best be achieved, and of how this end should be balanced against sometimes conflicting national objectives, but it also represents an admirable attempt to balance the priorities of states at very different levels of development.

11

Intellectual property

MICHAEL HANDLER AND BRYAN MERCURIO

I. Introduction

The Agreement on Trade-Related Aspects of Intellectual Property (TRIPS Agreement) forever changed the relationship between intellectual property (IP) and international trade. While there had always been a link between IP and international trade, the TRIPS Agreement formally integrated the two areas at the multilateral level for the first time. The TRIPS Agreement is comprehensive in its coverage of IP: it deals with copyright and related rights, trademarks, geographical indications (GIs), industrial designs, patents, layout-designs of integrated circuits and protection of undisclosed information, and contains further provisions relating to anti-competitive practices in contractual licences and enforcement of IP rights. Further, much like other covered agreements of the WTO, the most-favoured-nation (MFN) and national treatment (NT) principles lie at the heart of the Agreement.

Where the TRIPS Agreement is perhaps unusual is that it establishes standards of IP protection that each WTO Member must accord to nationals of other Members.[1] Such a regulatory, harmonised approach is different from the approaches of the other covered agreements of the WTO and might have prevented further developments outside of the multilateral forum. However, Members are specifically permitted under the Agreement to apply higher levels of protection if they so desire, as long as the principles of MFN and NT are respected.[2] Thus unlike Article XXIV of the GATT, Article 4 of the TRIPS Agreement does not exempt Preferential Trade Agreements (PTAs) from the operation of MFN – any Member which grants 'any advantage, favour, privilege or immunity' to the nationals of *any* other country (whether a WTO Member or not) must accord the same treatment to the nationals of other WTO Members.

Such higher standards of IP protection than those mandated by the TRIPS Agreement are often called 'TRIPS-Plus' provisions. Members may negotiate PTAs

1 TRIPS Agreement, Article 1.3. The Agreement also requires that Members comply with certain provisions of other international IP agreements, most notably the Paris Convention for the Protection of Industrial Property (1967) (TRIPS Agreement, Article 2.1) and the Berne Convention for the Protection of Literary and Artistic Works (1971) ('Berne Convention') (excluding Article 6*bis*) (TRIPS Agreement, Article 9.1).

2 TRIPS Agreement, Article 1.1.

which provide for TRIPS-Plus provisions that require, *inter alia*, the inclusion of additional protectable subject matter, broader and more extensive standards of protection, stronger enforcement mechanisms, and a weakening of 'flexibilities' and 'special and differential treatment' granted to developing and least developed countries in the TRIPS Agreement. The effect of these provisions is, in part, to 'ratchet up' international IP standards, as the more PTAs are negotiated, the more far-reaching the implications of the PTA provisions become. In such a circumstance, it appears that if enough PTAs are negotiated containing TRIPS-Plus provisions, some of these may well become the new minimum standards from which any future WTO trade round will proceed.[3]

This chapter does not attempt to analyse comprehensively all recent negotiations involving TRIPS-Plus provisions. Instead, it seeks to illustrate certain trends by highlighting and considering some of the more popular, important and potentially far-reaching TRIPS-Plus provisions that have recently been negotiated. Our analysis in this chapter will therefore focus on three areas of IP – copyright, geographical indications and patents – as well as briefly considering overarching issues of enforcement.[4]

II. Subject area analysis

A. Copyright

While numerous PTAs make specific reference to copyright law,[5] it is in those PTAs negotiated by the United States (US) that we see the imposition of the most significant obligations going beyond those required by the TRIPS Agreement. Two of the most notable areas in this regard relate to the term of copyright protection and to the protection of technological protection measures.[6]

1. Extension of copyright term

By virtue of Article 7(1) of the Berne Convention for the Protection of Literary and Artistic Works, which is incorporated into the TRIPS Agreement through Article 9.1, WTO Members are required to grant a minimum term of copyright protection for

3 See Bryan Mercurio, 'TRIPS-Plus Provisions in PTAs: Recent Trends', in Lorand Bartels and Federico Ortino (eds.), *Regional Trade Agreements and the WTO Legal System* (Oxford: Oxford University Press, 2006), pp. 215–37, at p. 223.

4 Even within this framework, considerations of space force us to narrow our scope to only some contemporary and controversial issues.

5 See, e.g., Japan–Malaysia Economic Partnership Agreement, Article 122; and Singapore–Australia Free Trade Agreement, Chapter 13, Article 3.

6 For discussion of other copyright provisions in the context of US PTAs, see Pedro Roffe, *Bilateral Agreements and a TRIPS-Plus World: The Chile–USA Free Trade Agreement*, TRIPS Issues Papers 4 (Ottawa: Quaker International Affairs Programme, 2004), at pp. 27–9 and 31–2, at www.qiap.ca/pages/documents/Chile_US_final.pdf.

most literary and artistic works (excluding photographs) that expires fifty years after the death of the author.[7] The TRIPS Agreement further stipulates that the minimum term of protection for certain works whose term is not calculated by reference to the life of the author (which might include collective works) is to be fifty years from the first publication or the making of the work (Article 12). In addition, it provides a minimum term for performances of fifty years from the first fixation of the performance, and for phonograms of fifty years from the first publication of the phonogram (Article 14.5). These terms broadly reflected US law as it stood in 1994.

In 1993, however, the European Communities (EC) required its member States to adopt a term of protection for most literary and artistic works (including photographs) of the life of the author plus seventy years, and for a range of other works of seventy years from the first lawful making available of the work.[8] Further, member States were placed under an obligation not to apply this TRIPS-Plus term to works from countries, such as the US, with shorter terms of protection. Such works were only to be protected in the EC for the shorter term provided for under the laws of their originating countries.[9] This was a significant factor that drove the US Congress to enact domestic legislation in 1998 that increased the term of protection for most works to the life of the author plus seventy years.[10] The US also took the opportunity at that time to raise the term of protection for subject matter whose term was not based on the life of a natural person to the shorter of ninety-five years from publication or 120 years from creation.

Although such domestic legislation proved controversial,[11] the US has since used PTAs and Trade Promotion Agreements (TPAs) with both developed and developing countries to require the term of protection to be extended beyond TRIPS standards to approximate US standards, so that US works are protected for longer in those countries. All but one of its recent PTAs include a requirement that for works (including photographic works), performances and phonograms where the term is to be calculated by the protecting party on the basis of the life of a natural person, the minimum term shall be the life of the author plus 70 years. This TRIPS-Plus requirement first appeared in the United States–Singapore Free Trade Agreement (Article 16.4.4(a)) and was followed in PTAs with Chile (Article 17.5.4(a)),

7 More particularly, fifty years after the end of the year of the death of the author (see *Berne Convention*, Article 7(5)). All references to periods of years in our discussion of copyright term are calculated from the end of the year of the act or event in question.

8 Council Directive 93/98/EEC of 29 October 1993 harmonising the term of protection of copyright and certain related rights [1993] OJ L290/9, Articles 1, 2 and 13.1. This Directive has since been repealed and replaced by Directive 2006/116/EC of the European Parliament and of the Council of 12 December 2006 on the term of protection of copyright and certain related rights 2006/116/EC [2006] OJ L372/12.

9 Council Directive 93/98/EEC, above n. 8, Article 7.1. See also Berne Convention, Article 7(8).

10 See generally Orrin G. Hatch, 'Toward a Principled Approach to Copyright at the Turn of the Millennium' (1998) 59(4) *University of Pittsburgh Law Review* 719–57, at 729–32.

11 Apart from substantial academic criticism, the legislation was the subject of an unsuccessful constitutional challenge in the US Supreme Court: *Eldred* v. *Ashcroft*, 537 US 186 (2003).

Australia (Article 17.4.4(a)), Morocco (Article 15.5.5(a)), Bahrain (Article 14.4.4(a)), Oman (Article 15.4.4(a)) and Korea (Article 18.4.4(a)), in CAFTA–DR (Article 15.5.4(a)) and in TPAs with Peru (Article 16.5.5(a)), Colombia (Article 16.5.5(a)) and Panama (Article 15.5.4(a)). The exception to this trend is the United States–Jordan Free Trade Agreement (one of the earliest PTAs), which does not address the issue.

Where the term of protection for works, performances and phonograms is to be calculated other than by reference to the life of a natural person, there is a strong, albeit surprising, consistency between the PTAs. In PTAs with Singapore (Article 16.4.4(b)), Chile (Article 17.5.4(b)), Australia (Article 17.4.4(b)), Morocco (Article 15.5.5(b)) and Bahrain (Article 14.4.4(b)), in CAFTA–DR (Article 15.5.4(b)) and in TPAs with Peru (Article 16.5.5(b)), Colombia (Article 16.5.5(b)) and Panama (Article 15.5.4(b)), the required minimum term for such works, performances and phonograms is the same: either a minimum of seventy years from the end of the year of the first authorised publication, or, failing such publication within fifty years from creation, a minimum of seventy years from the end of the year of creation.[12] This is somewhat unexpected because these are lesser terms than those provided for under US law. It is noteworthy that while the US Industry Functional Advisory Committee on Intellectual Property Rights for Trade Policy Matters, commenting in the context of the Central America–Dominican Republic–United States (CAFTA–DR–US), thought that such extensions represented a 'major advance' for US interests, it also urged the US to seek to increase the minimum levels of protection in future PTAs,[13] presumably so that these aligned more closely with US standards. Thus far, only the PTA with Oman (Article 15.4.4(b)) does this, requiring a minimum term of ninety-five years from the end of the year of the first authorised publication of the work, performance or phonogram, or, failing such publication, within twenty-five years from creation – a minimum of 120 years from the end of the year of creation.

These provisions would seem to be a windfall for copyright owners in the US as well as each of the above-mentioned countries. They have, however, been the subject of criticism in this latter group of countries. Each is a net importer of copyright products, meaning that the benefits of extension will flow primarily to US owners, at the expense of such works falling into the public domain. This imposes additional costs on the protecting country. For example, in the Australian context it has been suggested that as a result of the term provisions of the Australia–United States Free Trade Agreement (AUSFTA) net royalty payments are likely to be significantly

12 Under Article 18.4.4(b) of the Korea–United States Free Trade Agreement (KORUS PTA), the '70 years from the end of the year of creation' term applies if there has been no authorised publication within twenty-five years of creation of the work.

13 Report of the Industry Functional Advisory Committee on Intellectual Property Rights for Trade Policy Matters (IFAC-3), 'The US–Central American Free Trade Agreement (PTA): The Intellectual Property Provisions' (12 March 2004), at p. 11, at www.ustr.gov/assets/Trade_ Agreements/Bilateral/CAFTA/CAFTA_Reports/asset_ upload_file571_5945.pdf.

increased, additional compliance costs may be imposed on libraries, archives and other cultural organisations, and problems with dealing with 'orphan works' (generally, older works whose copyright owners cannot be located) are likely to be exacerbated.[14] An additional concern, expressed by a number of US commentators, relates to the impoverishment of the 'public domain' that results from term extension, in that the content on which people can rely for education and future creation is limited.[15] Nevertheless, given the potential benefits that are thought to flow to US copyright owners from term extension,[16] the trend for the US to insist on TRIPS-Plus term provisions in its PTAs is likely to continue.[17]

2. Technological protection measures

Technological protection measures (TPMs) are, in short, devices and software developed to prevent unauthorised copying of digital works.[18] The TRIPS Agreement does not deal with TPMs, which only came to prominence in the 1990s in light of advances in information and communication technology that more easily facilitated the copying of works in digital form. The omission of the issue, however, was seen as a serious oversight by content holders and software organisations.[19] As such, these organisations lobbied for legal protection of TPMs in an alternative forum, namely the World Intellectual Property Organisation (WIPO), which included provisions on TPMs in the WIPO Copyright Treaty (1996) (WCT) and the WIPO Performances and Phonograms Treaty (1996) (WPPT). These require Contracting Parties to provide 'adequate legal protection and effective legal remedies against the circumvention of effective technological measures' used by authors, performers and phonogram producers in connection with the exercise of their rights that restrict unauthorised acts in respect of their works, performances or phonograms.[20] The wording of the WCT and WPPT provisions offers a degree of flexibility for Contracting Parties as to the domestic implementation of such protection and remedies.

14 See, e.g., Matthew Rimmer, 'Robbery Under Arms: Copyright Law and the United States–Australia Free Trade Agreement' (2006) 11(3) *First Monday*, at www.firstmonday.org/issues/issue11_3/rimmer/; cf. Allen Consulting Group, *Copyright Term Extension: Australian Benefits and Costs*, Report Commissioned by the Motion Picture Association (March 2003), at www.allenconsult.com.au/publications/download.php?id=249&type=pdf&file=1.

15 See, e.g., Lawrence Lessig, *Free Culture* (New York: Penguin, 2003), Chapters 13–14.

16 Cf. Paul J. Heald, 'Copyright Ownership and Efficient Exploitation: An Empirical Study of American Works Before and After They Enter the Public Domain', in Fiona Macmillan (ed.), *New Directions in Copyright Law* (Cheltenham, UK: Edward Elgar, 2007), vol. 6.

17 See, e.g., the Third Draft Free Trade Area of the Americas (FTAA) Agreement, Chapter XX, Article 9.

18 Two common examples are password protection systems and encryption.

19 See South Centre and Centre for International Environmental Law, 'Intellectual Property and Development: Overview of Developments in Multilateral, Plurilateral, and Bilateral Fora', South Centre and CEIL IP Quarterly Update: First Quarter 2005, at p. 7, at www.southcentre.org/info/sccielipquarterly/ipdev2005q1.pdf.

20 See WCT, Article 11 and WPPT, Article 18.

Almost all of the PTAs concluded by the US contain a provision requiring the parties to ratify or accede to the WCT and WPPT (or affirm that they have done so),[21] thus obliging them to afford at least the protection and remedies outlined above. However, each of these PTAs also contains further, highly detailed requirements on TPMs, similar to those contained in the US Digital Millennium Copyright Act of 1998 (DMCA). While the level of protection varies slightly between PTAs, most impose a similar, restrictive standard.

In each US PTA, apart from that with Jordan, the parties are essentially obliged to impose liability and make civil and criminal remedies available against those engaging in one of two types of conduct involving TPMs.[22] The first is the act of circumventing a TPM that controls access to a protected work, performance, phonogram, or other subject matter. The second is the manufacture of and trafficking in devices, or the provision of services, for the circumvention of all types of TPM (i.e., both access control and copy control devices).[23] This two–tiered approach closely follows that taken under the DMCA.

The PTAs also permit the parties to make available a limited number of exceptions to liability. These include reverse engineering a computer program for interoperability purposes, encryption research by a qualified researcher, government acts undertaken for law enforcement or security purposes, access by libraries or similar institutions for the sole purpose of making acquisition decisions, and particular uses exempted by the parties following periodic government review.[24] However, in line with the position under the DMCA, not all of the exceptions can be made available in relation to both acts of circumvention and the trafficking of circumvention devices/provision of circumvention services.

One area in which the PTAs differ is in their treatment of 'knowledge' in the context of circumvention. For instance, Article 17.7.5(a) of the United States–Chile Free Trade Agreement requires the parties to proscribe only the *knowing* circumvention of an

21 Under Article 4.1 of the US–Jordan PTA the parties are required only to 'give effect to' the substantive provisions of the WCT and WPPT. There is no mention of the issue in the United States–Chile Free Trade Agreement (presumably because both countries were already Contracting Parties at the date of the PTA).

22 Under Article 4.13 of the US–Jordan PTA, the parties are only required to proscribe the second type of conduct.

23 See US PTAs with Singapore, Article 16.4.7(a); Chile, Article 17.7.5(a)–(b); Australia, Article 17.4.7(a); Morocco, Article 15.5.8(a); Bahrain, Article 14.4.7(a); Oman, Article 15.4.7(a); and Korea, Article 18.4.7 (a); CAFTA–DR, Article 15.5.7(a); and TPAs with Peru, Article 16.7.4(a); Colombia, Article 16.7.4(a); and Panama, Article 15.5.7(a). With the exception of the US–Chile PTA, the parties may exempt from criminal liability non-profit libraries, archives, educational institutions and public non-commercial broadcasting entities. Under Article 17.7.5(b) of the US–Chile PTA, '[a] Party may exempt from criminal liability, and if carried out in good faith without knowledge that the conduct is prohibited, from civil liability, acts . . . carried out in connection with a nonprofit library, archive or educational institution'.

24 See US PTAs with Singapore, Article 16.4.7(e)–(g); Chile, Article 17.7.5(d); Australia, Article 17.4.7(a); Morocco, Article 15.5.8(d); Bahrain, Article 14.4.7(e); Oman, Article 15.4.7(d); and Korea, Article 18.4.7 (d); CAFTA–DR, Article 15.5.7(d)–(f); and TPAs with Peru, Article 16.7.4(e)–(f) and (h); Colombia, Article 16.7.4 (e)–(f) and (h); and Panama, Article 15.5.7(d).

effective technological measure. In contrast, PTAs with Singapore (Article 16.4.7(a)), Australia (Article 17.4.7(a)) and Korea (Article 18.4.7(a)) go further in requiring the prohibition of both knowing acts of circumvention and acts where the person had *reasonable grounds to know* that he or she was engaged in circumvention. The trend, however, seems to be for a knowledge requirement to be dispensed with altogether,[25] which more closely accords with the DMCA.

Laws protecting TPMs tend to receive the support of copyright owners concerned about financial losses said to be incurred by widespread and unchecked copyright piracy. Nevertheless, the inclusion of WCT and WPPT-Plus provisions on TPMs in US PTAs is highly controversial. For example, it is said that US-style TPM laws provide over-broad protection to copyright owners in that they prevent consumers from engaging in conduct with copyright works that would not in fact infringe copyright. The exceptions to circumvention liability contained in US PTAs are limited in scope – most notably, they make no provision for circumvention to allow a user to engage in general 'fair use'-type conduct with the protected work. Thus, circumventing a TPM in Chile to make a back-up copy of a protected computer program would be impermissible, even though the making of the back-up copy would not constitute copyright infringement under Chilean law. In addition, it has been argued the exceptions that are allowed under US PTAs intended to ensure access for educational, research and other legitimate interests are so narrowly drafted that they are inadequate for their stated purpose.[26]

It has also been claimed that TPM laws are being used by some copyright owners for anti-competitive purposes and to stifle free expression and scientific research.[27] For example, it has been noted that such laws have been used as part of attempts to segment global markets for films and computer games through region-coding technology, as well as in attempts to control aftermarkets in non-copyright products such as ink cartridges and garage door openers.[28] While not all of these attempts have been successful, such conduct raises questions about whether the full consequences of strong TPM laws have been appreciated.

There is thus a real apprehension that the imposition of DMCA-type provisions in US PTAs, going beyond the mere requirement to accede to the WCT and WPPT, deprives other countries of the ability to draft their TPM provisions and include

25 See US PTAs with Morocco, Article 15.5.8(a)(i); Bahrain, Article 14.4.7(a)(i); and Oman, Article 15.4.7(a)(i); CAFTA–DR, Article 15.5.7(a)(i); and TPAs with Peru, Article 16.7.4(a)(i); Colombia, Article 16.7.4(a)(i); and Panama, Article 15.5.7(a).

26 See, in the context of the DMCA, Pamela Samuelson, 'Intellectual Property and the Digital Economy: Why the Anti-Circumvention Regulations Need to Be Revised' (1999) 14 *Berkeley Journal of Law and Technology* 519–66.

27 See Electronic Frontier Foundation, 'Unintended Consequences: Seven Years Under the DMCA' (April 2006), at www.eff.org/IP/DMCA/?f=unintended_consequences.html.

28 See Dale Clapperton and Stephen Corones, 'Locking in Customers, Locking out Competitors: Anti-Circumvention Laws in Australia and Their Potential Effect on Competition in High Technology Markets' (2006) 30(3) *Melbourne University Law Review* 657–715.

exceptions that best take into account the needs and concerns of users of copyright material in those countries.[29] Strong doubts have also been raised as to whether such provisions are, in practice, likely to raise standards beyond those required by the WCT and WPPT in any meaningful manner.[30] However, as with the issue of copyright term, it is probable that TRIPS-Plus provisions on TPMs, in a form similar to the DMCA provisions, will continue to be a key feature of future US PTAs.

B. Geographical indications

The TRIPS Agreement imposes complex obligations on WTO Members to protect other Members' GIs, defined in Article 22.1 as 'indications which identify a good as originating in the territory of a Member, or a region or locality in that territory, where a given quality, reputation or other characteristic of the good is essentially attributable to its geographical origin'. These obligations include providing the legal means to prevent misleading uses of GIs or uses that constitute unfair competition (Article 22.2), with a higher standard of protection required in respect of GIs for wines and spirits (Article 23.1). They also involve providing for the refusal or invalidation of the registration of a trademark that contains or consists of another Member's GI with respect to goods not originating in the territory indicated, provided (in the case of non-wine or spirit GIs only) that the use of the trademark would mislead the public as to the true place of origin of those goods (Articles 22.3 and 23.2). These obligations are, however, subject to a range of exceptions. For example, a Member is not required to prevent the use of another Member's GI for wines or spirits where the GI has been used in the first Member's territory in respect of goods or services either continuously or in good faith before certain dates (Article 24.4). Nor is a Member under any obligation to protect another's GI where the term has become generic in the first Member's territory (Article 24.6). Further, in implementing GI protection Members must not prejudice the eligibility for or validity of either the registration of or the right to use certain prior trademarks that are identical with or similar to GIs (Article 24.5).

A number of recent PTAs contain TRIPS-Plus provisions concerning GIs. Some of these provisions are relatively minor. For example, in a number of European Free Trade Association (EFTA) Agreements, parties are simply required to make protection

29 Cf. Switzerland's proposed liberal approach to TPMs: see Lucie Guibault *et al.*, *Study on the Implementation and Effect in Member States' Laws of Directive 2001/29/EC on the Harmonisation of Certain Aspects of Copyright and Related Rights in the Information Society*, Final Report, Institute for Information Law, University of Amsterdam (February 2007), at pp. 93–4 and 121–3, at www.ivir.nl/publications/guibault/Infosoc_report_2007.pdf.

30 See Robert Burrell and Kimberlee Weatherall, 'Exporting Controversy? Reactions to the Copyright Provisions of the US–Australia Free Trade Agreement: Lessons for US Trade Policy', University of Queensland TC Beirne School of Law Research Paper No 07–13 (2007), at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1010833.

available for GIs in respect of *services* as well as goods.[31] However, the most noteworthy TRIPS-Plus provisions relating to GIs are those contained in EC and US PTAs. This is due to the significantly different approaches to GI regulation that have been taken by these parties. In essence, the EC has been using TRIPS-Plus provisions in recent bilateral agreements on trade in wine and/or spirits to secure increased protection amongst certain of its trading partners for European wine and spirit GIs, in particular those that had become generic or semi-generic terms in such countries. In contrast, the major aim of the US appears to be to ensure that its PTA partners implement their TRIPS obligations on GIs in a particular manner to ensure that GIs are not afforded extra levels of protection or given pre-eminence over trademarks.

Before separately analysing the two approaches in detail, it is necessary to place them in context. Despite the fact that the EC and US are broadly in step on many IP issues, the parties have historically disagreed over the relative importance and proper means of protecting GIs. The EC has long considered the strong protection of European GIs – of which there are several thousand – to be a crucial aspect of its agricultural policy of sustaining the rural European economy. To this end it has established systems specifically regulating the use of GIs for agricultural foodstuffs, wines and spirits.[32] These provide for high levels of protection that exceed TRIPS standards. The US, on the other hand, despite its burgeoning wine industry, has not traditionally sought to promote artisanal and localised production through its rural policies. It thus has relatively few GIs of value and has shown little interest in regulating GIs in the same manner as the EC. This has meant that producers in the US wishing to identify their goods using GIs must, for the most part, rely on trademark laws (e.g., by obtaining certification trademark registration) or consumer protection legislation, with more detailed laws applying in respect of wines and spirits.[33]

Given these domestic attitudes, it is unsurprising that the EC and US have clashed over the international protection of GIs. The incoherence of the GI Section of the TRIPS Agreement, negotiated largely by the EC and the US – in which Members are obliged to provide different levels of protection depending on the goods to which the GI relates and in which various substantive issues were left open for further negotiation – is testament to the deep divisions between the parties on the issue. More recently, the EC has been at the forefront of a campaign at the WTO to

31 See the Convention Establishing EFTA (Vaduz Convention), Annex J, Article 5; and EFTA PTAs with Croatia, Annex VII, Article 3; the Former Yugoslav Republic of Macedonia (FYROM), Annex V, Article 3; Jordan, Annex VI, Article 3; Korea, Annex XIII, Article 5; Lebanon, Annex V, Article 6; Mexico, Annex XXI, Article 3; Morocco, Annex V, Article 3; Singapore, Annex XII, Article 5; and Turkey, Annex XII, Article 3.

32 See Council Regulation (EC) No 510/2006 of 20 March 2006 on the protection of geographical indications and designations of origin for agricultural products and foodstuffs [2006] OJ L93/12; Council Regulation (EC) No 1493/1999 of 17 May 1999 on the common organisation of the market in wine [1999] OJ L179/1; Council Regulation (EEC) No 1576/89 of 29 May 1989 laying down general rules on the definition, description and presentation of spirit drinks [1989] OJ L160/1.

33 See generally Justin Hughes, 'Champagne, Feta, and Bourbon: The Spirited Debate About Geographical Indications' (2006) 58(2) *Hastings Law Journal* 299–386.

increase the scope of protection that Members must afford to GIs. This has involved calling for the higher standard of protection currently applying only to wine and spirit GIs under Article 23.1 of the TRIPS Agreement to apply to all GIs, and for Members to accept unconditionally a list of forty-one selected European GIs (including such controversial expressions as 'Feta', 'Prosciutto di Parma', 'Champagne' and 'Porto') as non-generic, protected terms. The EC has also called for the establishment of a multilateral register for the notification and registration of GIs that would facilitate the international protection of its own GIs and marginalise the role of the TRIPS Article 24 exceptions.[34] Not only has the US consistently opposed the EC's agenda, but it also initiated dispute settlement proceedings against the EC at the WTO, claiming in part that the EC's domestic laws regulating GIs for agricultural foodstuffs violated its TRIPS obligations.[35] It is arguable that a major aim of the US in bringing such proceedings was to embarrass the EC politically by exposing deficiencies in its GI regime, potentially diminishing its credibility as an advocate for greater international GI protection.[36]

The recent attempts by the EC and the US in their bilateral PTAs to export their particular models of GI protection thus need to be seen as part of an ongoing and larger battle over the scope of GI protection that has been taking place in various international fora.

1. GIs in EC PTAs

Notwithstanding its broader goals outlined above, the EC has so far in the bilateral PTA context concentrated on securing increased protection for its wine and spirit GIs,[37] in return for granting increased access to European markets to foreign producers. This can be seen in the various agreements on trade in wine and/or spirits into which it has entered with Australia,[38] Mexico,[39] South Africa,[40]

34 See Michael Handler, 'The EU's Geographical Indications Agenda and its Potential Impact on Australia' (2004) 15(3) *Australian Intellectual Property Journal* 173–95.

35 See Panel Report, *EC–Trademarks and GIs (US)*.

36 See Michael Handler, 'The WTO Geographical Indications Dispute' (2006) 69(1) *Modern Law Review* 70–80.

37 It may be the case, however, that future EC PTAs and Economic Partnership Agreements will contain provisions seeking increased protection for GIs in line with the EC's broader expansion agenda, as well as stronger protection for IP rights more generally: see Maximiliano Santa-Cruz, *Intellectual Property Provisions in European Union Trade Agreements: Implications for Developing Countries*, ICTSD Programme on Intellectual Property Rights and Sustainable Development Issue Paper 10 (Geneva: ICTSD, 2007), at pp. 33–55, at www.iprsonline.org/ictsd/Dialogues/2007-05-30/Documents/IP%20Provisions%20in%20EU%20Ags.pdf.

38 Agreement between Australia and the European Community on trade in wine [1994] OJ L86/94 ('EC–Australia Wine Agreement').

39 Agreement between the European Community and the United Mexican States on the mutual recognition and protection of designations for spirit drinks [1997] OJ L152/16 ('EC–Mexico Spirits Agreement').

40 Agreement between the European Community and the Republic of South Africa on trade in wines [2002] OJ L28/4 ('EC–South Africa Wine Agreement'), Agreement between the European Community and the Republic of South Africa on trade in spirits [2002] OJ L28/113 ('EC–South Africa Spirits Agreement').

Switzerland,[41] Chile[42] and Canada,[43] each containing detailed provisions on the recognition and protection of certain listed wine and/or spirit GIs. Most recently, the EC and US entered into an Agreement on trade in wine[44] which, although not dealing specifically with the issue of GIs, is significant for its requirements relating to the protection of 'names of origin' for wines, and thus merits separate consideration.

Similar TRIPS-Plus provisions are contained in the EC's agreements with each of the first-mentioned countries above. Three are worthy of particular discussion.

First, in each agreement the parties agree to provide either reciprocal or mutual protection to each other's listed GIs.[45] Unsurprisingly, the vast majority of the GIs required to be protected are European. Under the EC–Mexico Spirits Agreement, for example, the EC is only obliged to protect 'Tequila', 'Mezcal', 'Sotol' and 'Charanda', whereas Mexico is required to protect around 200 European terms.[46] More significant is that the protection under these agreements is to happen *automatically*. There is no scope for the protecting party to determine whether the GI in question is required to be protected under the TRIPS Agreement, and the protecting party must recognise the examination procedure of the other's authorities as sufficient for its domestic purposes.[47] In addition, most agreements impose obligations as to the levels of protection that are to be afforded to the listed GIs. Apart from the EC–Canada Wine and Spirits Agreement, each agreement

41 Agreement between the European Community and the Swiss Confederation on trade in agricultural products [2002] OJ L114/132, Annex 7 ('EC–Switzerland Wine Agreement'), and Annex 8 ('EC–Switzerland Spirits Agreement').

42 Agreement establishing an association between the European Community and its member States, of the one part, and the Republic of Chile, of the other part [2002] OJ L352/1, Annex V: Agreement on trade in wines ('EC–Chile Wine Agreement') and Annex VI: Agreement on trade in spirit drinks and aromatised drinks ('EC–Chile Spirits Agreement').

43 Agreement between the European Community and Canada on trade in wines and spirit drinks [2004] OJ L35/3 ('EC–Canada Wine and Spirits Agreement').

44 Agreement between the European Community and the United States of America on trade in wine [2006] OJ L87/2 ('EC–US Wine Agreement').

45 EC–Australia Wine Agreement, Article 6.1; EC–Mexico Spirits Agreement, Article 4.3; EC–South Africa Wine Agreement, Article 7.1; EC–South Africa Spirits Agreement, Article 5.1; EC–Switzerland Wine Agreement, Article 5.1; EC–Switzerland Spirits Agreement, Article 5.3; EC–Chile Wine Agreement, Article 5.1; EC–Chile Spirits Agreement, Article 5.1; and EC–Canada Wine and Spirits Agreement, Articles 10.1, 11.1, 14.1 and 15.1.

46 See EC–Mexico Spirits Agreement, Annexes I and II (as modified by Commission Decision 2004/785/EC of 26 October 2004 on the conclusion of an Agreement in the form of an exchange of letters between the European Community and the United Mexican States concerning amendments to Annex II of the Agreement between the European Community and the United Mexican States on the mutual recognition and protection of designations for spirit drinks [2004] OJ L346/28).

47 See David Vivas-Eugui and Christophe Spennemann, 'The Treatment of Geographical Indications in Recent Regional and Bilateral Free Trade Agreements', in Meir Perez Pugatch (ed.), *The Intellectual Property Debate: Perspectives from Law, Economics and Political Economy* (Cheltenham, UK: Edward Elgar, 2006), pp. 305–44, at pp. 315–16.

provides that a party's GIs must not be used in the other party other than under the conditions laid down in the laws and regulations of the *first* party.[48]

The above provisions alter the TRIPS Agreement standards, under which parties are free to determine under their own laws whether the sign in question satisfies the Article 22.1 definition of a GI, and are only obliged under Article 23.1 to provide the 'legal means' to prevent the misuse of the wine or spirit GI (which could well differ from the means used in the originating country). The coercive, detailed approach taken in these agreements is also highly unusual. It is rare in any international agreement dealing with IP to see requirements imposing obligations to provide automatic protection for specified examples of IP (i.e., listed names), as distinct from provisions harmonising the legal standards of the parties that would facilitate such protection.[49] Such an approach demonstrates the importance to the EC of securing as high a level of protection as possible for its wine and spirit GIs in international markets.

Second, and directly related to the first point, the EC agreements do not allow the parties to take advantage of certain key exceptions under the TRIPS Agreement. In fact, only a few exceptions are specifically preserved. All agreements allow the parties to provide dual protection for homonymous GIs (in line with Articles 23.3 and 22.4 of the TRIPS Agreement)[50] and most allow the maintenance of an exception permitting non-misleading use of a trader's personal name (Article 24.8).[51] Some also state that the parties are not obliged to protect a GI that ceases to be protected in its country of origin or has fallen into disuse in that country (Article 24.9).[52] But other TRIPS exceptions are excluded. At times this is done explicitly, such as in the

48 EC–Australia Wine Agreement, Articles 7.2–7.3; EC–Mexico Spirits Agreement, Articles 4.1–4.2; EC–South Africa Wine Agreement, Article 7.2; EC–South Africa Spirits Agreement, Article 5.2; EC–Switzerland Wine Agreement, Article 5.2; EC–Switzerland Spirits Agreement, Articles 5.1–5.2; EC–Chile Wine Agreement, Article 5.2; and EC–Chile Spirits Agreement, Article 5.2.

49 However, this approach is taken in other PTAs not involving the EC where countries consider that they have particular indications worth protecting in foreign markets: see, e.g., Canada–Chile Free Trade Agreement, Annex C–11 (under which Chile is required to protect the GI 'Canadian whisky' in return for Canada protecting the Chilean wine GI 'Chilean Pisco'); China–Chile Free Trade Agreement, Article 10 and Annexes 2A and 2B (under which Chile is required to protect 'Shaoxing Wine' and 'Anxi Tieguanyin' in return for China protecting 'Chilean Pisco'); and Korea–Chile Free Trade Agreement, Article 16.4 and Annexes 16.4.3–16.4.4.

50 EC–Australia Wine Agreement, Article 6.5; EC–Mexico Spirits Agreement, Article 6; EC–South Africa Wine Agreement, Articles 7.4–7.5; EC–South Africa Spirits Agreement, Articles 5.4–5.5; EC–Switzerland Wine Agreement, Article 5.4; EC–Switzerland Spirits Agreement, Article 7; EC–Chile Wine Agreement, Articles 5.4–5.5; EC–Chile Spirits Agreement, Articles 5.4–5.5; and EC–Canada Wine and Spirits Agreement, Article 34.1.

51 EC–Australia Wine Agreement, Article 6.6; EC–Mexico Spirits Agreement, Article 7; EC–South Africa Wine Agreement, Article 7.6; EC–South Africa Spirits Agreement, Article 5.6; EC–Switzerland Spirits Agreement, Article 8; EC–Chile Wine Agreement, Article 5.6; EC–Chile Spirits Agreement, Article 5.6; and EC–Canada Wine and Spirits Agreement, Article 34.2.

52 EC–Australia Wine Agreement, Article 6.7; EC–Mexico Spirits Agreement, Article 8; EC–South Africa Wine Agreement, Article 7.7; EC–South Africa Spirits Agreement, Article 5.7; EC–Switzerland Spirits Agreement, Article 9; and EC–Canada Wine and Spirits Agreement, Article 34.2.

EC–Mexico Spirits Agreement and the two EC–Switzerland Agreements, each of which contain express waivers of Articles 24.4–24.7 of the TRIPS Agreement.[53] In other agreements, this exclusion is implicit in the fact that each party is obliged to provide exclusive protection to the listed GIs of the other.[54]

The significance of the EC's approach to the TRIPS exceptions is that it obliges the other parties to its agreements to protect terms that may have become generic wine or spirit descriptions in those countries (such as champagne, sherry and port), and to cancel the registration of trademarks identical with or similar to protected GIs, even if such rights were acquired before the coming into force of the TRIPS Agreement in that country. Such provisions have, however, proven to be highly contentious. For example, negotiations between the EC and South Africa in the late 1990s over the much larger Trade, Development and Cooperation Agreement almost broke down over the EC's insistence that South Africa cease using certain generic wine and spirit denominations.[55] In this regard, it is worth noting that some of the EC agreements contain detailed provisions allowing for the gradual phasing out of generic names in non-EC countries. Thus, under the EC–South Africa Agreements, South Africa is required to phase out the domestic and export use of such names as 'Sherry' and 'Ouzo'.[56] In the area of trademarks, the EC–Chile Agreements list various registered Chilean trademarks for names such as 'Moselle' and 'La Rioja' that must be cancelled within particular periods of time.[57]

It is also worth mentioning that the EC's approach to the TRIPS exceptions in its bilateral agreements is consistent with its broader extension agenda at the WTO. Under the EC's model for a multilateral register for the notification and registration of GIs under Article 23.4 of the TRIPS Agreement, a WTO Member would be required to protect another Member's nominated GI unless it lodges an objection, which could only be based on a limited number of TRIPS Article 24 exceptions (not including the exception for prior trademarks).[58] When combined with the EC's separate demand for the 'claw-back' of forty-one GIs, including wine and spirit terms understood as generic in many countries, this demonstrates that at the multilateral level the EC is attempting to reclaim the use of generic terms and to establish some form of primacy of GIs over trademarks. While the EC has had

53 EC–Mexico Spirits Agreement, Article 4.4; EC–Switzerland Wine Agreement, Article 5.7; and EC–Switzerland Spirits Agreement, Article 5.4.

54 Cf. Articles 34.2–34.3 of the EC–Canada Wine and Spirits Agreement, which preserve some aspects of the TRIPS Articles 24.5 and 24.6 exceptions.

55 Emily Craven and Charles Mather, 'Geographical Indications and the South Africa–European Union Free Trade Agreement' (2001) 33(3) *Area* 312–20, at 313–5.

56 EC–South Africa Wine Agreement, Article 25; and EC–South Africa Spirits Agreement, Article 23.

57 EC–Chile Wine Agreement, Article 7 and Appendix VI; and EC–Chile Spirits Agreement, Article 7 and Appendix VI (see also Article 8.4, which provides that certain trademarks may not be used to prevent the use of protected GIs).

58 WTO Documents IP/C/W/107/Rev.1 (22 June 2000), TN/IP/W/3 (24 June 2002), and WT/GC/W/547 (14 June 2005).

difficulty in the multilateral arena in encouraging other WTO Members to accept these demands, it is having greater success at the bilateral level in the context of wine and spirit GIs.

Third, EC Wine Agreements with Australia, Chile and Switzerland go further than requiring the protection of GIs in that they impose obligations to protect certain listed 'traditional expressions'. These are names legally recognised in a country that are traditionally used to refer to the production or ageing method, or the quality, colour or other traditional feature, of wine originating from that country. As with GIs, most of the traditional expressions to be protected are European – examples contained in these agreements include common words such as 'ruby', 'tawny', 'vintage' and 'superior'. Traditional expressions are not recognised as a form of intellectual property under the TRIPS Agreement and the requirement that non-EC countries protect European traditional expressions is a potentially onerous one in that it deprives traders in those countries of the ability to use ordinary, descriptive terms that their consumers would not associate with a particular country's wines or spirits.[59] While the EC has stated in WTO negotiations that it is not seeking to have traditional expressions included in its proposed multilateral GI register,[60] it will be worth seeing whether it seeks increasingly to protect these potentially valuable terms in future bilateral agreements.

The EC–US Wine Agreement is different from the above-mentioned agreements. It is the product of a longstanding difference of opinion between the parties over, amongst other things, whether the US provides adequate legal protection for European wine GIs. Under US law a geographical term that is also understood in the US to describe a class of wine can be designated as 'semi-generic'. Such a term may be used on wine originating other than in the geographical region suggested by the term, provided that the true place of origin is indicated. Designated semi-generic terms in the US include famous European GIs such as 'burgundy', 'champagne', 'chianti', 'madeira', 'port' and 'sherry'.[61] The key feature of the EC–US Wine Agreement that goes much of the way to resolving the conflict between the parties over this issue is the requirement under Article 6.1 for the US to seek to change the legal status of the terms currently designated as semi-generic and to restrict the use of such terms on wine labels solely to wine originating in the EC. This is subject to a 'grandfathering' provision in Article 6.2, which allows for the continued use of semi-generic names where used on wine labels bearing a certified brand name where the certification was issued before 10 March 2006. In addition, under Article 7, certain listed European and US 'names of origin' are only to be used to designate wines with

59 Vicki C. Waye, 'Assessing Multilateral vs Bilateral Agreements and Geographic Indications Through International Food and Wine' (2005) 14(2) *Currents: International Trade Law Journal* 56–68, at 60–1.

60 WTO Document TN/IP/M/5 (28 April 2003), paras. 44 and 49.

61 See 26 USC §5388(c); 27 CFR §4.24(b) (2006). See further Leigh A. Lindquist, 'champagne or Champagne? An Examination of US Failure to Comply with the Geographical Provisions of the TRIPS Agreement' (1999) 27(2) *Georgia Journal of International and Comparative Law* 309–44, at 326–9.

those geographical origins. In return for agreeing to protect or phase out the use of certain European geographical names, the US has secured more stable access to EC markets for wines made in accordance with practices not recognised in the EC.[62]

Interestingly, the Agreement refers only to 'terms' and 'names of origin', and Article 12.4 states that the names to be protected 'are not necessarily considered, nor excluded from being considered, geographical indications' under either US or EC law. Article 12.1(a) further provides that nothing in the Agreement shall 'affect the rights and obligations of the Parties under the WTO Agreement'. Notwithstanding this, it is hard to see how the EC–US Wine Agreement could be interpreted other than to impose conditions on the US's treatment of EC GIs, and in this light it can be said to impact on and extend the US's TRIPS obligations. Further, it will be interesting to see whether the consensus reached on this issue by the two major antagonists over the international protection of GIs will have any impact on negotiations for the establishment of the multilateral GI register for wines and spirits that are currently stalled at the WTO.[63]

2. GIs in US PTAs

Separate from its specific dealings with the EC on wine, the US has included detailed GI provisions in most of its recent PTAs. Unlike the EC, however, this has not been done primarily for the benefit of US producers wishing to secure stronger protection for their GIs in foreign countries.[64] Rather, the goal of the US appears to be to encourage other countries to adopt a particular model of protection of GIs, namely through trademark law. The hoped-for result is that such countries will not provide special treatment to GIs and, in particular, will not give GIs primacy over traditional trademarks in the event of any conflict between the two. While such parties remain free under these PTAs to implement *sui generis* systems regulating GIs that afford high levels of protection, along the lines of the EC model, this is potentially made more difficult in light of the fact that they are obliged to make trademark protection available for GIs. The US approach can therefore be seen as a tactic being employed as part of its broader strategy of resisting EC attempts to have the European model of GI protection become a *de facto* global standard.

62 See EC–US Wine Agreement, Article 4.2.

63 Timothy E. Josling, 'The War on *Terroir*: Geographical Indications as a Transatlantic Trade Conflict' (2006) 57(3) *Journal of Agricultural Economics* 337–63, at 355.

64 The US has, however, sought specific recognition for the names 'Bourbon Whiskey' and 'Tennessee Whiskey' in the Market Access chapters of some of its PTAs and TPAs: see PTAs with Chile, Article 3.15.1 (in return for the US recognising 'Pisco Chileano', 'Pajarete' and 'Vino Asoleado': Article 3.15.2); Korea, Article 2.13.1 (in return for the US recognising 'Andong Soju' and 'Gyeongju Beopju': Article 2.13.2); CAFTA–DR, Article 3.12.1; and TPAs with Peru, Article 2.12.1 (in return for the US recognising 'Pisco Perú': Article 2.12.2); Colombia, Article 2.12.1; and Panama, Article 3.12.1. See also exchange of side letters between Mark Vaile, Australian Minister for Trade, and Robert B. Zoellick, USTR, 18 May 2004, at www.ustr.gov/assets/Trade_Agreements/Bilateral/Australia_PTA/Final_Text/asset_upload_file778_3889.pdf.

We now turn to the GI provisions of US PTAs. Despite some differences in structure there is a strong degree of consistency between them in terms of substance. For a start, each PTA makes clear that GIs may be protected as trademarks. In PTAs with Jordan (Article 4.6), Singapore (Article 16.2.1), Chile (Article 17.2.1), Australia (Article 17.2.1) and Korea (Article 18.2.2), in CAFTA–DR (Article 15.2.1) and in the TPA with Panama (Article 15.2.1), it is explicitly stated that the parties are to provide that trademarks may include GIs. PTAs with Bahrain (Article 14.2.2) and Oman (Article 15.2.2) and TPAs with Peru (Article 16.2.2) and Colombia (Article 16.2.2) contain a more detailed requirement that GIs may constitute certification or collective marks (themselves a subset of trademarks).[65] In addition, a number of PTAs provide that GIs may consist of much the same subject matter as trademarks, namely words (including personal and geographic names), as well as letters, numerals, figurative elements and colours (including single colours).[66]

The approach of conflating GI and trademark protection has been criticised as 'undermining the intention of the drafters of the TRIPS Agreement, which specifically established two different categories of IPRs'.[67] However, this criticism is misplaced. Not only does it assume that a settled 'intention' of the drafters can be discerned from such a heavily compromised negotiating process in relation to the GI Section,[68] but it also pays insufficient regard to Article 1.1 of the TRIPS Agreement, which provides that 'Members shall be free to determine the appropriate method of implementing the provisions of this Agreement within their own legal system and practice'. While the US approach might cause a degree of consternation amongst those more familiar with *sui generis* models of GI protection, there is nothing illogical or conceptually problematic about protecting GIs through trademark law. What is more interesting is to explore some of the consequences of requiring countries to adopt this particular model of GI protection.

One noted outcome of the US approach is that it establishes a potentially different set of obstacles for individual traders to overcome in order to secure protection for their GIs compared with those likely to be faced under a *sui generis* system. Some of these obstacles are the result of specific terms of the PTAs which oblige countries to have particular procedures in place relating to applications for GI protection.[69]

65 While the United States–Morocco Free Trade Agreement does not contain such an explicit statement, it is clear that GIs may be protected as trademarks from Article 15.2.5, which states that '[e]ach Party may provide limited exceptions to the rights conferred by a trademark, including a geographical indication'.

66 See US PTAs with Chile, Article 17.4.1; Australia, Article 17.2.1, note 17–5; Morocco, Article 15.3.3; Bahrain, Article 14.2.2, n. 4; Oman, Article 14.2.2, n. 4; and Korea, Article 18.2.2, n. 5. See also TRIPS Agreement, Article 16.1.

67 Vivas-Eugui and Spennemann, above n. 47, at p. 327. See also Bernard O'Connor, 'The EC Need not be Isolated on GIs' (2007) 29(8) *European Intellectual Property Review* 303–6, at 306.

68 See UNCTAD–ICTSD, *Resource Book on TRIPS and Development* (New York: Cambridge University Press, 2005), at pp. 279–89.

69 See US PTAs with Chile, Articles 17.4.4–17.4.8; Australia, Article 17.2.12; Morocco, Article 15.3.1; Bahrain, Article 14.2.12; Oman, Article 15.2.13; and Korea, Article 18.2.14; CAFTA–DR, Articles

Others are simply due to the inherent requirements of trademark registration processes. For example, to obtain certification or collective trademark registration for a GI, a party would need to demonstrate that the sign is distinctive. Given that most GIs are geographically descriptive terms and thus not inherently distinctive, acquired distinctiveness would almost invariably need to be established in order to secure registration. Under a *sui generis* system for protecting GIs, no such requirement would be likely to exist.[70] However, the effect of these differences should not be overstated, for it cannot be said that obtaining trademark protection for GIs would necessarily be a more onerous process. For example, under the *sui generis* EC regime a party seeking registration of a GI for an agricultural product needs to comply with a number of detailed procedural and substantive requirements[71] that an applicant for certification or collective trademark registration in, say, the US would not need to satisfy.[72]

A different, and much more significant, consequence of the US approach to GIs in its PTAs is that it encourages countries to prioritise trademarks over GIs in the event of any conflict between them. For example, each PTA obliges countries to grant to owners of registered trademarks the exclusive right to prevent third parties from using in the course of trade identical or similar signs – specifically stated to include GIs – for goods or services related to those in respect of which the trademark is registered, where such use would result in a likelihood of confusion.[73] In addition, PTAs with Oman (Article 15.2.7) and Korea (Article 18.2.7) include a provision requiring the prohibition of the use of a mark or GI that is identical or similar to a well-known trademark if the use of the mark or GI is 'likely to cause confusion, or to cause mistake, or to deceive or risk associating the trademark or geographical indication with the owner of the well-known trademark, or constitutes unfair exploitation of the reputation of the trademark'. While these provisions might, in isolation, give trademarks precedence over conflicting GIs, most PTAs allow parties to provide exceptions to trademark owners' rights in line with Article 17.1 of the TRIPS Agreement.[74] In *EC–Trademarks and GIs*, the WTO panel determined, in effect, that a provision of EC law that allowed for the co-existence of a later GI with an earlier trademark was, in the circumstances, a permissible exception under

15.3.2–15.3.6; and TPAs with Peru, Article 16.3.1; Colombia, Article 16.3.1; and Panama, Articles 15.3.2–15.3.6.

70 See Roffe, above n. 6, at p. 41. 71 Council Regulation (EC) No 510/2006, above n. 32, Articles 4–5.

72 See Hughes, above n. 33, at 309–11.

73 See US PTAs with Jordan, Article 4.7; Singapore, Article 16.2.2; Chile, Article 17.2.4 (with a limitation to 'subsequent' GIs); Morocco, Article 15.2.4; Australia, Article 17.2.4; Bahrain, Article 14.2.4; Oman, Article 15.2.4; and Korea, Article 18.2.4; CAFTA–DR, Article 15.2.3; and TPAs with Colombia, Article 16.2.4; Peru, Article 16.2.4; and Panama, Article 15.2.3. In the PTAs with Morocco, Australia, Oman and Korea, CAFTA–DR and the TPA with Panama it is further stipulated that a likelihood of confusion shall be presumed 'in the case of the use of an identical sign, including a geographical indication, for identical goods or services'.

74 See US PTAs with Singapore, Article 16.2.3; Chile, Article 17.2.5; Morocco, Article 15.2.5; Australia, Article 17.2.5; Bahrain, Article 14.2.5; Oman, Article 15.2.5; and Korea, Article 18.2.5; CAFTA–DR, Article 15.2.4; and TPAs with Colombia, Article 16.2.5; Peru, Article 16.2.5; and Panama, Article 15.2.4.

Article 17.1, even if this resulted in a degree of consumer confusion.[75] Parties to US PTAs could potentially allow for similar exceptions, thus limiting the rights of trademark owners in relation to confusingly similar GIs.

A more telling example of the way in which US PTAs prioritise trademarks over GIs is a provision contained in all PTAs after the US–Singapore PTA that requires parties to provide certain grounds for refusing an application for protection or recognition of a GI. Two such grounds are mandated: first, that the GI is likely to cause confusion with a trademark that is the subject of a good-faith pending application or registration; and second, that the GI is likely to cause confusion with a pre-existing trademark, the rights to which have been acquired through use in good faith in that party.[76] The second of these grounds appears to be a straightforward example of the 'first in time, first in right' principle – that is, the first user of the term in question gains priority.[77] However, the first ground is different because it only requires the application for or registration of the trademark to pre-date the application for protection or recognition of the GI. Thus, it may be the case that a first-used GI will be denied recognition if the application for protection of the GI post-dated the application for registration of a confusingly similar trademark. In either situation, co-existence of conflicting GIs and trademarks is not contemplated, and trademarks are given primacy over GIs.

In summary, it can be seen that the US is taking a consistent approach to GIs in its PTAs in that it is encouraging other countries to adopt a minimalist, trademark-oriented model of legal regulation of GIs, as distinct from a *sui generis* scheme of protection as exists under EC law. Thus, the divergent approaches currently taken by the EC and US to GIs in the bilateral context (apart from in the Wine Agreement between them), and the fact that these approaches are unlikely to change in the foreseeable future, undoubtedly make common understanding on GIs at the multilateral level less likely,[78] short of serious political compromise.

C. *Patents*

While the EC has essentially been the only WTO Member pushing for increased protection of GIs, the US is the only major WTO Member actively negotiating for TRIPS-Plus provisions in the area of patents, particularly in the area of medicines. Thus, while most PTAs either do not directly mention the topic or simply re-affirm

75 *EC–Trademarks and GIs (US)*, paras. 7.644–7.687. See further Handler, above n. 36, at 75–7.

76 See US PTAs with Chile, Article 17.4.10; Morocco, Article 15.3.2; Australia, Article 17.2.12(b)(v); Bahrain, Article 14.2.13; Oman, Article 15.2.14; and Korea, Article 18.2.15; CAFTA–DR, Article 15.3.7; and TPAs with Colombia, Article 16.3.2; Peru, Article 16.3.2; and Panama, Article 15.3.7.

77 See Stephen Stern, 'The Conflict Between Geographical Indications and Trade Marks or Australia Once Again Heads Down the Garden Path' (2005) 61 *Intellectual Property Forum* 28–37, at 31–2.

78 Vivas-Eugui and Spennemann, above n. 47, at p. 338.

that both parties agree to abide by their TRIPS commitments,[79] US agreements contain numerous provisions relating to patents that have the potential to impact significantly upon the provision of health services in signatory countries. Not surprisingly, several of these provisions remain controversial. It must be noted, however, that as a result of pressure stemming from Democratic control of US Congress, future US PTAs will apparently require slightly less onerous commitments in a number of areas, including pharmaceutical patents. The recent TPAs with Peru, Colombia and Panama will apparently be amended to include these new standards and are referenced below.[80]

1. Patent term extensions

The TRIPS Agreement requires Members to grant patent protection for a period of at least twenty years from the date of filing of an application for a patent (Article 33). This is a minimum period of protection and, like other aspects of the TRIPS Agreement, Members can offer more protection if they so desire. While the grant of a patent entitles most inventors the exclusive right to market and distribute their inventions for the entire twenty-year period, the pharmaceutical industry and other medical researchers do not benefit from the entire period of protection. This is due to the fact that in order to protect their potential medical invention from competitors, those wishing to apply for patent protection must do so at a very early stage of basic research, many years before filing an application for regulatory approval. However, as drugs, vaccines and other medicinal products require lengthy testing periods and regulatory approval (often lasting between eight and twelve years) before they can be marketed and distributed to the public, pharmaceutical patent holders do not get the full benefit of the twenty-year term.

While the TRIPS Agreement does not obligate Members to 'compensate' patent holders for 'unreasonable' delays in approving a patent or registering the product, several Members do attempt to rebalance the effects of the time delay and 'compensate' the pharmaceutical patentee for any 'unreasonable' delay caused by the national drug regulatory authority in examining an application for registration or a patent office in assessing the application for a patent. Such 'compensation'

79 This ranges from agreements negotiated between developing countries (e.g., Armenia–Kazakhstan PTA, Article 11; Bulgaria–Bosnia and Herzegovina PTA, Article 26; and Chile–Costa Rica PTA (no specific provision)), to agreements negotiated between developed and developing nations (e.g., European Union–Jordan Association Agreement, Article 27; EFTA–Tunisia PTA, Article 1; and Japan–Mexico Economic Partnership Agreement, Article 73), to agreements between developed countries (e.g., New Zealand–Singapore Closer Economic Partnership Agreement, Part 9; and Australia–New Zealand Closer Economic Relations Trade Agreement (no specific provision)).

80 See Office of the USTR, Statement from Ambassador Susan C. Schwab on US Trade Agenda, 10 May 2007, at www.ustr.gov/Document_Library/Press_Releases/2007/May/Statement_from_Ambassador_Susan_C_Schwab _on_US_ trade_agenda.html; and Office of the USTR, *Bipartisan Agreement on Trade Policy: Intellectual Property Provisions*, 11 May 2007, at www.ustr.gov/assets/Document_Library/Fact_Sheets/2007/asset_upload_file312_11283.pdf.

occurs by extending the patent term for the same amount of time as the 'unreasonable' delay.[81] For example, Article 17.10.2 of the US–Chile PTA states:

> With respect to pharmaceutical products that are subject to a patent, each Party shall:
>
> (a) make available an extension of the patent term to compensate the patent owner for unreasonable curtailment of the patent term as a result of the marketing approval process . . .

A similar clause appears in US PTAs with Singapore (Article 18.8.4(a)), Australia (Article 17.10.4), Morocco (Article 15.10.3), Bahrain (Article 14.8.6), Oman (Article 15.8.6 (a)) and Korea (Article 18.8.6 (b)) and in CAFTA–DR (Article 15.10.2). Interestingly, in each PTA, the term 'unreasonable' is not defined.

With respect to 'unreasonable' delays in the issuance of a patent, an additional period of patent protection is also available, but it is often stated as a period extending beyond five years from the date of the filing or three years after a request for an extension. For example, Article 17.9.6 of the US–Chile PTA states:

> Each Party *shall* provide for the adjustment of the term of a patent, at the request of the patent owner, to compensate for unreasonable delays that occur in granting the patent. For the purposes of this paragraph, an unreasonable delay shall be understood to include a delay in the issuance of the patent of more than five years from the date of filing of the application in the Party, or three years after a request for examination of the application has been made, whichever is later, provided that periods of time attributable to actions of the patent applicant need not be included in the determination of such delays.[82]

Other US PTAs have similar provisions, with the only variation being the number of years considered 'unreasonable'. For example, PTAs with Singapore (Article 16.7.7), Australia (Article 17.9.8), Morocco (Article 15.9.7), Bahrain (Article 14.8.6) and Oman (Article 15.8.6(a)) refer to four and two years respectively. In Article 16.7.8 of the US–Singapore PTA, there is a further provision regarding a five-year extension of the patent term when a patent is granted based on the examination conducted in another country.[83] The extension will be awarded when it has also been awarded in the other country. Interestingly, the US–Jordan PTA, while containing the extension provision relating to unreasonable delays resulting from the marketing approval process, does not contain an extension provision relating to unreasonable delays in the issuance of a patent.

These provisions are unlikely to have much impact in the developed world. In fact, as noted above, it is common international practice to grant extensions for delays

81 The provisions negotiated by the US reflect domestic American law and have their origins in the US Drug Price Competition and Patent Term Restoration Act of 1984 (Hatch–Waxman Act).

82 Emphasis added. See also KORUS PTA, Article 18.8.6(a); and CAFTA–DR–US, Article 15.9.6.

83 This provision also appears to be in the proposed United States–Andean Trade Promotion Agreement.

caused by registration and examination, especially in developed countries. The concern, however, relates to developing countries with scarce economic resources that may take more time in approving the marketability of drugs and processing patent applications. In the case of the former, how long a delay is to be considered 'reasonable'? One would imagine it will be answered on a case-by-case basis, but would the issuing country and the US agree on the result (especially if the delay is five or six years)? In relation to delays in the issuance of a patent, the time lines assist in the determinative process, but can a delay over and above the timeline set out in the various agreements ever be considered 'reasonable'? It does not appear so.

The extra years added to a patent may also have serious consequences for public health in poorer developing countries.[84] Poorer countries rely on lower prices generated by generic competition in order to supply their populations with many life saving drugs. Delays in allowing generic competition could prevent large portions of the population from accessing needed drugs.

It seems entirely sensible to extend patents when 'unreasonable' delay prevents the patent holder from exploiting their invention, and it is easy to imagine abuse from patent offices and regulatory authorities. However, the undefined nature over what is considered 'unreasonable' as it relates to delays caused by the regulatory process and the strict timeline as relating to delays caused by the patent office are both potentially troublesome.

The recent agreement between the Democratic Party and the Bush Administration, however, alters the standard language used in US agreements in a manner which takes into account the challenges faced by developing countries. More specifically, the US TPAs with Peru (Article 16.9.6), Colombia (Article 16.9.6) and Panama (Article 15.9.6) will be amended to modify the requirement that each party '*shall*' provide for the adjustment of the term of a patent to '*may*', indicating a more flexible approach to the issue.[85] Additionally, the agreements now also state that parties should use their 'best efforts' to process applications expeditiously with a view to avoiding unnecessary delays and call on both parties to co-operate and provide assistance to meet these objectives.[86]

2. Protection of test data

As discussed in the preceding section, before marketing or distributing a drug the manufacturer must apply for regulatory/marketing approval with a national drug regulatory authority to ensure that the drug is safe, effective and of sufficient quality. The regulatory authority does not undertake clinical trials or otherwise test the drugs; instead, it relies on the clinical trials and other data conducted and submitted

84 See Ruth Mayne, *Regionalism, Bilateralism, and 'TRIP Plus' Agreements: The Threat to Developing Countries*, UN Human Development Report Office Occasional Paper 2005/18 (2005), at p. 14, at http://hdr.undp.org/docs/publications/ background_papers/2005/HDR2005_Mayne_Ruth_18.pdf.

85 See Office of the USTR, Statement and *Bipartisan Agreement*, above n. 80. 86 *Ibid.*

by the applicant. When a later applicant (a generic manufacturer) seeks registration of the same drug, it need not re-conduct the same clinical trials but only must submit and prove that the drug it seeks to distribute is of the same quality and therapeutically equivalent to the previously approved drug. This process facilitates the introduction of generic drugs to the market and, without having to conduct any clinical trials, generic manufacturers save resources and can introduce their drug on the market at a reduced rate.

The TRIPS Agreement does not explicitly require Members to provide any period of data exclusivity to an original applicant – that is, it does not explicitly prevent others from using the data of the patent holder in gaining marketing approval. While the interpretation of the TRIPS Agreement on this point is contentious, the wording of Article 39.3 merely states the need to protect 'undisclosed test or other data' from 'unfair commercial use' and 'disclosure', provided that the data required 'considerable effort' to generate, that it is undisclosed and that the product involves a 'new chemical entity'.[87] The provision does not dictate how protection should occur, the limit of such protection or a time period for the protection. On the contrary, the text indicates that it is up to the individual Member to determine what constitutes 'unfairness'.[88] In addition, the provision does not define what is meant by a 'new chemical entity'.

Recent US PTAs, however, seek to bring the US's PTA partners into line with domestic law by preventing the later applicant and the national authority from relying on the clinical studies and data provided by the original applicant when seeking to register the generic version of the drug for a given period of time following the first registration.[89] US PTAs generally seek a five-year period of exclusivity for a new pharmaceutical product (ten years for a new agricultural chemical product). For instance, Article 17.10.1(a) of the AUSFTA reads:

> If a Party requires, as a condition of approving the marketing of a new pharmaceutical product, the submission of undisclosed test or other data concerning safety or efficacy of the product, the Party shall not permit third persons, without the consent of the person who provided such information, to market a same or similar product on the basis of (1) such information or (2)

87 Commentators such as Carlos Correa strongly assert that Article 39.3 is not a limit on generic manufacturers, but rather a requirement that, when data has been submitted to the regulatory agency, it must be protected against 'unfair commercial use': see Carlos M. Correa, *Protection of Data Submitted for the Registration of Pharmaceuticals: Implementing the Standards of the TRIPS Agreement* (Geneva: SADAG, 2002), at www.southcentre.org/publications/protection/protection.pdf.

88 Indeed, during TRIPS negotiations, negotiators rejected the option to include stronger 'data exclusivity' provisions, as originally proposed by the US: see UNCTAD–ICTSD, above n. 68, at pp. 522–6.

89 See Jayashree Watal, *Intellectual Property Rights in the WTO and Developing Countries* (Oxford: Oxford University Press, 2001), at p. 200. US PTAs with Singapore, Article 16.7.5; Chile, Article 17.9.4; Morocco, Article 15.9.6; and Bahrain, Article 14.8.5; and CAFTA–DR, Article 19.5.3 also limit the availability of data to after the expiry of the patent, and if the party permits exportation, the product shall only be exported outside the territory of that party for purposes of marketing approval requirements of that party.

> the approval granted to the person who submitted such information for at least five years from the date of marketing approval in the Party.

Other US PTAs, such as those with Singapore (Article 16.8.1), Chile (Article 17.10.1), Morocco (Article 15.10.1), Bahrain (Article 14.9.1), Oman (Article 15.9.1) and Korea (Article 18.9.1), and CAFTA–DR (Article 15.10.1), contain similar provisions. Moreover, certain agreements contain an additional provision which keeps the data exclusivity period intact even after the expiration of the patent. For instance, Article 17.10.3 of the AUSFTA states:

> When a product is subject to a system of marketing approval pursuant to Article 17.10.1 or 17.10.2 as applicable and is also subject to a patent in the territory of that Party, the Party shall not alter the term of protection that it provides pursuant to Article 17.10.1 and 17.10.2 in the event that the patent protection terminates on a date earlier than the end of the term of protection specified in Article 17.10.1 and 17.10.2, as applicable.

This is also the case in US PTAs with Singapore (Article 16.8.1), Morocco (15.10.1, note 11), Oman (Article 15.9.3) and Korea (Article 18.9.4). However, the new language applying to US TPAs with Peru, Colombia and Panama alters the general data exclusivity provision for a country that relies on the US Food and Drug Administration for marketing approval and grants approval within six months of a US firm's application. In such a circumstance, the period of exclusivity required to be maintained would run 'concurrent' with that in the US, meaning that, no matter when the test data is registered in the PTA-partner country, the exclusivity period expires at the time it would in the US.[90] Moreover, these agreements will also contain an exception to the data exclusivity provision for measures to protect public health in accordance with the Doha Declaration and subsequent implementing protocols.

As a result of the general provisions detailed above, generic manufacturers wishing to market and distribute a generic whilst the period of data exclusivity is in force must conduct their own clinical trials and submit their own findings to the national authority. Such an approach is troublesome, not least because conducting tests and generating clinical data is extremely expensive (sometimes costing into the tens of millions of dollars).[91] The generic industry will find it difficult to implement such onerous requirements, and therefore from a public health perspective, this requirement is difficult to justify.[92] Even if generic manufacturers were able to generate this data, the cost of the resulting drugs produced would rise considerably as well as delay the generics' introduction into the marketplace. Moreover, such

90 See Office of the USTR, Statement and *Bipartisan Agreement*, above n. 80.

91 Robert Weissman, 'Dying for Drugs: How CAFTA Will Undermine Access to Essential Medicines', *Health Now*, 6 March 2004, at www.health-now.org/site/article.php?articleId=75&menuId=13.

92 Sisule F. Musungu and Cecilia Oh, *The Use of Flexibilities in TRIPS by Developing Countries: Can They Promote Access to Medicine*, Commission on Intellectual Property Rights, Innovation and Public Health (CIPIH), Study 4C (August 2005), at p. 66, at www.who.int/intellectualproperty/studies/TRIPSFLEXI.pdf.

duplication of testing could be viewed as unethical, as it simply repeats the testing and clinical trials where safety and efficacy has already been determined.[93]

Even more, the US is also seeking to include provisions in certain regional PTAs which apply a period of data exclusivity from the approval date of another country even if the manufacturer has not sought to register the drug in that particular country.[94] In such a circumstance, the generic manufacturer would still be prohibited from relying on the data for a certain time period with the end result being that the country does not have access to that particular drug until the expiration of the data exclusivity period.

Several US PTAs also effectively prohibit generic manufacturers from using evidence of registration of the originator drug in another country to prove the safety and efficacy of their version. The only condition that can be imposed on the originator is to require that marketing approval be sought within five years of registering the product in a country other than a party to that particular PTA.[95] Depending on how the originator times its entry into the market, the effect of the provision could result in ten years of test data protection. For example, a pharmaceutical company could register the original drug in one of the PTA countries but wait five years before submitting the market approval application in another PTA-member country. It would then be entitled to a further five years of exclusivity from that date.

In addition, certain US PTAs eliminate the Article 39.3 requirement in the TRIPS Agreement which protects data only in cases where the pharmaceutical in question utilises 'new chemical entities' and where the generation of data involves considerable effort.[96] The provision in these PTAs requires data protection with respect to any new product (with 'new product' being loosely defined as 'one that does not contain a chemical entity that has previously been approved by the Party').[97] The effect of this provision is to allow a first registrant of a new pharmaceutical product to obtain protection even in the case of old and well known products and such protection may be sought irrespective of whether any effort was spent in generating the data.[98]

93 Rahul Rajkumar, 'The Central American Free Trade Agreement: An End Run Around The Doha Declaration on TRIPS and Public Health' (2005) 15(2) *Albany Law Journal of Science & Technology* 433–75, at 465.

94 See, e.g., Article 15.10 of CAFTA–DR–US.

95 These provisions are found in US PTAs with Singapore, Article 16.8.2; Australia, Article 17.10.1(c); Morocco, Article 15.10.1; Bahrain, Article 14.9.1(b); Oman, Article 15.9.1(b); and Korea, Article 18.9.1 (b); and in CAFTA–DR, Article 15.10.1(b).

96 See US PTAs with Australia, Article 17.10.1(d); Morocco, Article 15.10.1; Bahrain, Article 14.9.1(c); Oman, Article 15.9.1(c); and Korea, Article 18.9.1(c); and CAFTA–DR, Article 15.10.1(c).

97 This extends the provision found in Article 4.22, n. 10 of the US–Jordan PTA which restrictively defined 'new chemical entity' as including 'protection for new uses for old chemical entities for a period of three years'.

98 See Frederick M. Abbott, 'The Doha Declaration on the TRIPS Agreement and Public Health and the Contradictory Trend in Bilateral and Regional Trade Agreements', Quaker United Nations Office Occasional Paper 14 (April 2004), at p. 8, at www.quno.org/geneva/pdf/economic/ Occassional/TRIPS-Public-Health-PTAs.pdf.

Finally, as noted above, US PTAs link test data protection to the patent term, meaning generic manufacturers may not obtain marketing approval at any time during the patent period, even when a compulsory licence is issued and even in preparation to enter the market upon expiration of the patent (both of which are allowed under the TRIPS Agreement).[99] A period of data exclusivity increases the final cost of the marketed product as well as possibly delays its entry onto the market.[100] Data exclusivity can also act as a *de facto* patent, ensuring a minimum period of monopoly for pharmaceutical companies, preventing competition and, in some instances, even prohibiting a generic manufacturer from seeking registration in a country. Furthermore, a period of exclusivity relying upon the registration in another country potentially deprives a country of the drug for the entirety of that period. It is also important to note that the period of data exclusivity negotiated in PTAs is independent from the patent process and applies regardless of whether the drug is patented in the country. Thus, the effect of a period of data exclusivity where a patent does not exist serves to maintain an artificial barrier to entry into the marketplace and higher prices to consumers.

As with the linkage of market approval to patent status, a period of data exclusivity could be detrimental to countries taking advantage of a compulsory licence. Again, a manufacturer granted authority to produce a generic drug under compulsory licence must still be registered by the national drug regulatory authority and if the generic manufacturer cannot rely on existing data to gain regulatory approval it cannot respond to the compulsory licence and supply the needed drug. Thus, where a medicine is protected by patent, data exclusivity could effectively render the compulsory licence meaningless if the generic manufacturer cannot make effective use of the licence without repeating time-consuming and costly tests to obtain marketing approval of its drug.[101]

The US has countered this argument by contending that 'if circumstances ever arise in which a drug is produced under a compulsory license, and it is necessary to approve that drug to protect public health or effectively utilize the TRIPS/health solution, the data provision provisions in the PTA would not stand in the way'.[102] Leaving aside for the moment the legal effect of such statements, the meaning from a US standpoint is if a compulsory licence fits within the US view of what is 'necessary', then it would not allow the PTA to stand in the way of the licence. Such a stance removes the ability to protect public health from the signatory country and shifts it to the US.

99 These rules are embodied in US PTAs with Singapore, Article 16.8.4(c); Australia, Article 17.10.4; Morocco, Article 15.10.4; Bahrain, Articles 14.9.4; Oman, Article 15.9.4; and Korea, Article 18.9.5; and in CAFTA–DR, Article 15.10.2.

100 It also must be queried whether requiring duplicate tests promotes the best allocation of resources.

101 Some PTAs limit the use of compulsory licensing to emergency situations. In such circumstances, due to time constraints, it will be impossible to conduct the necessary tests and obtain registration of the drug.

102 Letter from USTR General Counsel John K. Veroneau to Congressman Sander M. Levin, 19 July 2004 (in the context of the US–Morocco PTA).

3. Linkage of patent status and regulatory approval

Several US PTAs introduce provisions which prevent national drug regulatory authorities from granting marketing approval to generic versions of a drug that is under patent in the country without the consent of the patent holder. For instance, Article 16.8.4 of the US–Singapore PTA requires both notification and consent before the regulatory authority can grant marketing approval to a pharmaceutical product under patent. The provision reads:

> With respect to pharmaceutical products that are subject to a patent:
> . . .
> (b) the patent owner shall be notified of the identity of any third party requesting marketing approval effective during the term of the patent; and
> (c) the Party shall not grant marketing approval to any third party prior to the expiration of the patent term, unless by consent or acquiescence of the patent owner.

Similar provisions appear in PTAs with Australia (Article 17.10.5), Oman (Article 15.9.4) and Korea (Article 18.9.5) and in CAFTA–DR (Article 15.10.3).[103] The United States–Morocco Free Trade Agreement contains a similar provision but may go further and limit applications to the regulatory authority during the patent term to those that are consistent with the research and testing exemption (commonly known as a 'Bolar' provision) contained earlier in the PTA.[104] On the other hand, the recent shift in US policy means that US TPAs with Peru, Colombia and Panama do not contain the requirement that the country's regulatory agency withhold approval of a generic drug until it can certify that no patent would be violated if marketing approval were granted for the generic.[105]

The typical provision reproduced above represents a significant shift from traditional operating standards, where the market approval of a drug – that is, the regulatory approval granted to a product which proves its safety and efficacy – has been entirely separate to a drug's patent status. Thus, the patent status of a drug has always been irrelevant to whether a drug is of sufficient quality, safety and efficacy to be marketed in a particular nation or region. The separation of patent status and regulatory approval is due to the fact that the authorities granting patents and those granting regulatory and marketing approval have very different areas of expertise and competency. Authorities assessing and granting patents decide whether the drug at issue is novel and inventive and otherwise meets the criteria for a patent in that country, whereas national drug regulatory authorities simply assess whether the

103 Interestingly, Article 4.23 of the US–Jordan PTA contains the notification language identified above but does not link approval to consent or acquiescence of the patent owner.

104 See Article 15.10.4, n. 15 of the US–Morocco PTA.

105 However, each party must provide procedures and remedies for adjudicating patent infringement or validity disputes which, inter alia, respect due process and offer effective rewards. See Office of the USTR, Statement and *Bipartisan Agreement*, above n. 80.

drug at issue is of sufficient quality, safety and efficacy to be marketed as a potential medical treatment. As a result, national drug regulatory authorities have traditionally not been concerned with the patent status of a drug they are assessing and the potential infringement of a patented drug by the applicant generic manufacturer has never had a bearing on decisions of such authorities.

Therefore, if a patent holder believes that its patent is being infringed, it traditionally has had the responsibility of enforcing its rights. In practice, this entails the patent holder bringing suit against the alleged infringer in an effort to prevent further sales of the infringing product and recover damages. This process can be lengthy and costly, but it ensures the validity of a patent before enforcing the rights asserted by the plaintiff. In addition, IPRs have always been recognised as 'private rights' (the TRIPS Agreement supports this position) and it seems logical that the owner of private rights should be responsible for their enforcement. The newly delegated role of the regulatory authority as an 'enforcer' of a private right is therefore of significant benefit to the rights holder.

Not only will these provisions delay access to generic drugs, the linkage between market approval and patent status could also be detrimental to countries taking advantage of the TRIPS-recognised flexibility of a compulsory licence.[106] More specifically, it is unclear whether a compulsory licence may be issued to provide entry of generic drugs where the law does not allow registration prior to the expiration of the patent. This potential impediment is caused by the fact that a manufacturer granted authority to produce under compulsory licence still must be registered by the national drug regulatory authority. Thus, if the regulatory authority is prohibited from registering generics until the patent expires, the compulsory licence will be prevented from coming to fruition.

4. Limits on compulsory licences

Compulsory licensing is recognised in the TRIPS Agreement as a public health safeguard temporarily allowing a government to override a patent and authorise the production of generic versions of a patented product.[107] Despite the Doha Declaration, which affirmed countries' rights to use compulsory licensing and to determine the circumstances warranting this action,[108] this safeguard is being restricted in numerous US PTAs.

106 It is well established that the introduction of generic drugs results in lower prices. See, e.g., Patented Medicines Price Review Board, Treasury Board of Canada, *A Study of the Prices of the Top Selling Multiple Source Medicines in Canada* (November 2002), at www.pmprb-cepmb.gc.ca/CMFiles/study-e22SHF-8292005-2710.pdf.

107 See further Carlos M. Correa, 'Intellectual Property Rights and the Use of Compulsory Licenses: Options for Developing Countries', Trade-Related Agenda, Development and Equity Working Paper 5, South Centre (1999), at www.southcentre.org/publications/workingpapers/wp05.pdf.

108 The US unsuccessfully negotiated for such provisions in the TRIPS negotiations. See Watal, above n. 89, at p. 320.

The restrictions placed on compulsory licensing are two-fold. First, PTAs indirectly restrict compulsory licensing as a result of the data exclusivity provisions discussed above. Second, direct restrictions limit the grounds on which compulsory licences can be issued. For instance, and unlike in the TRIPS Agreement, these provisions are stated in the negative and confine the use of compulsory licences to specified cases (such as remedying an anti-competitive practice, public non-commercial contexts, national emergencies and other cases of extreme urgency, and the failure to meet working requirements). For example, Article 4.20 of the US–Jordan PTA states:

> Neither Party shall permit the use of the subject matter of a patent without the authorization of the right holder except in the following circumstances:
>
> (a) to remedy a practice determined after judicial or administrative process to be anti-competitive;
> (b) in cases of public non-commercial use or in the case of a national emergency or other circumstances of extreme urgency, provided that such use is limited to use by government entities or legal entities acting under the authority of a government; or
> (c) on the ground of failure to meet working requirements, provided that importation shall constitute working.[109]

Moreover, while the TRIPS Agreement mandates that 'adequate' remuneration be paid to the patent holder, the US–Singapore PTA raises the level of compensation required to 'reasonable and entire' (Article 16.7.6(b)(ii)), terms which are undefined. The PTA also expressly restricts the transfer of 'know how' (Article 16.7.6(b)(iii)), a term not found in the TRIPS Agreement.[110] This latter restriction is important because 'know how' licensing agreements frequently accompany a licensing arrangement and enable the licensee to make efficient use of the patent. Without access to 'know how', the commercial value of access to a patent is often worth much less to a licensee.

It should be noted that the above agreements are not necessarily indicative of the US imposing restrictions on compulsory licensing across its PTAs. In fact, US PTAs with Morocco and Chile, and CAFTA–DR do not contain any language directly relating to compulsory licensing. In addition, Australia and Singapore prior to their PTAs with the US already restricted the use of compulsory licences to cases of emergency or other circumstances of extreme urgency. The draft text of the Free Trade Area of the Americas (FTAA), however, is similar to the US–Singapore PTA, despite the vastly different circumstances of the countries involved.[111] Such a

109 Similar provisions also appear in US PTAs with Singapore, Article 16.7.6; and Australia, Article 17.9.7.

110 See also Article 17.9.7(b)(iii) of the AUSFTA.

111 There are two versions of Subsection B.2e, Article 6.1 of the FTAA concerning compulsory licensing. The less restrictive uses TRIPS Article 31 as a guide. The more restrictive includes the following limits: (1) public, non-commercial use or in cases of national emergency; (2) governmental purchases produced under licence; (3) prohibition of exports of goods produced under a compulsory licence; and (4)

restrictive approach potentially has far more significant public health implications in the context of the FTAA.[112] For instance, the inability to import ingredients or pharmaceutical products in situations other than those stated in the FTAA could undermine the accessibility of generic medicines and other key public health strategies in Latin America.[113]

5. Limitations on 'flexibilities'? Side letters on public health

The above demonstrates that certain requirements imposed on the US's PTA partners pose a threat to public health and welfare by removing the flexibilities granted in the TRIPS Agreement and mandating a more restrictive system of healthcare.[114] The US has asserted, however, that certain side letters to some of its PTAs contain a waiver for public health purposes.

It is certainly true that the side letters in question attempt to reserve the ability of signatories to protect public health. The side letters to US PTAs with Morocco,

requires 'reasonable and entire' compensation. It should also be noted that this is only one example of US PTAs providing similar treatment to countries of vastly differing levels of development. Another area in this regard involves US attempts to restrict and/or prohibit parallel importation of patented products or products produced from patented processes: see, e.g., US PTAs with Morocco, Article 15.9.4; and Australia, Article 17.9.4. However, it should be noted that both PTAs provide that the prohibition may be limited to cases where the patent owner has placed restrictions by contract or other means. Notwithstanding this, the provisions may effectively prohibit parallel importation and essentially allow patent holders, through contract law, to segment markets and maintain price discrimination. The US–Singapore PTA, Article 16.7.2, also restricts parallel importation by allowing patent holders to block parallel importation into either country when the same is done in violation of a distribution agreement anywhere in the world. Interestingly, a number of US PTAs with developing countries, including Chile and Jordan, and CAFTA–DR, are silent on the exhaustion of patent rights; thus, these countries have retained the flexibility granted by TRIPS. On the other hand, the draft text of the FTAA only partially allows for the retention of the TRIPS flexibility, allowing each country to determine its own rules on parallel importation but then obliging them to set up regional exhaustion under their domestic laws within five years. In effect, this would allow parallel importation within the FTAA zone, while keeping the world market segmented.

112 Interestingly, by adopting TRIPS-Plus compulsory licensing provisions in their patent laws, several countries negotiating the FTAA may be adopting more restrictive laws than required in US domestic law. Compulsory licensing is not part of US patent law, but provisions on compulsory licensing are found in other parts of US law such as the Clean Air Act (42 USC §7608) and the Atomic Energy Act (42 USC §2183) and provide a key remedy in the context of anti-trust litigation. Therefore, countries that adopt a restrictive approach to compulsory licensing as part of their patent laws and do not compensate by having licensing access provisions in other parts of their law are offering patent owners stronger rights than exist under US domestic law. See Peter Drahos, 'Expanding Intellectual Property's Empire: The Role of PTAs' (November 2003), at p. 11, at www.grain.org/rights_files/drahos-fta-2003-en.pdf.

113 For strategies to calculate the effect of these provisions, see Musungu and Oh, above n. 92, at p. 65.

114 In addition, the 'net gains analysis' presumes that earnings in agriculture or other sectors due to increased market access translate into ability to afford higher priced medicine; this presumption is questionable: *ibid.*, at p. 55. For other concerns, see Abbott, above n. 98; and Commission on Intellectual Property Rights, *Integrating Intellectual Property Rights and Development Policy*, 3rd edn (London: Commission on Intellectual Property Rights, 2003), at www.iprcommission.org/graphic/documents/final_report.htm.

Bahrain and Oman, and to CAFTA–DR, each contain an extensive and potentially restrictive understanding reached by the parties, which is worth setting out in full:

> The obligations of [the Intellectual Property Chapter] of the Agreement do not affect the ability of either Party to take necessary measures to protect public health by promoting access to medicines for all, in particular concerning cases such as HIV/AIDS, tuberculosis, malaria, and other epidemics as well as circumstances of extreme urgency or national emergency.
>
> In recognition of the commitment to access to medicines that are supplied in accordance with the Decision of the General Council of 30 August 2003 on the Implementation of Paragraph Six of the Doha Declaration on the TRIPS Agreement and Public Health (WT/L/540) and the WTO General Council Chairman's statement accompanying the Decision (JOB(03)/177, WT/GC/M/82) (collectively the 'TRIPS/health solution'), [the Intellectual Property Chapter] does not prevent the effective utilisation of the TRIPS/health solution.
>
> With respect to the aforementioned matters, if an amendment of the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (1994) enters into force with respect to the Parties and a Party's application of a measure in conformity with that amendment violates [the Intellectual Property Chapter] of the Agreement, our Governments shall immediately consult in order to adapt [the Intellectual Property Chapter] as appropriate in the light of the amendment.

The interpretative value of the side letters is, however, questionable as side letters are not part of the actual text and will likely carry little legal weight in a dispute settlement proceeding. Moreover, despite United States Trade Representative (USTR) assertions that 'the United States has no intention of using dispute settlement to challenge any country's actions that are in accordance with that solution',[115] such statements cannot be relied upon and are not binding.

In any event, the information contained in the side letters themselves provide interpretative difficulties, as some disagreement still exists as to what is a 'TRIPS/health solution'. Thus, the US could still pressure partners to submit to its understanding or initiate dispute settlement proceedings for clarification of the understanding. For instance, and importantly, the side letters state that the PTA does not affect 'necessary' measures to protect public health. Such a term is not used in the Doha Declaration and could be used restrictively to limit many health alternatives. Moreover, the side letter with Oman seemingly restricts the ability of either party to issue compulsory licences to protect public health to situations of 'extreme' urgency. Such vague language is part of an unfortunate trend in many negotiating areas, where PTA texts are increasingly dependent upon the

115 Letter from Veroneau, above n. 102.

interpretation of complex and often poorly drafted side letters of understanding. The World Bank recognised potential difficulties with the side letters in stating:

> Notwithstanding the potential flexibilities provided by these side letters, they raise several questions. How widely will the parties to the three agreements define the 'protection of public health' – or, what definitions would an arbitration panel use? Uncertainty, in this respect may become itself a barrier to making use of the flexibilities and may open the door for restrictive interpretations by vested interest. Also, several of the other US PTAs do not contain comparable side letters, raising questions about conflicts between intellectual property obligations and public health objectives in at least some of the affected countries'.[116]

Perhaps as a result of the uncertainty surrounding side letters, the US has recently shifted its position on the issue and has agreed to include the contents of its side letters in the text of its agreements with Peru, Colombia and Panama and, to a lesser extent, Korea.[117] More specifically, the US policy shift calls for an affirmation of the Doha Declaration, a clarification that the agreement does not and should not prevent the parties from taking measures to protect public health or from utilising the TRIPS/health solution, and the inclusion of an exception to the data exclusivity provision for measures to protect public health in accordance with the Doha Declaration and subsequent implementing protocols.

D. Enforcement

The TRIPS Agreement contains detailed provisions relating to enforcement of IP rights, set out in Articles 41 to 61. However, the most noteworthy provision relates to the making available of criminal procedures and penalties for certain conduct. Article 61 requires WTO Members to provide for criminal procedures and penalties in cases of 'wilful trademark counterfeiting or copyright piracy on a commercial scale'. Members are specifically permitted to make such procedures and penalties available in relation to infringements of other IP rights, in particular those committed wilfully or on a commercial scale. The Article also provides that remedies shall include imprisonment and/or fines sufficient to provide a deterrent, consistent with the level of penalties applied for crimes of a corresponding gravity, and may also include the seisure, forfeiture and destruction of infringing goods.

While many PTAs contain a provision obliging parties to provide for enforcement measures in line with the TRIPS Agreement standards,[118] relatively few require parties

116 World Bank, *Global Economic Prospects 2005: Trade Regionalism and Development* (Washington, DC: World Bank, 2004), at p. 110, at www.go.worldbank.org/U051HQ8JZ0.

117 See Office of the USTR, Statement and *Bipartisan Agreement*, above n. 80.

118 This is a feature of PTAs involving the EFTA: see the Convention Establishing EFTA (Vaduz Convention), Annex J, Article 7; and PTAs with Chile, Annex XII, Article 8; Croatia, Annex VII, Article

to go further and impose stronger enforcement measures than those required by TRIPS, particularly in the context of criminal procedures and measures. The major exception here is the US,[119] whose PTAs require parties to implement their TRIPS obligations in specific ways and also impose additional, TRIPS-Plus obligations.

Many US PTAs set forth in detail the sort of conduct that parties must consider to be 'wilful copyright piracy on a commercial scale' and thus made subject to criminal measures. For example, under Article 17.11.26(a) of the AUSFTA such conduct must include:

> (i) significant wilful infringements of copyright, that have no direct or indirect motivation of financial gain; and
> (ii) wilful infringements for the purposes of commercial advantage or financial gain.

Virtually identical provisions are contained in PTAs with Singapore (Article 16.9.21), Morocco (Article 15.11.26(a)), Bahrain (Article 14.10.26), Oman (Article 15.10.26) and Korea (Article 18.10.26), in CAFTA–DR (Article 16.11.26(a)), and in TPAs with Peru (Article 16.11.26), Colombia (Article 16.11.26) and Panama (Article 15.11.26).[120] Such provisions are noteworthy because they require parties to implement their TRIPS obligations so as to require them not only to criminalise conduct that is objectively on a 'commercial scale' but also conduct involving particular commercial 'purposes'. More recently, we can see provisions requiring parties to criminalise copyright piracy irrespective of whether it is on a commercial scale or not. Article 18.10.29 of the KORUS PTA obliges the parties to:

> provide for criminal procedures to be applied against any person who, without authorization of the holder of copyright or related rights in a motion picture or other audiovisual work, knowingly uses or attempts to use an audiovisual recording device to transmit or make a copy of the motion picture or other audiovisual work, or any part thereof, from a performance of the

5; FYROM, Annex V, Article 5; Jordan, Annex VI, Article 5; Korea, Annex XIII, Article 7; Lebanon, Annex V, Article 8; Mexico, Annex XXI, Article 5; Morocco, Annex V, Article 5; Singapore, Annex XII, Article 8; Tunisia, Annex V, Article 8; and Turkey, Annex XII, Article 5. See also Korea–Chile PTA, Article 16.5; and Panama–El Salvador Free Trade Agreement, Articles 17.02–17.03.

119 See, however, Article 140.1 of the Japan–Thailand Economic Partnership Agreement, which states that both parties 'shall provide for criminal procedures and penalties to be applied at least in cases of infringement of patents, utility models, industrial designs, trademarks, copyrights and related rights, layout-designs of integrated circuits and rights relating to new varieties of plants, committed wilfully and on a commercial scale'.

120 Article 4.28 of the US–Jordan PTA defines 'wilful copyright piracy on a commercial scale' only by reference to the conduct in paragraph (i). Article 17.11.22(a) of the US–Chile PTA refers only to the conduct in paragraph (ii) but, unlike any other PTA, further stipulates that such piracy must include 'willful infringing reproduction or distribution, including by electronic means, of copies with a significant aggregate monetary value, calculated based on the legitimate retail value of the infringed goods': for comment, see Roffe, above n. 6, at p. 45.

> motion picture or other audiovisual work in a public motion picture exhibition facility.

This provision thus requires the parties to adopt standards going well beyond those contained in the TRIPS Agreement.

In addition, most PTAs specify that criminal measures must be available for conduct that is related to copyright piracy and trademark counterfeiting. For instance, many PTAs provide that the wilful importation or exportation of pirated copyright goods or trademarked counterfeit products is to be criminalised.[121] More tellingly, some PTAs also cover conduct that may occur in the absence of copyright piracy or trademark counterfeiting. For example, Article 15.11.27 of the US–Morocco PTA requires the criminalisation of the:

> (a) knowing trafficking in counterfeit labels affixed or designed to be affixed to: a phonogram, a copy of a computer program, documentation or packaging for a computer program, or a copy of a motion picture or other audiovisual work; and
> (b) knowing trafficking in counterfeit documentation or packaging for a computer program.

Similar provisions are contained in PTAs with Australia (Article 17.11.28), Bahrain (Article 14.10.28), Oman (Article 15.10.28) and Korea (Article 18.10.27(f)) and TPAs with Peru (Article 16.11.26) and Colombia (Article 16.11.28).

The US regards the enforcement of its nationals' IP rights in foreign countries as a major concern, and has used a variety of tactics to attempt to force such countries to provide stronger and more effective protection against copyright piracy and trademark counterfeiting.[122] The PTA provisions discussed above are a relatively new aspect of its larger strategy to increase enforcement standards at an international level. Clearly, it is hoped that by entering into bilateral agreements with developing countries, not only will levels of IP infringement decrease in those countries, but also that there might be 'flow-on' effects in that such countries might co-operate with their regional neighbours in an attempt to reduce piracy in the broader region.[123] However, it is well recognised that in such countries there may continue to be a discrepancy, for cultural and other reasons, between the strong enforcement measures that exist on the books and the actual levels of, and resources

121 See US PTAs with Australia, Article 17.11.26(b); Morocco, Article 15.11.26(a); Bahrain, Article 14.10.26; Oman, Article 15.10.26; and Korea, Article 18.10.26; CAFTA–DR, Article 16.11.26(a); and TPAs with Peru, Article 16.11.26; Colombia, Article 16.11.26; and Panama, Article 15.11.26.

122 See Executive Office of the President of the United States, *2007 Trade Policy Agenda and 2006 Annual Report of the President of the United States on the Trade Agreements Program* (March 2007), at www.ustr.gov/assets/ Document_Library/Reports_Publications/2007/2007_Trade_ Policy_Agenda/asset_upload_file278_10622.pdf.

123 See Assafa Endeshaw, 'Intellectual Property Enforcement in Asia: A Reality Check' (2005) 13(3) *International Journal of Law and Information Technology* 378–412, at 396–7.

allocated to, enforcement of IPRs. In addition, it has also been doubted that enforcement provisions in US PTAs with developed countries that already have criminal measures and procedures in place will have much meaningful impact at all.[124] Nevertheless, the clear trend is for detailed enforcement provisions to be an integral part of US PTAs and, given the increased level of detail that can be seen in the KORUS PTA, it may well be the case that future US PTAs will be even more specific as to the types of infringing conduct that parties are required to criminalise.

III. Conclusion

While numerous PTAs contain TRIPS-Plus provisions, the US is the main party that has sought higher and stronger standards of IP protection and enforcement in its bilateral agreements. In bypassing the WTO, the US has in its recent PTAs served to entrench amongst a growing number of developed and developing countries (although not its major trading partners) ever-higher minimum standards of IP protection and the removal of certain flexibilities made available under multilateral instruments.[125] This can be seen particularly in the areas of copyright and patents. However, it is important to recognise that despite the close similarities in the form and substance of the IP Chapters of US PTAs and TPAs (at least after the US–Jordan PTA), the provisions of these agreements are not identical to each other, some key differences between the agreements exist and there does not appear to be a trend emerging for ever-increasing standards across all areas of IP. Indeed, given the recent change in control of the US Congress, it may be the case that future PTAs will see a shift in required IP standards, particularly in the area of pharmaceutical patents.

Other major producers and exporters of IP-protected products, such as the EC and Japan, have not to date used bilateral agreements to increase standards of IP protection in the same manner as the US. As has been seen, the EC's approach in particular has been more targeted, focusing largely on securing greater protection for European wine and spirit GIs amongst key trading partners. Nevertheless, it appears from the EC's current negotiations for trade agreements with regional blocs, such as those with the African, Caribbean and Pacific Group of States or with the Andean Community, that it will seek to impose comprehensive obligations on these parties in relation to IP protection and enforcement.[126] These developments will be worth watching closely to see whether the EC joins the US in consistently seeking higher IP standards in its bilateral agreements, and what impact this might have on future multilateral negotiations on IP rights.

124 See Burrell and Weatherall, above n. 30.

125 See Peter Drahos, 'BITs and BIPs: Bilateralism in Intellectual Property' (2001) 4(6) *Journal of World Intellectual Property* 791–808, at 798–9.

126 See Santa-Cruz, above n. 37, at pp. 33–55.

12

Social issues: Labour, environment and human rights

LORAND BARTELS*

I. Introduction

A. *Trade and social issues*

International trade agreements have various effects on the ability of countries to protect their social values, including labour and environmental standards and human rights. At the most general level, trade increases welfare, which can be spent on social protection; indeed, the preamble of the WTO Agreement claims as one of its primary objectives the 'raising [of] standards of living'. As the World Commission on the Social Dimension of Globalisation said in its 2004 report, 'wisely managed, [the global market economy] can deliver unprecedented material progress, generate more productive and better jobs for all, and contribute significantly to reducing world poverty'.[1]

But the 'mutual supportiveness' of trade and social protection is ambiguous at best. At the overall level, structural economic changes as a result of increased trade can enhance employment opportunities for minority groups, but can also do the opposite, and can in addition (and indeed should) also lead to short-term unemployment in inefficient sectors. Increased economic competition, a primary function of trade, should make goods and services more affordable to consumers, but if this undermines public subsidies, it can do precisely the opposite, with detrimental social consequences. With respect to the environment, the economic efficiencies resulting from trade should lead to an efficient use of natural resources, but any increase in economic activity, also a result of trade, can put pressure on the environment. In a very direct sense, trade can increase consumers' access to goods and services useful for achieving non-trade objectives, but also to those that are harmful to social values including national culture, as well as health and safety. At the individual level, trade can enable individuals to enjoy the fruits of their labour, including their intellectual labour, but the restrictions on producing unauthorised goods and services that are inherent in the notion of intellectual property law can

* I am grateful to those who read and commented on this contribution, including the editors, Meredith Kolsky Lewis, Armand de Mestral and Andrew Lang.

1 World Commission on the Social Dimension of Globalization, *A Fair Globalization – Creating Opportunities for All* (Geneva: ILO, 2004), at p. x.

limit a country's ability to meet its social objectives, as the debate on TRIPS and essential medicines has amply demonstrated.

Government efforts to achieve social protection in *other* countries can also impact on trade if they use trade sanctions to achieve this goal. Market access restrictions, whether unilateral or agreed (and this by no means excludes some degree of coercion),[2] are frequently applied to products from countries involved in human rights abuses, from those not complying with environmental treaties, and as an indirect means, via the exclusion of competition, of protecting high domestic standards of social protection (the so-called 'social dumping' issue).[3] The reasons for imposing these restrictions may be moral, more generally political or economically protectionist, or a combination of all three.[4] Trade restrictions with protectionist effects are especially controversial, as the country imposing the restrictions will usually justify its restrictions as a legitimate means of achieving worthy objectives, while the recipient country will see them as merely illegitimate protectionism in another guise.[5]

B. Links between trade and non-trade issues in the WTO

Precisely because of their sensitivity, within the WTO there has barely been a debate on the mutual impacts of trade on social protection, and vice versa. There has, it is true, been some recognition of these linkages in the case of trade and environment, though the degree to which this has been resolved is often exaggerated. It is true that the preamble of the WTO Agreement contains a reference to sustainable development, there is a WTO Committee of Trade and Environment, and WTO Members have little trouble agreeing on the importance of liberalising environmental goods and services.

2 For a discussion of the EU's 'deep trade agenda' in pursuing multilateral agreement on regulatory issues, including social issues, see Alasdair R. Young and John Peterson, 'The EU and the New Trade Politics' (2006) 13(6) *Journal of European Public Policy* 795–814; and Dirk De Bièvre, 'The EU Regulatory Trade Agenda and the Quest for WTO Enforcement' (2006) 13 *Journal of European Public Policy* 851–66.

3 The Preamble of the 1919 Constitution of the International Labour Organisation (ILO) states that 'the failure of any nation to adopt humane conditions of labour is an obstacle in the way of other nations which desire to improve the conditions in their own countries' and efforts to reduce competition by means of low labour standards date back to Daniel Legrand in 1840. See Steve Charnovitz, 'The Labor Dimension of the Emerging Free Trade Area of the Americas', in Philip Alston (ed.), *Labour Rights as Human Rights* (Oxford: Oxford University Press, 2005), at p. 164. The empirical evidence on whether countries with low social standards have an advantage in the competitiveness of their traded goods and services is equivocal: for a survey of the literature, and the conclusion that there is no 'race to the bottom', see Keith Maskus, 'Trade and Competitiveness Aspects of Environmental and Labor Standards in East Asia', in Kathie Krumm and Homi Kharas (eds.), *East Asia Integrates: A Trade and Policy Agenda for Shared Growth* (Washington, DC: World Bank and Oxford University Press, 2004), at pp. 115–34.

4 Steve Charnovitz, 'The International Labour Organization in its Second Century' (2000) 4 *Max Planck Yearbook of United Nations Law* 147–84, at 167, discussing the ILO.

5 See, e.g., Gregory Shaffer, 'The Under-Examined Trade–Environment Linkage: Domestic Politics and WTO Disputes' (2005), available at www.columbia.edu/~ap2231/jbconference/Papers/Shaffer_Bhagwati%20Conference.pdf.

It is also true that the Appellate Body has said that achieving 'sustainable development' is one of the objectives of the WTO itself, basing itself on the questionable argument that 'WTO objectives may well be pursued through measures taken under provisions characterized as exceptions'.[6]

But for all this, virtually no progress has been made on the more difficult aspects of the relationship between trade and social protection, including environmental protection. The 2001 Doha Ministerial Declaration required negotiations on a number of environmental matters,[7] including, at the urging of the European Union (EU), 'the relationship between existing WTO rules and specific trade obligations set out in multilateral environmental agreements',[8] but this mandate has produced nothing of substance.[9] The topic of labour standards has barely been mentioned at the WTO since the 1996 WTO Singapore Ministerial Conference issued a Declaration punting the issue to the ILO,[10] and adding, for good measure, that high labour standards should not be used for protectionist purposes.[11] And while there has been a recent fruitful joint report by the WTO and ILO Secretariats on the links between trade and employment,[12] at the diplomatic level the relationship remains cool. The Singapore Ministerial Conference was marked by the embarrassing withdrawal, at the request of some developing countries, of an unofficial speaking invitation to the Director-General of the ILO,[13] and a decade later, the ILO enjoys neither regular observer status at WTO meetings,[14] nor speaking rights at WTO Ministerial Conferences.[15] At the more general level, despite UN reports on

6 Appellate Body Report, *EC–Tariff Preferences*, para. 94. It is more accurate to say, as the Appellate Body did in an earlier report, that sustainable development is one of the objectives of WTO Members. Appellate Body Report, *US–Shrimp*, para. 154. The WTO Members committed themselves to this objective in the Doha WTO Ministerial Declaration, WT/MIN(01)/DEC/1, 20 November 2001, para. 6.

7 Doha Declaration, paras. 31–3 and 51.

8 Ibid., para. 31(i). On the EU's role in the adoption of this statement see Bart Kerremans, 'What Went Wrong in Cancun? A Principal-Agent View on the EU's Rationale Towards the Doha Development Round' (2004) 9(3) *European Foreign Affairs Review* 363–93, at 378.

9 For a summary, see WTO Committee on Trade and Environment, *Environmental Aspects of the Negotiations – Note by the Secretariat*, WT/CTE/W/243, 27 November 2006.

10 Ironically, this had the effect of boosting that organisation's profile. See Charnovitz, above n. 4, at 158–9 and 163.

11 WTO Singapore Ministerial Declaration, WT/MIN(96)/DEC, 18 December 1996, para. 4. The statement is repeated in the ILO Declaration on Fundamental Principles and Rights at Work, 18 June 1998, (1998) 37 ILM 1233, para. 5. Even the mention of labour standards was too much for India, Pakistan and Sri Lanka, which consented only very reluctantly: see Kevin Kolben, 'The New Politics of Linkage: India's Opposition to the Workers' Rights Clause' (2006) 13 *Indiana Journal of Global Legal Studies* 225–59, at 241.

12 WTO/ILO, *Trade and Employment: Challenges for Policy Research* (Geneva: WTO/ILO, 2007). The Singapore Ministerial Declaration, *ibid.*, para. 4, also promised that 'the WTO and ILO Secretariats will continue their existing collaboration'.

13 Chakravarthi Raghavan, 'EC Labour Standards Move Trashed', *Third World Network*, 8 November 1999, available at www.twnside.org.sg/title/trashed-cn.htm.

14 A list of WTO observers is available at www.wto.org/english/thewto_e/igo_obs_e.htm.

15 The ILO has always been invited to attend WTO Ministerial Conferences.

the potentially negative effect of the WTO on human rights,[16] there has been no systematic attempt in the WTO to consider these issues itself.[17]

Since its founding, then, social issues have been left to one side of the main WTO agenda, much to the relief no doubt of those who were at one stage concerned about its 'contamination' by 'non-trade issues'.[18] And there matters might have remained, but for the sudden increase in the number of regional trade agreements being negotiated since the early 1990s which has generated new opportunities for negotiating links between trade and social protection.

II. Social issues and regional trade agreements

A. Introduction

Express links in regional trade agreements between social protection and trade liberalisation were originally forged by a handful of developed countries (the United States (US), Canada and the European Union (EU)) during the 1990s, but this practice has now been taken up by others, including a limited number of developing countries.[19] On the other hand, the practice is far from universal, even among developed countries. Australia, for example, rejects any such linkage as a matter of principle[20] and, as the following will show, the European Free Trade Association (EFTA) countries and Japan are barely more than lukewarm on the link.

Echoing the practice at the multilateral level, most of the regional trade agreements to consider social protection pretend that there is no conflict between this objective and that of trade liberalisation. Thus, many agreements promise to '[p]romote economic

16 E.g. the following UN ECOSOC documents: *Human Rights and Intellectual Property – Statement by the Committee on Economic Social and Cultural Rights*, E/C.12/2001/15, 14 December 2001; *Globalization and its Impact on the Full Enjoyment of Human Rights – Report of the High Commissioner for Human Rights*, E/CN.4/2002/54, 15 January 2002; *The Impact of the Agreement on Trade-Related Aspects of Intellectual Property Rights on Human Rights – Report of the Commissioner*, E/CN.4/Sub.2/2001/13, 27 June 2001; *Liberalization of Trade in Services and Human Rights – Report of the High Commissioner*, E/CN.4/Sub.2/2002/9, 25 June 2002; *Human Rights, Trade and Investment – Report of the High Commissioner*, E/CN.4/Sub.2/2003/9, 2 July 2003; and *Mainstreaming the Right to Development into International Trade Law and Policy at the World Trade Organization, – Note by the Secretariat*, E/CN.4/Sub.2/2004/17, 9 June 2004.

17 See the discussion on the proposed ILA Declaration on Trade and Human Rights in ILA, *Report of the International Trade Law Committee*, Toronto Conference (2006), at pp. 18–21; also Ernst-Ulrich Petersmann, 'The WTO and Regional Trade Agreements as Competing Fora for Constitutional Reforms: Trade and Human Rights', in Lorand Bartels and Federico Ortino (eds.), *Regional Trade Agreements and the WTO Legal System* (Oxford: Oxford University Press, 2006), Chapter 12.

18 See the statement signed by 103 intellectuals in 'Third World Intellectuals and NGOs' Statement Against Linkage (TWIN-SAL)', CUTS International, 15 November 1999, available at www.cuts-international.org/Twin-sal.htm.

19 This chapter does not discuss the role of social issues in integrated 'communities' including those at a nascent stage, such as ASEAN.

20 Australian Parliament, Joint Standing Committee on Treaties, Report 63: Treaties tabled on 7 December 2004, Chapter 3 (Australia–Thailand), para. 3.160. Australia's agreement with the US is an obvious exception, and clearly a product of US negotiating objectives.

development in a manner consistent with environmental protection and conservation and with sustainable development'[21] or even to promote sustainable development directly,[22] while in others the parties reaffirm their commitments to various values (such as human rights or labour standards) without explaining what these commitments have to do with the core business of the agreement.[23]

In contrast, there are examples of agreements which respond to the fact that trade and social protection are not always *ad idem*. Some agreements seek to improve on the policy space allowed to WTO Members under the WTO Agreements by modifying the general exceptions clauses, or by subordinating the agreement as a whole to other international agreements with social policy objectives. Others focus directly on the ways in which social protection can be raised or lowered for the illegitimate purposes of influencing trade, for example by way of clauses discouraging the parties from reducing social protections in order to gain trade (or investment) advantages, or, alternatively, discouraging them from using high social standards for protectionist purposes. And still other agreements set positive social standards in the territories of the respective parties to the agreement. These are sometimes linked to trade, as in the North American Free Trade Agreement (NAFTA) model, or not, as in the model of the EU human rights clause, and occasionally, as in both of these cases, they use the threat of trade sanctions as an enforcement mechanism.

The following will analyse the main techniques for ensuring social protection that have so far been manifested in regional trade agreements. These can be divided into two main categories: provisions seeking to safeguard a right to regulate for social purposes, and provisions seeking to set positive social standards among the parties to the agreement.[24] For the sake of brevity, this chapter focuses on the basic obligations concerning trade in goods, leaving aside for the most part obligations relating to technical barriers to trade, sanitary and phytosanitary standards, services and intellectual property.

B. Rights to regulate

With one notable recent exception,[25] all regional trade agreements include a general exceptions clause similar to Article XX of the GATT 1994, which sets out a list of mainly public policy reasons which (subject to certain conditions) entitle the parties to

21 See, e.g., the Preamble to the Chile–Costa Rica Free Trade Agreement. This phrase is drawn from the Preamble of the WTO Agreement.

22 Preambles to CARICOM–Costa Rica Free Trade Agreement, EFTA–Mexico Free Trade Agreement and China–Pakistan FTA.

23 This is common in the preambles of many regional trade agreements concluded by the Balkan countries.

24 See also Marie-Claire Cordonier Segger, 'Sustainable Development in Regional Trade Agreements', in Bartels and Ortino, above n. 17, Chapter 13; and Petersmann, above n. 17.

25 The 2006 China–Pakistan FTA contains no general or security exceptions. See big5.mofcom.gov.cn/gate/big5/english.mofcom.gov.cn/accessory/200611/1164848706093.doc. However, Article 3 is a conflicts clause in which the parties 'affirm their existing rights and obligations with respect to each other under

ignore the remaining obligations in the agreement. One way that parties to regional trade agreements have enhanced their rights to regulate for public policy reasons has been by increasing the scope of these clauses. But countries have also sought to gain regulatory space by including conflicts clauses in their agreements giving priority to rights or obligations under other international agreements between the parties in cases of conflict. Such clauses often make reference to the WTO agreements (including their exceptions) but they also often refer, usually by implication but sometimes expressly, to other agreements between the parties with a more direct purpose of social protection, such as ILO Conventions, or environmental or human rights treaties.

An additional point concerns the effect of any such carve-outs under WTO law. Article XXIV of the GATT requires the parties to a regional trade agreement to eliminate 'duties and other restrictive regulations of commerce' with respect to 'substantially all the trade' in products originating in their territories 'except, where necessary, those permitted under ... Article XX'.[26] This raises the question of the WTO legality of provisions in regional trade agreements that are more generous than Article XX, as well as the question, more likely to arise in practice, of the WTO legality of measures taken under those provisions. The simple answer would be that under the WTO, a measure not covered by a relevant WTO exception is simply not permitted. Indeed, in the WTO case *Canada–Periodicals*,[27] Canada failed to mention the NAFTA 'cultural industries' exception, even though this was undoubtedly relevant to the subject matter of the dispute. On the other hand, it is possible that the WTO dispute settlement system can take account of such law 'applicable between the parties',[28] and therefore it is not entirely certain that Canada should have given up on this possibility. In any case, it is likely that a future defendant in WTO dispute

the WTO Agreement and other agreements to which both Parties are parties'. On the effect of such clauses see below at n. 57 and accompanying text.

26 Article XXIV:8(a)(i) of the GATT for customs unions and Article XXIV:8(b) of the GATT for free-trade areas. Two additional points: first, it is difficult to see the lexical relevance of the apparent condition 'where necessary' in these paragraphs; second, the security exception in Article XXI of the GATT, which is not included in the list of permitted exceptions in Article XXIV, also overrides Article XXIV by its own terms. This reduces the value of the argument that the treaty drafters cannot have intended to prohibit parties from taking security measures under regional trade agreements, and therefore that the list in Article XXIV is not exclusive. This argument is usually made in support of the legality of other non-listed trade restrictions under regional trade agreements, in particular trade remedies. On the other hand, this does not explain the inclusion of Article XX in the list.

27 Appellate Body Report, *Canada–Periodicals*.

28 For a general discussion of these themes, see Joost Pauwelyn, *Conflict of Norms in Public International Law: WTO Law Relates to Other Rules of International Law* (Cambridge: Cambridge University Press, 2003). Recent jurisprudence is more conservative, though not entirely on point. In Appellate Body Report, *Mexico–Taxes on Soft Drinks*, the defendant claimed that its measure was justified as a counter-measure in response to an illegal act by the complainant under another agreement (NAFTA). The Appellate Body refused to consider this argument on the basis that this would amount to 'adjudicat[ing] non-WTO disputes' (para. 56). For criticism of this reasoning, see comments by this author at www.worldtradelaw.typepad.com/ielpblog/2006/03/ soda_pop.html# comments. See also Chapter 6 by Andrew Mitchell and Tania Voon.

settlement proceedings will invoke a clause in a regional trade agreement between the same parties as a defence to the WTO claim.

1. Exceptions

When it comes to the social exceptions to their core trade obligations, many regional trade agreements simply adopt the list of general exceptions found in Article XX of the GATT, sometimes even incorporating this provision by reference.[29] However, a number of countries have modified these clauses to provide greater policy space, and they have done this in three main areas: environment, culture and indigenous rights. By contrast, and no doubt reflecting the greater sensitivity of these issues, there has been no attempt to meddle with the application of these clauses to measures designed to protect labour and human rights.

2. Environment

A first class of modifications to the WTO exceptions concerns Article XX of the GATT, which, subject to non-discrimination conditions in the chapeau, permits measures (b) 'necessary to protect human, animal or plant life or health' and (g) 'relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption'. The word 'environment' does not appear, for the obvious reason that the concept of environmental protection did not exist in 1947, when these words were drafted.

In 1993, the NAFTA became the first regional trade agreement to modify these clauses expressly. This agreement incorporates Article XX of the GATT by reference, but then adds the following comment:

> The Parties understand that the measures referred to in GATT Article XX(b) include environmental measures necessary to protect human, animal or plant life or health, and that GATT Article XX(g) applies to measures relating to the conservation of living and non-living exhaustible natural resources.[30]

29 E.g. Singapore–Australia Free Trade Agreement, Article 12 (reiterating GATT Article XX); Thailand–Australia Free Trade Agreement, Article 1601 (incorporating by reference); Australia–United States Free Trade Agreement (AUSFTA), Article 22.1 (incorporating by reference with some modifications, as discussed below); New Zealand–Thailand Closer Economic Partnership Agreement (NZ–Thailand CEPA), Article 15.1 (reiterating GATT Article XX); Trans-Pacific Strategic Economic Partnership (Trans-Pacific SEP), Article 11.22(2) (reiterating with some modifications, as discussed below); Mexico–Chile Free Trade Agreement, Article 19.02; Mexico–Uruguay Free Trade Agreement, Article 19.02; Japan–Mexico Economic Partnership Agreement (Japan–Mexico EPA), Article 168.1 (all incorporating by reference); Mexico–Costa Rica Free Trade Agreement, Article 9.16 (reiterating); Japan–Singapore Economic Partnership Agreement (Japan–Singapore EPA), Article 19.2(2); Japan–Malaysia Economic Partnership FTA, Article 10; Japan–Philippines Economic Partnership Agreement (Japan–Philippines EPA), Article 23 (all incorporating by reference); Chile–China Free Trade Agreement, Article 99; Chile–Costa Rica FTA, Article 20.02; Korea–Chile, Article 20.01 (all incorporating by reference); China–Macao Closer Economic Partnership Agreement (China–Macao CEPA), Article 18; and China–Hong Kong Closer Economic Partnership Agreement (China–Hong Kong CEPA), Article 18 (both incorporating by reference).

30 NAFTA, Article 2101.

This wording has been adopted in subsequent agreements by the NAFTA parties[31] as well as by New Zealand in its recent trade agreements[32] – despite the fact that arguably this additional wording achieves nothing. The qualification of the exception to include 'environmental measures' does not increase its scope (the measure must still meet the other criteria), and the clarification that the term 'exhaustible natural resources' includes living resources must be considered redundant since the WTO Appellate Body decided precisely this point almost a decade ago in *US–Shrimp*.[33]

Another model clause, taken from Article 30 of the EC Treaty, states as follows:

> The Agreement shall not preclude prohibitions or restrictions on imports, exports, goods in transit or trade in used goods justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archaeological value; or the protection of intellectual, industrial and commercial property or rules relating to gold and silver. Such prohibitions or restrictions shall not, however, constitute a means of arbitrary or unjustifiable discrimination where the same conditions prevail or a disguised restriction on trade between the Parties.

This provision is found in all of the regional trade agreements concluded by the EU except for those with Chile and Mexico, which incorporate by reference Article XX of the GATT. It is also adopted by the EFTA regional trade agreements,[34] other than those with Chile, Mexico, Singapore and SACU, and by a number of agreements concluded by Balkan countries (in almost all cases with the addition of a reference to measures 'justified on grounds of ... protection of the environment').[35]

Needless to say, the European Court of Justice (ECJ) has produced a rich jurisprudence on the interpretation of Article 30 of the EC Treaty, which implies a 'strict' proportionality test involving a balancing of the benefits of the measure against the resulting detriment to trade. This is a more intrusive test than under WTO law, which never second guesses the level of protection which a measure is intended to achieve.[36] Where the ECJ has exercised jurisdiction over such clauses in the EU's regional trade agreements, it has interpreted this wording in the same way

31 AUSFTA, Article 22.1; Central America–Dominican Republic–United States Free Trade Agreement (CAFTA–DR–US), Article 21.1; Canada–Chile Free Trade Agreement, Article O–01; Canada–Israel Free Trade Agreement, Article 10.1; Mexico–Israel Free Trade Agreement, Article 11.02; United States–Jordan Free Trade Agreement, Article 12; United States–Morocco Free Trade Agreement, Article 21.1 and side letter; and United States–Singapore Free Trade Agreement, Article 21.1.

32 Trans-Pacific SEP, Article 19.1(2). 33 Appellate Body Report, *US–Shrimp*, para. 131.

34 E.g. EFTA–Croatia Free Trade Agreement, Article 17.

35 E.g. Croatia–Albania Free Trade Agreement, Article 23.

36 For a comparison see Jan Neumann and Elisabeth Türk, 'Necessity Revisited: Proportionality in World Trade Organization Law After *Korea–Beef*, *EC–Asbestos* and *EC–Sardines*' (2003) 37(1) *Journal of World Trade* 199–233.

as under Community law,[37] but it is an open question whether other tribunals would also apply the stricter ECJ test.

Other agreements have amended the exceptions available for measures designed to achieve social protection in ways that are not easy to follow. Australia's 1983 agreement with New Zealand abandons the GATT requirement that a measure to conserve exhaustible natural resources be taken in conjunction with domestic restrictions,[38] while India's agreements with Sri Lanka and Nepal[39] and the many agreements concluded by countries of the former Soviet Union (now the Commonwealth of Independent States or CIS) omit any reference to such an exception at all.[40] Perhaps the ANZCERTA provision truly is the product of a negotiation process, but one wonders whether the other countries wished to abandon their rights to conserve their exhaustible natural resources. There are also several examples of *ad hoc* exceptions clauses. For example, the Egypt–Jordan FTA, allows measures 'for religious, hygienic, security or environmental reasons' so long as they are 'in conformity with the applicable laws and regulations in both countries',[41] which is not much of a condition. As mentioned, the China–Pakistan FTA is remarkable for not containing *any* exceptions clauses.

3. Culture

A second modification concerns the GATT exceptions available for the protection of cultural heritage. Article XX(f) of the GATT permits measures 'imposed for the protection of national treasures of artistic, historic or archaeological value', but this does not protect domestic content not rising to the level of a 'national treasure'. To remedy this perceived deficiency, beginning with its 1988 agreement with the US, Canada has sought in all of its regional trade agreements to protect 'cultural industries', defined in terms of persons engaged in the production, distribution or exhibition of print, audio and audio-visual materials.[42] Such a clause has not been adopted by other countries, with the exception of New Zealand, which has an exception in its agreements with Thailand and the Transpacific countries for measures to support 'creative arts of national value'.[43]

37 Case C-340/97, *Nazli* [2000] ECR I-957, paras. 55–6.

38 Australia–New Zealand Closer Economic Relations Trade Agreement (ANZCERTA), Article 18.

39 India–Nepal Free Trade Agreement, Article IX; and India–Sri Lanka Free Trade Agreement, Article IV (which adopts a subjective test for measures 'which [the party] considers necessary for . . . the protection of human, animal or plant life and health').

40 E.g. Georgia–Armenia Free Trade Agreement, Article 10.

41 Egypt–Jordan FTA, Article 8. 42 Canada–Chile FTA, Article O-07.

43 NZ–Thailand CEPA, Article 15.1(f); and Trans-Pacific SEP, Article 19.1(3). Footnote 1 of the latter agreement defines this term to include 'the performing arts – including theatre, dance and music – visual arts and craft, literature, film and video, language arts, creative on-line content, indigenous traditional practice and contemporary cultural expression, and digital interactive media and hybrid art work, including those that use new technologies to transcend discrete art form divisions. The term encompasses

4. Indigenous rights

New Zealand is also responsible for a general exceptions clause in its Thailand and Transpacific agreements allowing affirmative action measures to support its indigenous population. These clauses state that:

> Provided that such measures are not used as a means of arbitrary or unjustified discrimination against persons of the other Parties or as a disguised restriction on trade in goods and services, nothing in this Agreement shall preclude the adoption by New Zealand of measures it deems necessary to accord more favourable treatment to Maori in respect of matters covered by this Agreement including in fulfilment of its obligations under the Treaty of Waitangi.[44]

Other regional trade agreements also make allowance for positive discrimination, but in the more limited contexts of cross-border services, investment and government procurement. Thus, in respect of cross-border services and investment Canada reserves 'the right to adopt or maintain any measure denying investors of another Party and their investments, or service providers of another Party, any rights or preferences provided to aboriginal peoples'.[45] Australia's agreements are similar, but also include exemptions in the area of government procurement.[46] Some, though apparently not all, of the US agreements contain exemptions in the areas of services and investment for 'small and minority businesses'.[47]

5. Modifications to the 'chapeau' conditions

In a number of agreements, the parties to regional trade agreements have also relaxed the strict conditions set out in the chapeau to Article XX of the GATT that measures not amount to unjustifiable discrimination, arbitrary discrimination or disguised restriction on international trade.

One very common variation, found in most of the regional trade agreements concluded by the EU,[48] the EFTA countries and other associated European

those activities involved in the presentation, execution and interpretation of the arts; and the study and technical development of these art forms and activities'.

44 NZ–Thailand CEPA, Article 15.8; and Trans-Pacific SEP, Article 19.5.

45 NAFTA, Annex II; and Canada–Chile FTA, Annex II (both on cross-border services and investment). The Canada–Costa Rica Free Trade Agreement does not contain significant obligations in services and investment.

46 AUSFTA, Annex II (investment and services) and Annex 15A, Section 7, General Notes (government procurement); Singapore–Australia FTA, Chapter 6, Article 15 (government procurement) and Annex 4-II(A) (investment and services); Thailand–Australia FTA, Annex on Australian commitments on services and investment (this agreement contains no substantive obligations on government procurement).

47 E.g. AUSFTA, Annex II (investment and services).

48 European Union–South Africa Trade, Development and Cooperation Agreement (EU–SA TDCA), Article 27, is unusual in that it replicates the three chapeau conditions, despite the fact that it is otherwise on the model of Article 30 of the EC Treaty.

countries, follows Article 30 of the EC Treaty in not making express reference to the first condition that a measure not amount to unjustifiable discrimination. This probably changes little, if anything, as the change can be explained on the basis that, according to these clauses, the measures must be 'justified' on the grounds specified therein, and therefore, like the chapeau, measures amounting to unjustified discrimination still remain unprotected.[49]

More significant perhaps are agreements omitting (or almost omitting) any chapeau-type conditions, such as the CARICOM–Dominican Republic Free Trade Agreement (CARICOM–DR FTA). But worthy of particular mention is the formulation found in the many regional trade agreements concluded by the CIS countries, allowing for:

> measures generally accepted in the international practice which are considered by the Contracting Party necessary for the protection of its vital interests or which are undoubtedly necessary for the implementation of international agreements of which [the party] is a signatory or intends to become a signatory if these measures concern ... health protection of people, animals and plants.[50]

Doing away with the traditional non-discrimination conditions, this provision adds two alternatives. One is that, in the opinion of the relevant party, the measure is necessary for the protection of its 'vital interests', a test which, despite its subjectivity, is set rather high for a measure designed, for example, to protect a minor species of animal. A subset of the CIS agreements (some of the Kyrgyzstan and Georgia agreements)[51] add that such measures must also be 'general[ly] accepted in the international practice', though it is not entirely clear what this might mean. Second, measures are permitted if they are 'undoubtedly necessary' for the implementation of an international agreement. This test is, as the next section will demonstrate, unusual more for being placed in an exceptions clause than for its content.

6. Conflicts with other international agreements

Many regional trade agreements have made use of conflicts clauses to protect rights and/or obligations under other international agreements with social objectives. Such

49 Admittedly, the Appellate Body in *US–Shrimp* stated that '[t]he policy goal of a measure at issue cannot provide its rationale or justification under the standards of the chapeau of Article XX' but this makes no sense, otherwise there is no way to assess the possibility of 'justifiable discrimination'. For this point, see Sanford Gaines, 'The WTO's Reading of the GATT Article XX Chapeau: A Disguised Restriction on Environmental Measures' (2001) 22(4) *University of Pennsylvania Journal of International Economic Law* 739–862, at 778.

50 Kyrgyzstan–Moldova Free Trade Agreement, Article 11. On these agreements generally, see Rilka Dragneva and Joop de Kort, 'The Legal Regime for Free Trade in the Commonwealth of Independent States' (2007) 56(2) *The International and Comparative Law Quarterly* 233–66.

51 E.g. Kyrgyzstan–Moldova FTA, Article 11.

conflicts clauses have effect under Article 30(2) of the Vienna Convention on the Law of Treaties[52] ('Vienna Convention'), which provides that '[w]hen a treaty specifies that it is subject to, or that it is not to be considered as incompatible with, an earlier or later treaty, the provisions of that other treaty prevail'.[53]

There is a well known example of such a conflicts clause in NAFTA, which states that certain environmental treaties[54] are to take priority in the event of any inconsistency, 'provided that where a Party has a choice among equally effective and reasonably available means of complying with such obligations, the Party chooses the alternative that is the least inconsistent with the other provisions of this Agreement'.[55] The US abandoned this clause in subsequent regional trade agreements,[56] but it survived in the practice of the two other NAFTA parties, being adopted in Canada's agreements with Chile and Costa Rica and Mexico's agreement with Chile. Chile evidently found this clause to its liking, taking it up in its agreement with Costa Rica, and it has recently surfaced in an agreement between Panama and Taiwan.[57]

There are also examples of more wide-ranging conflicts clauses, such as this clause in the EFTA–Singapore FTA:

> The provisions of this Agreement shall be without prejudice to the rights and obligations of the Parties under the [WTO Agreement] and any other international agreement to which they are a party.[58]

52 Done at Vienna 23 May 1969, in force 27 January 1980, 1155 UNTS 331; (1969) 8 ILM 679, UKTS (1980) 58.

53 See the International Law Commission Commentary on (then) Article 26(2) of the draft Vienna Convention on the Law of Treaties, in ILC, *Report of the International Law Commission on the work of the second part of its seventeenth session*, Document A/6309/Rev.l, (1966) II *Yearbook of the International Law Commission* 214–6.

54 Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES), done at Washington, DC, 3 March 1973, in force 1 July 1975; the Montreal Protocol on Substances That Deplete the Ozone Layer ('Montreal Protocol'), done at Montreal 16 September 1987, in force 1 January 1989; the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal ('Basel Convention'), done at Basel 22 March 1989, in force 5 May 1992; and two bilateral environmental agreements.

55 NAFTA, Article 104. The clause was very briefly considered in *S.D. Myers, Inc.* v. *Government of Canada*, NAFTA Arbitration under the UNCITRAL Arbitration Rules (Partial Award of 13 November 2000), para. 215, available at www.state.gov/s/l/c3746.htm.

56 The 2001 US–Jordan FTA contained nothing on point, and the later agreements contain statements on 'the mutual supportiveness' of environmental and trade agreements and promise to consult on this matter within the WTO: AUSFTA, Article 19.8; CAFTA–DR–US, Article 17.2; US–Morocco FTA, Article 17.8; US–Singapore FTA, Article 18.8; and United States–Colombia Trade Promotion Agreement (US–Colombia TPA), Article 18.12.

57 Canada–Chile FTA, Article A-04; Canada–Costa Rica FTA, Article I.3; Mexico–Chile FTA, Article 1-06; and Panama–Taiwan Free Trade Agreement, Article 1.03.

58 EFTA–Singapore FTA, Article 4. See also Korea–Chile FTA, Article 1.3; Trans-Pacific SEP, Article 18.2; China–Pakistan FTA, Article 3; China–Hong Kong CEPA, Article 20.1; China–Macao CEPA, Article 20.1; cf. EFTA–South African Customs Union Free Trade Agreement (EFTA–SACU FTA), Article 4.2 (which covers only 'obligations').

In addition, there are instances of a more targeted use of this formulation. Thus, in the Thailand–Australia Free Trade Agreement the parties 'affirm with respect to each other their existing rights and obligations relating to technical regulations' not only under the TBT Agreement but also under 'all other international agreements, including environmental and conservation agreements, to which the Parties are party'.[59]

Also worth noting are a number of ambiguous conflicts provisions, as in the China–Pakistan agreement mentioned above, in which the parties 'confirm' (or 'affirm') their rights and obligations under other agreements.[60] It is not entirely clear whether this means that the treaty 'is not to be considered as incompatible' with the other agreements, as required by Article 30(2) of the Vienna Convention; an alternative reading would be that the provision amounts to an unenforceable political statement of the 'mutual supportiveness' of the different regimes. In the same way, the parties frequently reiterate commitments under other regimes, for instance human rights regimes, but this does not necessarily mean that those regimes prevail in cases of conflict. The preambular recitals found in many EFTA (and now Balkan) agreements that 'no provision of this Agreement may be interpreted as exempting the Contracting Parties from their obligations under other international agreements' are of similarly ambiguous legal effect.[61] Here the language is clearer, though there are limits to how far mere 'interpretation' can avoid a conflict,[62] but the fact that the language is located in a preamble weakens the binding force of the statement.

C. Positive regulation of social issues

Provisions in regional trade agreements allowing the parties free scope to take protective measures go part of the way to resolving any problems between trade and social protection. However, some countries have decided on a more complete solution, which is to use regional trade agreements as a platform for the positive regulation of social protection in the territory of the other country. For convenience these are categorised here according to the countries which have adopted these clauses, though thematically they fall into two main groups: clauses which establish standards, sometimes enforceable, and clauses providing for co-operation on social matters.

59 Thailand–Australia FTA, Article 703(1).

60 China–Pakistan FTA, Article 3; EFTA–Chile Free Trade Agreement, Article 4; EFTA–Tunisia Free Trade Agreement, Article 42.4; and also Chile–China FTA, Article 3; and Singapore–Jordan Free Trade Agreement, Article 1.1(2).

61 The recital originates in the agreements between the EC and the four EFTA countries (Switzerland, Norway, Iceland and Liechtenstein) in 1972.

62 See Pauwelyn, above n. 28.

1. The North American model

NAFTA was groundbreaking in linking (via two side agreements) the regulation of social matters to trade obligations. These side agreements impose substantive social obligations on the parties: they require the parties to enforce their domestic environmental and labour legislation[63] (subject to a responsible exercise of discretion and a bona fide decision to allocate resources to other relevant matters);[64] and they require that each party 'shall ensure' that its legislation provides for high levels of environmental protection and labour standards respectively, and 'shall strive' continually to improve those regulations.[65] There is an emphasis on public participation: the parties are obliged to publicise their laws, and must provide for private party enforcement of these laws before impartial tribunals.[66]

Two types of enforcement are foreseen: the possibility of submissions by NGOs or other persons claiming that a party is not effectively enforcing its domestic laws ('citizen submissions') and a mechanism of inter-state enforcement. Under the environment side agreement, a citizen submission is lodged with the secretariat of the body administering the agreement (the Commission for Environmental Co-operation), and may lead to that body preparing a factual record of the issue;[67] under the labour agreement the submissions are lodged with the relevant party itself, which is under no obligation to take the matter any further.[68] There have been over 50 citizen submissions under the environment agreement, and slightly fewer under the labour agreement.[69]

The modes of inter-state enforcement vary according to the obligations at issue,[70] and have not yet been used. Simplifying somewhat, consultations are available for any matter under these agreements, while formal dispute settlement is only available in cases of a failure to enforce labour and environmental legislation

63 North American Agreement on Environmental Co-operation (NAAEC), Article 3; and North American Agreement on Labor Co-operation (NAALC), Article 4. Note that 'environmental law' excludes legislation with the primary purpose of managing commercial or aboriginal harvesting of natural resources: NAALC, Article 45(2)(b).

64 NAAEC, Article 45(1); and NAALC, Article 49(1).

65 In NAALC Annex 1, the labour agreement lists eleven guiding 'labour principles' on matters ranging from freedom of association to protection of migrant workers, though it is expressly stated that these principles do not represent minimum legal standards. These principles are: (i) freedom of association and protection of the right to organise; (ii) the right to bargain collectively; (iii) the right to strike; (iv) prohibition of forced labour; (v) labour protection for children and young persons; (vi) minimum employment standards, such as minimum wages and overtime pay, covering wage earners, including those not covered by collective agreements; (vii) elimination of employment discrimination on the basis of such grounds as race, religion, age, sex, or other grounds as determined by each party's domestic laws; (viii) equal pay for men and women; (ix) prevention of occupational injuries and illnesses; (x) compensation in cases of occupational injuries and illnesses; and (xi) protection of migrant workers.

66 NAAEC, Articles 4 and 6–7; and NAALC, Articles 4–7. 67 NAAEC, Articles 14 and 15.

68 NAALC, Article 16(3).

69 See the lists at www.cec.org/citizen/index. cfm?varlan=english and http://www.dol.gov/ilab/programs/nao/ status.htm respectively.

70 NAAEC, Parts 4 and 5; and NAALC, Parts 4 and 5.

in a manner that is trade-related, and when that failure represents a 'persistent pattern' of behaviour. In both cases, there is the possibility of arbitral panels with the power to award a monetary penalty, collected if necessary by suspending trade concessions, though the labour side agreements limit this remedy in cases involving occupational safety and health, child labour or minimum wage standards.[71] The monetary penalty is to be spent respectively on labour or environmental law enforcement (environmental improvements) in the territory of the party in default.[72]

The side agreements also set out elaborate institutional frameworks for co-operation in their respective fields. They each establish a commission, supported by a permanent secretariat, with a mandate for active promotion of co-operation on a variety of environment and labour-related topics (and, as mentioned, a role with respect to citizen submissions under the environment agreement). In terms of co-operation, the function of the commission under the labour agreement is informative in nature, while the commission under the environment agreement also has the power to make normative recommendations on matters such as public access to environmental information or appropriate pollutant limits,[73] as well as environmental impact assessments and follow-up.[74]

2. Canada

The first NAFTA party to conclude regional trade agreements after the NAFTA was Canada, which concluded agreements in 1996 with Israel and Chile and another in 2001 with Costa Rica. Its agreement with Israel contained no particular reference to social issues, but its agreement with Chile was accompanied by labour and environment side agreements very much on the NAFTA model. Its agreement with Costa Rica contains equivalent obligations, including a system of citizen submissions,[75] but has a reduced system of inter-state enforcement. Enforcement under the labour agreement is limited to 'reasonable and appropriate measures, exclusive of fines or any measure affecting trade, but including the modification of cooperative activities [. . .] to encourage the other Party to remedy that persistent pattern',[76] while the environment agreement replaces enforcement with a system of implementation by 'government to government coordination'.[77] The environment agreement also adds in its preamble that 'it is inappropriate to relax environmental laws in order to encourage trade'.

71 Canada is not subject to trade sanctions, and has arranged that any fines will be enforced domestically by Canadian courts: NAAEC, Annex 36A; and NAALC, Annex 41A.

72 NAAEC, Annex 34(3); and NAALC, Annex 39(3). 73 *Ibid.*, Article 10(5)(a) and (b).

74 *Ibid.*, para. 7.

75 Canada–Costa Rica Agreement on Environmental Co-operation (CCRAEC), Article 9; and Canada–Costa Rica Agreement on Labour Co-operation (CCRALC), Article 11.

76 CCRALC, Article 23(5). 77 CCRAEC, Article 7(1).

3. United States

Because of the absence of 'fast track' negotiating authority between 1994 and 2002, the US was only able to negotiate one regional trade agreement during this period, namely with Jordan in 2001. This agreement is often considered to represent the high-water mark of the US regulation of social protection in its regional trade agreements,[78] though, as the following will show in more detail, it is difficult to see why. In brief, its obligations are weaker than in NAFTA, there is no longer any obligation to provide for private party enforcement rights, and the parties have agreed not to use those enforcement mechanisms which are at least nominally available to them on the face of the agreement. On the first of these three points the subsequent agreements are similar, and on the remainder they are actually stronger.

The main obligation (now part of the body of the agreement) in the United States–Jordan FTA is that the parties must 'not fail to effectively enforce' domestic environmental and labour legislation in a manner affecting trade,[79] which matches the narrowest (and only enforceable) tier of the NAFTA obligations. The standard of protection for both labour and the environment is also effectively weakened. As far as labour is concerned, the parties 'reaffirm their obligations' as ILO members and their 'commitments under the ILO Declaration on Fundamental Principles and Rights at Work and its Follow-up'[80] but their obligation to 'ensure' a high standard of protection reflecting these norms[81] is reduced to an obligation to 'strive to ensure' this standard of protection.[82] Similarly, they are only obliged to 'strive to ensure' that their laws provide for high standards of environmental protection.[83]

In terms of inter-state co-operation and enforcement there are also some changes. No co-operation is foreseen for environmental matters, except insofar as this might be within the competence of the Joint Committee established to implement the agreement. By contrast, the parties 'recognize that cooperation between them

78 For a glowing report, see Roman Grynberg and Veniana Qalo, 'Labour Standards in US and EU Preferential Trading Arrangements' (2006) 40(4) *Journal of World Trade* 619–53; for a more sceptical view, see Philip Alston, '"Core Labour Standards" and the Transformation of the International Labour Rights Regime' (2004) 15 (3) *European Journal of International Law* 457–521.

79 US–Jordan FTA, Articles 5(3) and 6(4).

80 US–Jordan FTA, Article 6(1). Philip Alston has sparked a debate on whether the ILO Declaration (and the use of this Declaration in US regional trade agreements) threatens the ILO regime. See Alston, above n. 78, and responses: Brian Langille, 'Core Labour Rights – The True Story (Reply to Alston)' (2005) 16(3) *European Journal of International Law* 409–37; Francis Maupain, 'Revitalization not Retreat: The Real Potential of the 1998 ILO Declaration for the Universal Protection of Workers' Rights' (2005) 16(3) *European Journal of International Law* 439–65; and Philip Alston, 'Facing Up to the Complexities of the ILO's Core Labour Standards Agenda' (2005) 16(3) *European Journal of International Law* 467–80.

81 US–Jordan FTA, Article 6(6) contains a list of 'internationally recognized labor rights', which nonetheless fails to include the ILO 'core labour standard' of non-discrimination, and includes an additional standard requiring minimum wages.

82 US–Jordan FTA, Articles 6(1) and 6(3). Certainly it is not true to say that 'Article 6(1) requires parties to enact domestic legislation to provide for a minimum wage': see Grynberg and Qalo, above n. 78, at 630.

83 US–Jordan FTA, Article 5(2).

provides enhanced opportunities to improve labor standards' and specify that the Joint Committee shall 'consider any such opportunity identified by a Party'. In theory, enforcement for violations of the environmental and labour obligations is strengthened, as these obligations are now subject to the same dispute settlement provisions as the economic aspects of the agreement, which allow for 'any appropriate and commensurate measure'.[84] However, side letters between the US and Jordan have ruled out this option.[85]

The Trade Promotion Authority Act of 2002, which granted fast-track negotiating authority for another five years, sets out negotiating objectives on a range of matters, including labour and environmental provisions.[86] Similar to the US–Jordan FTA, future agreements are to include a provision prohibiting the parties from failing to enforce their environmental or labour legislation in a manner affecting trade, and negotiators must now 'seek' equal dispute settlement rights for all types of obligations (including this one).[87] But the standard which the parties are to 'strive to ensure' is lower, described in terms of 'not weakening or reducing' environmental and labour protections and limited to activities which are 'an encouragement for trade'.[88]

With two qualifications, US regional trade agreements negotiated pursuant to this legislation with Singapore, Chile, Morocco, Central America–Dominican Republic (CAFTA–DR), Bahrain, Colombia and Peru have generally met or exceeded these negotiating objectives. In addition to the primary obligation not to fail to effectively enforce their environmental and labour laws, the parties are obliged to 'strive to ensure' that their labour laws meet ILO standards, which they also reaffirm, and – improving on the US–Jordan model – to 'ensure' high levels of environmental protection. One new development is the inclusion of a clause in the Singapore, CAFTA–DR, Colombia and Peru agreements 'recall[ing] that paragraph 5 of the ILO Declaration states that labour standards should not be used for protectionist trade purposes'. The agreements all include NAFTA-style private party enforcement rights and establish, in various ways, institutions for future co-operation on environmental and labour matters.

The qualifications concern dispute settlement. First, only the primary obligation not to fail to enforce domestic environmental and labour legislation is subject to dispute settlement; and second, in contrast to the economic provisions of the agreements, which are generally subject to trade retaliation, for violations of the

84 *Ibid*., Article 17(2)(b).

85 See the identical side letters dated 23 July 2001, in which the representatives of the US and Jordan each promised that 'my Government would not expect or intend to apply the Agreement's dispute settlement enforcement procedures to secure its rights under the Agreement in a manner that results in blocking trade'. For discussion of the relevance of these side letters for the enforcement of the labour provisions of the agreement, US Congressional Record, Proceedings and Debates of the 107th Congress, First Session, House of Representatives, 31 July 2001, pp. H4871–H4881 (text of letters at H4874–H4875).

86 19 USC 3802(a)(5)–(7), (9) and (b)(11). 87 19 USC 3802(b)(12)(G). 88 19 USC 3802(a)(7).

social provisions there is only the possibility of fines (limited in all cases to $15m, adjusted for inflation, collected by suspension of concessions, and spent on labour and environmental matters in the territory of the party in default). Both of these points have attracted the ire of the US Labor Advisory Committee,[89] which compares these agreements unfavourably to the US–Jordan FTA and claims that they fail to meet the negotiating objective of equivalent dispute settlement provisions for all aspects of the agreement.[90] Perhaps these criticisms are a little harsh. Little is gained by the (theoretical) availability of dispute settlement in the US–Jordan FTA for an obligation to 'strive to ensure' high standards of labour and environmental protection; and the dispute settlement objective merely requires negotiators to 'seek' equivalence, not to achieve it. This is not to say that US negotiators have not failed to meet this particular objective; only that such a conclusion depends on evidence other than the final text of the agreement.

Recent events have also pointed to significant changes in US trade policy. In May 2007, both the Democrat and Republican parties announced agreement on strengthened social provisions in future regional trade agreements, among other changes.[91] It has been reported that this may lead to renegotiations of the agreements with Colombia, Peru, Panama and Korea, which have been signed but not yet ratified by Congress.[92] Under the title 'A New Trade Policy for America', the parties announced that future free-trade agreements would contain fully enforceable obligations to comply with five basic ILO labour standards[93] as well as certain multilateral environmental agreements,[94] and fully enforceable obligations not to

89 This is a body established to advise on trade negotiations.

90 See, e.g. Labor Advisory Committee for Trade Negotiations and Trade Policy, *Report to the President, the Congress and the United States Trade Representative on the US–Chile and US–Singapore Free Trade Agreements*, 28 February 2003.

91 The proposal also announces changes on intellectual property, port security, and investment provisions, as well as on US worker assistance legislation.

92 'Specter of FTA Renegotiation Rears Head', *English.chosun.com*, 13 May 2007, at http://english.chosun.com/w21data/html/news/200704/200704130016.html, reports that the US administration has already asked Colombia, Peru and Panama for renegotiations.

93 These are listed as freedom of association, the effective recognition of the right to collective bargaining, elimination of all forms of forced or compulsory labour; effective abolition of child labour and a prohibition on the worst forms of child labour; and elimination of discrimination in respect of employment and occupation.

94 These are listed as the CITES; the Montreal Protocol; the Convention on the Prevention of Marine Pollution by Dumping of Wastes and Other Matter, done at London 3 November 1972; the Convention for the Strengthening of the Inter-American Tropical Tuna Commission, done at Washington, DC, 31 May 1949, in force 3 March 1950; the Convention on Wetlands of International Importance, especially as Waterfowl Habitat, done at Ramsar 2 February 1971, in force 21 December 1975; the International Convention for the Regulation of Whaling, done at Washington, DC, 2 December 1946, in force 10 November 1948; and the Convention for the Conservation of Antarctic Marine Living Resources, done at Canberra 20 May 1980, in force 7 April 1982. Special mention is made of 'an Annex fully requiring Peru to take major specific steps to crack down on illegal logging, and additional action to stop illegal logging of mahogany' and an 'unprecedented' provision permitting the United States to inspect illegal logging within Peru and prevent shipping at the border.

lower existing labour and environmental standards.[95] Future agreements would also reduce the parties' discretion to direct resources from the enforcement of labour standards, would permit labour standards conditionality in government procurement, and would provide for the same remedies for these social provisions as for the economic provisions of the agreements.

These changes are indeed radical. For the first time, social provisions in US regional trade agreements would mandate an objective standard of protection; moreover, for the first time this standard would repeat fully the language of ILO core labour standards. Domestically, this proposal is highly controversial, as it would be the first time that the US would be subject to review of its domestic labour and environmental legislation, and it remains to be seen whether it will translate into reality.

4. New Zealand

The post-NAFTA practice of the US has clearly influenced New Zealand,[96] which has negotiated labour and environment side agreements to its agreement with Thailand and its Trans-Pacific Strategic Economic Partnership, (Trans-Pacific SEP) agreement with Singapore, Brunei and Chile. In these side agreements the parties promise that they will 'not seek to gain trade or investment advantage' by weakening or derogating from their labour or environment legislation, and reaffirm (or, in the case of non-Members, affirm) their ILO obligations and commitments. They also promise to 'work actively to ensure' that their legislation is 'in harmony' with 'internationally recognised labour principles and rights' and 'internationally accepted levels of environmental protection such as those established by multilateral environment agreements to which the Participants are party', and 'to promote public awareness of [their] environmental laws, regulations, policies and practices domestically'. Similar to at least some of the US agreements, these also state that each party 'will ensure' (this being notably stronger than the previous terminology of 'work actively to ensure') that its trade and environmental legislation and policies are not used for trade protectionist purposes.

The two sets of New Zealand agreements differ in one respect; namely that the Trans-Pacific SEP side agreements contain a provision in which the parties promise to respect the 'sovereign right' of each party to 'set, administer and enforce' its own legislation 'according to its priorities'. This provision seems to be drawn from the NAFTA model, which provides that a party does not violate its obligation to enforce its labour and environmental legislation if this represents a bona fide decision to allocate resources to other labour or environmental matters respectively.[97] In two

95 'Congress and Administration Announce New Trade Policy', Press Release, US House of Representatives, 11 May 2007, at http://waysandmeans.house.gov/news.asp?formmode= release&id=512.

96 In 2001 New Zealand adopted frameworks for integrating labour and environment issues into its regional trade agreements. See www.mfat.govt.nz/Trade-and- Economic-Relations/NZ-and-the-WTO/ Trade-Issues/.

97 NAAEC, Article 45(1); and NAALC, Article 49(1).

key respects however this version is broader: first, it applies to the 'setting' of environmental and labour legislation as well as to its enforcement; and second, the 'priorities' of the party are entirely unqualified. If taken seriously (as the term 'sovereign right' implies it should), this escape clause undermines the other provisions in these agreements.

Institutionally, the New Zealand–Thailand side agreements establish Labour and Environment Committees, with the function of organising co-operative activities, serving as a channel for dialogue, reviewing the agreement and managing disputes, while the Trans-Pacific SEP leaves these functions up to *ad hoc* meetings of respective government officials. On the other hand, in both the Thailand and Trans-Pacific agreements, there is no enforcement of the labour provisions, other than consultations, while in the environment agreements there is a dispute settlement procedure even if it is a little weak. A dispute may be referred to a meeting of the 'interested Parties' for report, and the affected parties are then under an independent obligation to implement the resulting report.

5. The European model

The approach of the European Union (EU) to social issues is rather different, and consists of two main components. On the one hand, it has a highly developed practice of including 'human rights clauses' in its international agreements (including regional trade agreements) which allow for the suspension of the agreement in the event that one of the parties violates human rights or democratic principles. On the other, it prefers to deal with 'softer' social issues, including labour and the environment, by way of co-operation, entailing where necessary financial and technical assistance.

Human rights clause Human rights clauses have their origins in the Lomé Conventions of the 1970s and 1980s, but the EU decided in 1995 to systematically include such clauses in all future international trade agreements, including regional trade agreements.[98] Clauses of this type are now found in the nine regional trade agreements between the EU and its Mediterranean neighbours,[99] in the three 'stabilization and accession' regional trade agreements with countries of the Western Balkans[100] and in the regional trade agreements with South Africa, Mexico and

98 For a full analysis of these clauses see Lorand Bartels, *Human Rights Conditionality in the EU's International Agreements* (Oxford: Oxford University Press, 2005).

99 There are EU 'Euro-Mediterranean' Association Agreements with Israel, Tunisia, Morocco, Jordan, Egypt, Lebanon and Algeria (all in force) and with Syria (initialled), and an 'interim' association agreement with the Palestinian Authority (in force). The political framework is known as the 'Barcelona Process'.

100 There are EU Stabilisation and Association Agreements (SAAs) with Croatia and the Former Yugoslav Republic of Macedonia (in force) and Albania (awaiting ratification by Albania). SAA negotiations have started with Bosnia-Herzegovina, Montenegro and Serbia (currently interrupted).

Chile. They are also found in the Cotonou Agreement[101] and it is planned that they are to be included in the six Economic Partnership Agreements currently being negotiated to replace the trade provisions of this agreement.[102] They are also included in a large number of non-preferential trade and co-operation agreements.

The human rights clause consists of two main parts. First is an 'essential elements' clause, which states that:

> Respect for the democratic principles and fundamental human rights established by the Universal Declaration of Human Rights shall inspire the domestic and international policies of the Parties and shall constitute an essential element of this Agreement.

This basic provision is given its main operative effect via a 'non-execution' clause, which states that a failure to fulfil an obligation under the agreement, including human rights obligations, entitles the other party, subject to a consultation procedure, to take 'appropriate measures'.

To date, human rights clauses have been applied in cases involving gross human rights violations and military coups, but there is little doubt that they have the potential to cover a range of matters, including any violations of labour or environmental rights that rise to the level of 'human rights'.

Co-operation on social issues As opposed to this standard setting for human rights and democratic principles, the EU's main approach to other social issues, such as environment, labour, culture and occasionally gender[103] is to treat these as matters for co-operation, where appropriate supported by financial and technical assistance.[104] Even in the case of labour, the EU shies away from the standard setting of the countries discussed above, preferring to use the general term 'social matters'. In those cases in which it has conceded to use the term 'fundamental social rights'[105] this is only for the purposes of 'giv[ing] priority' to such rights, though in one case the parties also 'recognise the responsibility to guarantee basic social rights'.[106] It has

101 The Cotonou Agreement is a framework trade and development agreement between the EU and 79 developing countries, mainly ex-colonies. Its trade provisions establish non-reciprocal free trade into the EU in violation of Article XXIV GATT, and the agreement therefore exists under a WTO waiver until 31 December 2007.

102 European Commission, *Recommendation for a Council Decision Authorising the Commission to Negotiate Economic Partnership Agreements with the ACP Countries and Regions*, SEC (2002) 351, Annex 1.

103 Separate provisions for co-operation on gender are set out in European Union–Chile Association Agreement (EU–Chile AA), Article 45; and Cotonou Agreement, Article 31.

104 In principle, co-operation in these areas is administered jointly by the Joint Councils established under the agreements; in practice, it is treated as part of the EU's development co-operation programme.

105 European Union–Algeria Association Agreement (EU– Algeria AA), Article 74; European Union–Jordan Association Agreement (EU–Jordan AA), Article 82(1); European Union–Syria Association Agreement (EU–Syria AA), Article 110(1); and EU–Chile AA, Article 44(1) (with a further promise to 'promote' relevant ILO Conventions).

106 EU–SA TDCA, Article 86(2). This provision also lists the core labour standards of the ILO.

been suggested that South Africa refused to accept positive commitments on labour standards in its agreement with the EU in order to protect its positive discrimination programme under its Black Economic Empowerment (BEE) programme,[107] but one can imagine, based on the EU's practice, that it was pushing at an open door. Only in the Cotonou Agreement do the parties go as far as incorporating a legally binding standard, when they 'reaffirm their commitment to the internationally recognised core labour standards, as defined by the relevant International Labour Organisation (ILO) Conventions'. The Cotonou Agreement also represents a novelty in the EU's practice by including a statement that 'labour standards should not be used for protectionist trade purposes'.[108]

6. Other countries

For other countries, the case for considering social protection as a relevant topic in regional trade agreements (not including integrationalist 'communities') is yet to be fully made out.

For instance, about half of the EFTA agreements contain a type of human rights clause on the model of the EU agreements,[109] but on more specific social issues the agreements are decidedly reticent, even on the prospect of co-operation: at most, some agreements allow that '[c]onservation of the environment shall be taken into account in the implementation of assistance [in the context of economic co-operation]'.[110] Japan has a stuttering practice of including provisions on co-operation,[111] in the areas of environmental conservation and the promotion of sustainable development,[112] though not on the more sensitive issue of labour

107 Paul Kruger, 'Labour provisions and commitments in the TDCA and Cotonou Agreement', Tralac, 17 October 2006, available at http://epa.tralac.org/scripts/content.php?id=5395. For potential conflicts between BEE objectives and non-discrimination provisions in WTO law (relevant to the equivalent provisions in the EU–South Africa TDCA), see Jon Mortensen, 'WTO vs BEE: Why Trade Liberalisation May Block Black South Africans' Access to Wealth, Prosperity or Just a White-Collar Job', Danish Institute for International Studies Working Paper No. 2006/30. I am grateful to Paul Kruger for providing me with this reference.

108 Cotonou Agreement, Articles 50(1) and (3).

109 Article 1.2 of the following FTAs: EFTA–Jordan Free Trade Agreement, EFTA–Morocco Free Trade Agreement, EFTA–Palestinian Authority Free Trade Agreement, and EFTA–Macedonia Free Trade Agreement. Two other agreements permit 'rebalancing measures' in the event of a failure to fulfil an obligation (see EFTA–Croatia FTA, Articles 1.2 and 28; and EFTA–Lebanon Free Trade Agreement, Articles 1.2 and 33). The preamble to the EFTA–Tunisia FTA refers to 'the observance of human rights and political and economic freedom, which form the very basis for co-operation between the EFTA States and Tunisia'. The EFTA agreements with Turkey, Israel, Mexico, Singapore, Chile, Singapore and SACU have no operative human rights provisions.

110 EFTA–SACU FTA, Article 31(2).

111 Japan–Malaysia Implementing Agreement, Article 41(b). Japan–Singapore (2002) did not have this; nor does Japan–Philippines (2006).

112 Japan–Malaysia Implementing Agreement, Article 41(a); Japan–Mexico EPA, Article 147(1); and Japan–Philippines Implementing Agreement, Article 35(a)(2).

standards. Another interesting development is the conclusion of two labour and environment side agreements to the Chile–China Free Trade Agreement,[113] of which, at the time of writing, only the first is publicly available.[114] This instrument does not purport to set standards, but provides for 'mutually agreed co-operation activities' consisting of research and information exchange. For these countries, then, standard setting is so far unattractive, and co-operation only partially less so.

Finally, one should mention the increase in preambular references to principles of sustainable development, ILO labour standards and human rights in agreements which otherwise contain no binding obligations on these matters. Though unwilling to replicate NAFTA-type binding standards in its later agreements, Mexico has included that agreement's preambular statements on social issues in a number of its later agreements with Latin American countries.[115] Other countries with exposure to such statements have also incorporated them into their own treaty practice. Thus, references to social protection are found in the preambles to the Chile–Costa Rica, Chile–Korea and CARICOM–Costa Rica agreements. Similarly, the EU's insistence on a human rights dimension has influenced the preambles of agreements concluded by the Balkan countries. Whether these preambular references presage operative provisions in future agreements by these countries is difficult to say.

III. Prospects for social issues in future RTAs

The relationship between trade and social issues has become both more obvious and more sensitive over the past decade, and it is a signal failure of WTO Members not to have grappled with those areas in which these objectives are in conflict. It is therefore to be welcomed that this inevitable discussion is being taken up in negotiations at the regional level, where parties with an interest in the matter are more able to experiment with different forms of regulation.

As has been shown, at present some countries are committed to negotiating a link between trade and social protection, some are feeling their way, and still others have doubts about any link. One may confidently predict that the US will continue to press for social protection in its future regional trade agreements, and, as mentioned above, it seems highly likely that these will be very much strengthened. Canada is likely to continue similar policies, with the addition of its 'cultural exception', the EU is committed to its policies of human rights conditionality and (mainly funded) co-operation on other social issues, New Zealand is testing forms of regulation for

113 Chile–China FTA, Article 108.

114 China–Chile Memorandum of Understanding on Labour and Social Security Cooperation, available at www.direcon.cl/documentos/China2/memorando_ entendimiento_laboral_china_en.pdf.

115 See Mexico's agreements with Costa Rica and Bolivia, Colombia and Venezuela, Nicaragua, Chile, and with El Salvador, Guatemala and Honduras. Mexico does not however mention human rights in its agreements with Israel, Uruguay or Japan.

labour and environmental standards with various countries, and Japan has indicated a willingness to include provisions on environmental co-operation in its agreements.

The picture is far from uniform, even among developed countries. Australia remains opposed to any link between trade and social protection (despite the existence of such provisions in its agreement with the US), the EFTA countries are ambivalent, allowing at times for a human rights clause but otherwise placing no great emphasis on social issues even as a matter for co-operation, and it is difficult to gauge the independent enthusiasm of those countries who have entered into social provisions with these pioneering countries. Nonetheless, the trend seems to favour a gradual acceptance of the role of social issues in regional trade agreements. Thanks partly to the social justice movement, the public in many countries are becoming more educated and vocal about their concerns about trade and social protection, and beginning to demand that these links be recognised in new regional trade agreements. In addition, the idea that the links are valid seems to be gaining its own dynamic. As has been shown, a number of agreements include preambular references to social issues in regional trade agreements, even in the absence of any follow-up normative provisions, and this may well lead to operative provisions at a later stage.[116] More generally, this trend fits with broader changes in international relations. All of the new supranational 'communities' cover social issues, a development no doubt related to the increasing willingness of countries to use international law as a means of regulating matters previously left to domestic discretion.[117]

One may also hazard a prediction as to the design of future provisions linking trade and social protection. The safeguarding of individual rights to regulate is at present a haphazard affair, and the implications of conflicts clauses privileging other agreements between the parties have yet to be fully worked out, especially in the WTO context. But those provisions seeking to regulate social protection by the parties to a regional trade agreement appear to be of two main types. One is the NAFTA model of requiring the parties to 'ensure a high standard of protection', which is likely to be upgraded in future US agreements into firm obligations to comply with ILO standards. A second is a provision requiring the parties not to reduce social protections as a means of encouraging trade (or investment). At present, this second type of provision is proving to be more popular.[118] Further, one sees the gradual introduction of a corollary clause stating (in line with the WTO Singapore Ministerial Declaration and ILO Declaration on core labour standards)

116 The EU's human rights clause evolved in this way from Lomé III (1985) to IV*bis* (1995).

117 This phenomenon is sometimes referred to as the 'Europeanization' of international law. See e.g. Joost Pauwelyn, 'Europe, America and the "Unity" of International Law', Conference on 'Europeanisation' of Public International Law: The Status of International Law in the EU and its Member States (Amsterdam) (September 2005).

118 This type of provision is itself a compromise, because if the 'race-to-the-bottom' theory is valid, a reduction in social protection can have the *effect* of increasing trade and investment, even if this is not its purpose.

that countries will not *increase* their social protections as a means of protecting their domestic industries. What both of these latter provisions have in common is a focus on the abuse of social policy, in both directions, for illegitimate economic purposes.

While it is impossible to predict precisely how future regional trade agreements will attempt to manage the various links between social protection and trade liberalisation, it can at least be said that this will continue to occur, and it will consist of some mix of clauses protecting rights to regulate, clauses setting mutual standards and prohibitions on backsliding on standards, with a variety of enforcement options, and provisions on future co-operation. However these provisions come to look in detail, it must be considered a positive development that so many countries are increasingly focusing on the different (and not always 'mutually supportive') ways in which trade and social protection relate to each other. It is certainly an improvement on the stalemate presently gripping the multilateral stage.

13

Dispute settlement

VICTORIA DONALDSON AND SIMON LESTER

I. Introduction

As international trade disputes have shifted over the years from diplomatic exercises to more legalistic contests,[1] the dispute settlement procedures set out in trade agreements have taken on a more important role. The dispute provisions of the GATT 1947 were a mere two paragraphs.[2] Over the years, these provisions were supplemented with additional rules, eventually developing into the detailed procedures of the WTO's Dispute Settlement Understanding. And in the 350-plus WTO disputes that have been brought since the WTO's inception, these rules have been elaborated by panels and the Appellate Body. The result is that today the WTO's dispute procedures are well-developed, widely studied, and generally considered reliable and credible by governments and other actors.

Not surprisingly, then, in drafting the preferential trade agreements (PTAs) discussed in this book, the state parties to these agreements came up with dispute provisions that are similar in many ways to the WTO rules. As a result, for many of the topics discussed in this chapter, we note the related WTO provisions and offer comparisons. However, there are differences as well. These differences may reflect the various opinions among WTO Members as to what the rules should be, as well as new thinking about the best approach to certain issues based on the experience at the WTO.

In this chapter, we examine the following aspects of the dispute procedures in recent bilateral and regional PTAs. First, we look at the *administration* of dispute settlement procedures. At the WTO, administration of the DSU is carried out by the Dispute Settlement Body, which is made up of all the WTO Members. In addition, the WTO has a Secretariat that provides various services in support of this administration. In this section, we examine whether and to what extent PTAs have similar bodies and support.

1 See generally, Robert E. Hudec, *Enforcing International Trade Law: The Evolution of the Modern GATT Legal System* (Salem, NH: Butterworth, 1993).

2 In fairness, the GATT was originally intended to be one chapter in the larger International Trade Organisation (ITO), which had six full articles setting out dispute settlement procedures. But the ITO never came into force, and the GATT thus had to function on its own.

Second, we address the relationship of PTA dispute settlement to other dispute settlement, such as the DSU. A key aspect of this issue is the recent talk about the 'spaghetti bowl' or 'noodle bowl' of trade agreements that now exist, with a great deal of overlap among the countries who have signed agreements with each other. In this context, we examine the rules these PTAs establish for addressing the options for bringing disputes in different fora.

Next, we turn to the details of bringing a complaint. In this section, we try to explain how agreements differ in the extent to which they set out specific rules in this regard, and also how they address certain systemic issues relating to the complaints that can be brought.

We then turn to the process of selecting the 'judges' who will hear the case. Trade disputes differ from most domestic judicial systems in that they do not have a standing body of judges who will hear cases. Rather, the disputing governments themselves choose the judges (for the most part).

We also examine the details of the panel process, comparing and contrasting the different rules that have been chosen.

Finally, we discuss several aspects of the rules on implementation of adverse decisions, that is, where a violation has been found. This is an area in which there has been some new thinking in recent years, as governments try to work out the most effective rules possible for ensuring that adverse judgments are followed.

Before turning to the substance, we note two overarching points at the outset. First, we are not dealing here with *all* dispute settlement under the PTAs at issue. Rather, we are focusing on government-to-government dispute settlement over 'trade' issues, which is generally the subject of a separate chapter in these agreements. In addition to this type of dispute settlement, some agreements have special dispute procedures in areas such as investment, environment and labour. These areas will be not be covered here, but will be discussed, albeit briefly, in the substantive chapters of the book covering these topics.

Second, we note that at the time of this writing there have been no disputes under the recent bilateral and regional trade agreements that are the focus of this book. Some older agreements, like the North American Free Trade Agreement (NAFTA) and the United States–Israel Free Trade Agreement, have seen a handful of government-to-government disputes, several of which resulted in panel reports being issued. For the more recent agreements, however, there has been nothing so far. As a result, there is no dispute settlement practice to look at, which creates some important gaps in the understanding of how the process will actually work.

II. Administration of dispute settlement

We first examine the various types of institutional frameworks created under PTAs for the administration of dispute settlement. Before doing so, we recall how this is handled in the context of the WTO.

The administration of dispute settlement is expressly identified in the WTO Agreement as one of the functions of the WTO.[3] Formally, all WTO functions are carried out, at the highest level, by the Ministerial Conference, which is composed of all WTO Members and which meets at least once every two years.[4] Between such meetings, responsibility for WTO functions lies with the General Council, also composed of representatives of all WTO Members.[5] The WTO Agreement further provides that the General Council is to convene as the Dispute Settlement Body, with its own chairman and rules of procedure, to discharge the responsibilities assigned to that Body under the DSU.[6]

Thus, it is the DSB which administers dispute settlement in the WTO on a day-to-day basis. The DSB has a formal role throughout the process, beginning with the requirement that it be notified of all requests for consultations through to its surveillance and monitoring of the implementation of adopted panel and Appellate Body reports. The findings set out in panel and Appellate Body reports bind the parties to the dispute only once those reports have been adopted by the DSB, and DSB authorisation is required before a complaining party may impose trade sanctions against a responding party who has not brought its inconsistent measure into conformity with its obligations. In this regard, the DSU expressly assigns to the DSB 'the authority to establish panels, adopt panel and Appellate Body reports, maintain surveillance of implementation of rulings and recommendations, and authorise suspension of concessions and other obligations'.[7] The DSB is directed to meet as often as necessary to carry out its functions.[8] In practice, this means that it meets regularly once a month, supplemented by special meetings from time to time.

The DSB takes decisions by consensus.[9] However, this decision-making rule is reversed at the following key stages of the dispute settlement system: the establishment of a panel,[10] the adoption of panel and Appellate Body reports,[11] and the authorisation of the suspension of concessions.[12] The fact that a 'negative consensus' decision-making rule applies at these vital steps in the proceedings operates to make it almost inconceivable that a responding party or its allies would succeed in getting the DSB to block any of these decisions. This, in turn, has the consequence that the essential responsibility for driving proceedings forward rests with the complaining party, who may request the DSB to take the necessary decisions to keep the process moving.[13]

As far as institutional support for dispute settlement is concerned, Article 27 of the DSU provides that the WTO Secretariat has the responsibility 'of assisting

3 Article III.3. 4 Article IV.1. 5 *WTO Agreement*, Article IV.2. 6 Article IV.3.
7 DSU, Article 2.1. 8 *Ibid.*, Article 2.3.
9 *Ibid.*, Article 2. Footnote 1 to that Article defines consensus to mean that no Member present when the decision is taken formally objects to the proposed decision.
10 DSU, Article 6.2. 11 *Ibid.*, Article 16.4. 12 *Ibid.*, Article 22, paras. 6 and 7.
13 The DSU imposes a 'negative consensus' rule by providing, in each case, that a decision 'shall' be taken unless the DSB decides by consensus otherwise.

panels, especially on the legal, historical and procedural aspects of the matters dealt with, and of providing secretarial and technical support'.[14]

A. The administration of PTAs

None of the PTAs examined has as elaborate an institutional system as the WTO. Various arrangements exist. Most PTAs provide for some sort of joint committee or commission to deal with administration of the agreement.[15] This body may be at the cabinet or ministerial level, or at a lower level, or both.[16] Some PTAs create a single administrative body, but specify that it may meet either at the level of Ministers or of senior officials.[17] Yet other PTAs do not provide for any body to administer the agreement at all. Instead, they combine a requirement that each party identify a 'contact point' to facilitate bilateral communication on issues related to the PTA with a requirement for a periodic meeting of Ministers to review the operation of the agreement.[18] The PTAs that contemplate the creation of a joint administrative body provide for decision making to be achieved through consensus or mutual agreement. Typically, the joint administrative body or ministerial meeting is also empowered to establish additional committees, subcommittees or working groups as necessary.

Although a few PTAs expressly provide a joint high-level body with the power to issue interpretations of the agreements,[19] many others are silent on this issue. Some

14 DSU, Article 27.1. Paragraphs 2 and 3 of Article 27 provide for the WTO Secretariat to make a qualified legal expert available to assist developing countries with dispute settlement – while ensuring the continued impartiality of the Secretariat – and contemplate the provision of special training courses on dispute settlement procedures and practices to WTO Members. Article 17.7 contains a similar provision regarding the support to be provided to the Appellate Body, which has an administratively separate secretariat. Article VI of the WTO Agreement deals with the WTO Secretariat more generally.

15 These bodies have a variety of names, including the Joint Committee (EFTA–Chile Free Trade Agreement, Article 85), the Free Trade Co-ordinators (Canada–Costa Rica Free Trade Agreement, Article XIII.2); the Free Trade Commission (United States–Chile FTA, Article 21.1) and the Association Committee (European Union–Chile Association Agreement (EU–Chile AA), Article 6). Most agreements provide for regular meetings to be held annually, with an additional possibility to call additional special meetings. Some PTAs call for only biennial meetings/reviews (e.g., the New Zealand–Singapore Closer Economic Partnership Agreement (NZ–Singapore CEPA), Article 68.1; and EFTA–Chile FTA, Article 85.6).

16 Some agreements name these cabinet or ministerial-level bodies (e.g., the Free Trade Commission created in Article XIII.1 of the Canada–Costa Rica FTA and the Association Council created in Article 3 of the EU–Chile AA).

17 For example, the Closer Economic Partnership Joint Commission created in Article 16 of the New Zealand–Thailand Closer Economic Partnership Agreement (NZ–Thailand CEPA); the Free Trade Commission created in Article 18.1 of the Korea–Chile Free Trade Agreement; and the Free Trade Agreement Joint Commission created in Article 1701 of the Thailand–Australia Free Trade Agreement.

18 See, e.g., Singapore–Australia Free Trade Agreement, Chapter 17, Articles 2 and 3. The NZ–Singapore and Korea–Singapore PTAs do not create any joint body to oversee implementation of the agreement, although they do provide for consultations in certain substantive areas (not including dispute settlement) as well as periodic review of the agreement at the Ministerial level and the possibility to create committees and working groups (Article 68.1 and Article 22.1, respectively).

19 An example is contained in Article 19.2.2(e) of the United States–Morocco Free Trade Agreement. Along the same lines, Article IX:2 of the WTO Agreement provides that '[t]he Ministerial Conference and the

PTAs provide that when an issue relating to the agreement arises in a domestic court or tribunal of either party, the relevant joint body created under that agreement is to submit an agreed interpretation of the PTA to that domestic court or administrative tribunal.[20]

With respect to the administration of dispute settlement under these agreements, only a few PTAs identify this as a discrete function to be carried out by a body created pursuant to the agreement.[21] Similarly, only a few PTAs refer to a secretariat that will be involved in administration of the agreement or in supporting a dispute settlement mechanism. However, even the agreements that do contemplate the provision of such support do not appear to envisage the creation of a new and autonomous entity so much as require each party to identify an existing body or individual within its territory that will serve as part of a 'secretariat' in order to provide support and co-ordinate, as necessary, with its counterpart in the territory of the other party to the PTA.[22]

B. The role of administrative bodies in dispute settlement

Generally speaking, the level of formal involvement of any administrative body in dispute settlement is significantly lower than is the case within the WTO, and in many PTAs there is no role for such bodies in individual disputes.[23] Many PTAs do,

General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements'.

20 E.g., Korea–Chile FTA, Article 19.16; US–Chile FTA, Article 22.19; Central American–Dominican Republic–United States Free Trade Agreement (CAFTA–DR–US), Article 20.20; and Canada–Costa Rica FTA, Article XIII.19. Such provisions usually also allow each party to submit its own interpretation to the domestic tribunal in the event that the joint administrative body is unable to reach agreement.

21 See, e.g., Canada–Costa Rica FTA, Article XIII.3. The PTAs to which the US is party contain specific provisions entitled 'Administration of Dispute Settlement Proceedings'. However, these provisions state only that each party to the agreement is to designate an office to provide administrative assistance to panels, notify the location of such office, and be responsible for its operation and costs as well as a share of the expenses of panellists. (CAFTA–DR–US, Article 19.3; Australia–United States Free Trade Agreement (AUSFTA), Article 21.3; US–Chile FTA, Article 21.2; United States–Singapore Free Trade Agreement, Article 20.2; US–Morocco FTA, Article 20.3) The Japan–Singapore Economic Partnership Agreement (Japan–Singapore EPA) provides for the establishment of a Consultative Committee to 'facilitate the implementation of' Chapter 21 on dispute settlement, and requires that the Committee include 'one legal expert designated by each Party' (Article 140.4).

22 Canada–Costa Rica FTA, Article XIII.3; CAFTA–DR–US, Article 19.3; AUSFTA, Article 21.3; US–Chile FTA, Article 21.2; US–Singapore FTA, Article 20.2; US–Morocco FTA, Article 20.3; EFTA–Chile FTA, Article 86; and Korea–Chile FTA, Article 18.2 and Annex 18.2.

23 At first glance, the terms of the PTA between the European Communities (EC) and Israel appear to give a prominent role to its ministerial-level Association Council in assigning to that body responsibility for settling disputes referred to it by either party. However the agreement also provides for the dispute to be referred to a three-person arbitration in the event that the Association Council is unable to resolve the dispute through a decision (European Union–Israel Association Agreement (EU–Israel AA), Article 75). The European Union–South Africa Trade, Development and Co-operation Agreement (EU–SA TDCA) contains similar provisions in its Article 104.

however, provide for the relevant joint administrative body to adopt rules of procedure and/or codes of conduct for panels.[24] Below we survey the types of involvement provided for in certain PTAs.

Several PTAs provide for the relevant joint body or secretariat to be notified of certain steps in the resolution of an individual dispute.[25] In the early stages of a dispute, quite a few PTAs require or allow a dispute to be referred to the joint body created under the agreement at the outset of the dispute, either in lieu of[26] or following bilateral consultations[27] and before the establishment of a panel. The EFTA–Chile FTA provides for bilateral consultations between the disputing parties, but adds that such '[c]onsultations shall take place before the Joint Committee unless the Party or Parties making or receiving the request for consultations disagree'.[28] A few PTAs allow a joint administrative body to provide or have recourse to good offices, conciliation or mediation.[29]

Another approach is to give joint bodies a role in sending the dispute to a panel and/or selecting the panellists. The India–Sri Lanka Free Trade Agreement provides for its Joint Committee to be notified if the parties are unable to negotiate a solution to their dispute, and then for a panel to be constituted by its Joint Committee 'in consultation with the relevant Arbitration Bodies in the two countries'.[30] The European Union–Israel Association Agreement (EU–Israel AA) provides for each party to the dispute to appoint an arbitrator and for the third arbitrator to be appointed by its ministerial-level Association Council, and the European Union–Chile Association Agreement (EU–Chile AA) provides for an Association Committee to establish a list of at least fifteen arbitrators and, upon receipt of a request to establish a panel, to select three names by lot from that list.[31]

As far as the work of panels is concerned, a number of agreements make some provision for administrative support. For example, the Canada–Costa Rica Free Trade Agreement provides for its Secretariat to provide administrative assistance to panels.[32]

24 For example, Turkey–Morocco FTA, Article 33.9; Canada–Costa Rica FTA, Article XIII.12; CAFTA–DR–US, Article 20.7.2(d) and Article 20.10; AUSFTA, Article 21.7. 5(b) and 21.8; US–Morocco FTA, Article 20.7.5(c) and Article 20.8; US–Singapore FTA, Article 20.4.4(b)(ii) and (d); US–Chile FTA, Article 22.7.2(b) and 22.10; and EC–SA TDCA, Article 104.8.

25 See Canada–Costa Rica FTA, Article XIII.7.2 (request for consultations) and XIII.8.3 (request for establishment of a panel); EFTA–Chile, Articles 96.5 (implementing measure); and EU–Chile AA, Article 188.5 (implementing measure).

26 Turkey–Morocco FTA, Article 33.2; EU–Chile AA, Article 183; and EU–Mexico FTA, Articles 42.2 and 42.3.

27 CAFTA–DR–US, Article 20.5.1; US–Singapore FTA, Article 20.4.2(a); AUSFTA, Article 21.6 and 21.7; US–Chile FTA, Article 22.5; US–Morocco, Article 20.6; and Japan–Singapore EPA, Article 140.3.

28 Article 90.1

29 E.g., CAFTA–DR–US, Article 20.5.4(b); and US–Chile FTA, Article 22.5.4(b).

30 India–Sri Lanka FTA, Article XIII.1 and XIII.2.

31 EU–Chile AA, Article 185.2 and 185.3. Article 104.7 of the EU–SA TDCA contains a similar provision.

32 Canada–Costa Rica FTA, Article XIII.3.3(a).

Although none of the PTAs have a formal procedure for adopting panel reports analogous to the WTO process, a few do stipulate that the panel report shall be delivered to the relevant joint administrative body.[33] Among these, a small number also provide for that joint body to then take a decision on the basis of the panel report which will bind the parties insofar as implementation is concerned.[34] In addition to requiring panel reports to be delivered to the Association Committee, the EU–Chile AA requires that all rulings on compliance measures and the level of suspension of benefits be provided to that Committee and made publicly available.[35] That agreement also requires responding parties to notify the Association Committee of implementing measures and complaining parties are to notify benefits that they propose to suspend.[36]

Most PTAs do not assign any joint body a role as far as the surveillance of panel rulings is concerned, but the Canada–Costa Rica FTA provides for its Free Trade Commission to include on its agenda the implementation of adopted recommendations or rulings whenever the measure found to be inconsistent has not been brought into conformity with the agreement.[37]

Lastly, as explained further in Part VI below, the Commissions/Joint Committees created in the various PTAs to which the United States (US) is party are given a special role in the collection and disbursement of monetary assessments in cases where there has been no implementation and the responding party elects to pay a monetary assessment rather than be subject to the suspension of concessions,[38] and in disputes relating to the enforcement of labour or environmental laws in which there has been no implementation.[39]

III. Relationship with other trade agreements and dispute settlement provisions

Possibly the most interesting, and thorniest, issues that arise in connection with the proliferation of PTAs concern how those agreements relate to each other and to the WTO's multilateral system. The substantive obligations created under the agreements are often similar or identical to those found in the WTO, and specific acts or measures taken by one country may give rise to a course of action under multiple agreements. In such circumstances, it is far from clear which dispute

33 E.g., Turkey–Morocco FTA, Article 33.6. 34 Turkey–Morocco FTA, Articles 33.7 and 33.8.

35 EU–Chile AA, Article 188.11. 36 *Ibid.*, Articles 188.5 and 188.8.

37 Canada–Costa Rica FTA, Article XIII.18.7. The reference to 'adopted' recommendations or rulings in this provision is puzzling because the agreement does not set out any procedure for the adoption of panel reports.

38 See US–Morocco FTA, Article 20.11.6; AUSFTA, Article 21.11.6; US–Chile FTA, Article 22.15.6; US–Singapore FTA, Article 20.6.6; and CAFTA–DR–US, Article 20.16.7.

39 See US–Morocco FTA, Article 20.12.4; AUSFTA, Article 21.12.4; US–Chile FTA, Article 22.16.4; US–Singapore FTA, Article 20.7.4; and CAFTA–DR–US, Article 20.17.4.

settlement mechanism an affected trading party can or should seek recourse to, and whether there is any relationship or hierarchy of norms among the various obligations created under the myriad of overlapping bilateral, regional and multilateral agreements.

The DSU does not expressly refer to other dispute settlement fora, identify any hierarchy of international law norms[40] or offer disputing parties any choice of forum. Article 23 of the DSU does, however, include a provision that was intended to reinforce the obligation to use the WTO's multilateral dispute settlement system and prevent Members from taking unilateral action in relation to alleged violations of WTO obligations.[41] This provision requires WTO Members to seek redress for any violation of the covered agreements exclusively through the dispute settlement mechanism contained in the DSU, including the procedures for determining the reasonable period of time for implementation and for obtaining authorisation to suspend concessions. In addition, Members are prohibited from making any unilateral determination that a violation has occurred. Instead, Members must pursue their concerns through the DSU, following the adoption of, and consistent with, the findings contained in a panel or Appellate Body report. Although Article 23 was by all accounts designed to prevent unilateral action by WTO Members, it seems possible to argue that the provision would preclude *any* determination, other than pursuant to the DSU, that a violation of a WTO obligation has occurred, including by panels operating pursuant to PTAs. This could raise interesting questions given the extensive incorporation by reference of WTO obligations found in many PTAs although, as discussed below, several PTAs themselves preclude panels from making determinations concerning WTO obligations.

In contrast to the DSU, many PTAs explicitly acknowledge the existence of legal obligations under multiple agreements (in particular the WTO) as well as the existence of multiple dispute settlement mechanisms (in particular that of the WTO) that may be available in respect of the same set of circumstances. Some of the ways in which PTAs address these issues are examined below.

A. Obligations in other agreements and conflicting norms

1. References to WTO obligations

Nearly all of the PTAs examined contain extensive references to, or incorporation by reference of, substantive WTO obligations. These range from statements that the PTA is established 'consistent with Article XXIV' of the GATT and Article V of the

40 Except that Article 3.2 of the DSU prescribes the use of customary rules of interpretation of public international law and Article 1.2 makes clear that certain special and additional rules and procedures contained in other WTO agreements prevail over those contained in the DSU.

41 Article 23 was widely seen as a reaction to an attempt to constrain the US use of Section 301 of its Trade Act of 1974, which allowed the President to make a determination of inconsistency with a trade agreement and to take retaliatory action against the foreign country or entity responsible.

GATS,[42] to statements that the PTA shall not diminish or reduce rights and obligations under the covered agreements,[43] and include statements confirming rights and obligations under the WTO Agreement[44] or under specific covered agreements;[45] as well as the wholesale incorporation of specific obligations, such as the rules on national treatment set out in Article III of the GATT 1994 and its interpretative notes,[46] or Article XX of the GATT and its interpretative notes.[47] The incorporation of WTO rights and obligations relating to the use of safeguards and antidumping measures is common in many of the PTAs examined,[48] and many also refer to WTO obligations in respect of SPS and TBT measures and customs valuation.

A few of these agreements direct panels to take account not only of the substantive WTO obligations, but also of the interpretation of those obligations in WTO dispute settlement.[49] The New Zealand–Singapore, Canada–Costa Rica, and Central

42 Thailand–Australia FTA, Article 101; and CAFTA–DR–US, Article 1.1.

43 For example: 'This Agreement shall not diminish the scope of any commitment made by either Party under GATS to which the other party has access' (Thailand–Australia FTA, Article 816); 'Nothing in this Article shall be construed so as to derogate from the obligations of the Parties' under the Agreement on Trade Related Investment Measures in Annex 1A to the WTO Agreement, or as parties to the Agreement on Government Procurement in Annex 4 to the WTO Agreement (Japan–Singapore EPA, Articles 75.3 and 101.5 respectively).

44 For example: 'The Parties confirm their rights and obligations under the Marrakesh Agreement establishing the World Trade Organization and the other agreements negotiated thereunder . . . to which they are party, and under any international agreement to which they are a party' (EFTA–Chile FTA, Article 4); 'The Parties affirm their existing rights and obligations with respect to each other under the WTO Agreement and other international agreements to which both Parties are party' (Korea–Chile FTA, Article 1.3.1.). See also US–Morocco FTA, Article 1.2.1; US–Singapore FTA, Article 1.1.2; US–Chile FTA, Article 1.3; AUSFTA, Article 1.1.1.2; CAFTA–DR–US, Article 1.3.1; and Canada–Costa Rica FTA, Article I.3.1.

45 For example: 'With respect to matters related to this Chapter [III on Trade in Services] the Parties confirm the rights and obligations existing under any bilateral or multilateral agreements to which they are a party' (EFTA–Chile FTA, Article 43); 'Nothing in this Chapter shall be construed so as to affect the rights and obligations that either Party has as a party to the Agreement on Technical Barriers to Trade in Annex 1A to the WTO Agreement' (Japan–Singapore EPA, Article 55.3. Article 8.8.2 of the Korea–Singapore FTA contains similar language); and '[T]he Parties affirm their existing rights and obligations with respect to each other under the TBT Agreement' (US–Morocco FTA, Article 7.2).

46 One of many such examples may be found in Article 3.2.1 of the CAFTA–DR–US.

47 CAFTA–DR–US, Article 21.1. In addition to incorporating Article XX, this provision records the parties' understanding 'that the measures referred to in Article XX(b) of the GATT 1994 include environmental measures necessary to protect human, animal, or plant life or health, and that Article XX(g) of the GATT 1994 applies to measures relating to the conservation of living and non-living exhaustible natural resources'.

48 The Turkey–Morocco FTA makes extensive reference to the covered agreements as the basis for its obligations with respect to such matters as SPS measures (Article 13.2), anti-dumping and countervailing duty measures (Article 18), safeguards (Article 19.1), balance of payments measures (Article 26), and technical barriers to trade (Article 34.3).

49 See, e.g., Article 4.2 of the Japan–Singapore EPA, which states that 'In the application of [the previous paragraph setting out security and general exceptions] the relevant interpretations and operation of the WTO Agreement shall, where appropriate, be taken into account'. Articles 19.2 and 69.2 of that Agreement contain similar provisions.

American–Dominican Republic–United States (CAFTA–DR–US) PTAs state that they are each to be interpreted in accordance with international law and with the objectives set out in that agreement.[50]

2. Provisions relating to conflicting norms

Several PTAs contain 'conflicts' provisions stipulating which, as between the PTA in question and another international agreement, is to prevail in the event of a conflict. As mentioned above, several such provisions are cast as 'confirming' rights under WTO agreements or clarifying that the PTA should not be construed as derogating from WTO rights and obligations. It is, however, interesting to survey a few of the different types of priorities that parties to PTAs have attached to potentially conflicting norms.

The New Zealand–Singapore Closer Economic Partnership Agreement (NZ–Singapore CEPA) makes clear that nothing in that agreement is to be regarded as exempting either party from its obligations under any other international, regional or bilateral agreement, and provides that any inconsistency between such other agreement and the PTA 'shall be resolved in accordance with the general principles of international law'.[51] The US agreements with Morocco, Singapore and Australia include a general provision that these agreements 'shall not be construed to derogate from any legal obligation between the Parties that entitles goods or services, or suppliers of goods or services, to treatment more favourable than that accorded' under those agreements.[52] Singapore's PTAs with Australia, Japan and Korea acknowledge the possibility of a conflict between an obligation assumed by the parties under another agreement and an obligation under the PTA and provide that, in such a situation, the parties shall consult and seek to find a mutually satisfactory solution, taking account of international law.[53] The Korea–Chile Free Trade Agreement appears to go even farther in providing that, in the event of an inconsistency between that agreement and another international agreement to which both parties are party, the Korea–Chile FTA 'shall prevail to the extent of the inconsistency, except as otherwise provided in this Agreement'.[54] The same agreement also includes a rather unique

50 NZ–Singapore CEPA, Article 58.2; Canada–Costa Rica FTA, Article 1.2.2; and CAFTA–DR–US, Article 1.2.2. The Singapore–Australia FTA also provides that panels 'shall clarify the provisions of this Agreement in accordance with customary rules of interpretation of public international law' (Chapter 16, Article 1.5).

51 NZ–Singapore CEPA, Article 80.

52 US–Morocco FTA, Article 1.2.2; US–Singapore FTA, Article 1.1.3; and AUSFTA, Article 1.1.3.

53 Singapore–Australia FTA, Chapter 17, Article 5; Japan–Singapore EPA, Article 6.1; and Korea–Singapore FTA, Article 1.3.2. However, Article 1.3.3 of the Korea–Singapore FTA adds that such general duty of consultation does not apply where there are express provisions of the Agreement regarding inconsistencies between that agreement and another international agreement. Article 18.6 of the NZ–Thailand CEPA also provides for consultations between the parties in the event that either one of them considers that there is an inconsistency between that agreement and any other agreement to which both are party.

54 Article 1.3.2.

provision deeming its SPS rules and disciplines to be consistent with the SPS Agreement.[55]

The agreement between Canada and Costa Rica also provides that it is to take precedence over any other agreement to which both countries are party 'except as otherwise provided'. That agreement then goes on to identify three multilateral environmental treaties that would prevail in the event of any inconsistency. However, the privileged position afforded the norms set out in those three environmental treaties is subject to the condition that 'where a Party has a choice among equally effective and reasonably available means of complying with such obligations, the Party chooses the alternative that is the least inconsistent with the other provisions of this Agreement'.[56] Korea's PTA with Singapore provides that its provisions on customs valuation 'shall take precedence over' the Customs Valuation Agreement.[57] Article 2(a) of the Japan–Mexico Economic Partnership Agreement (Japan–Mexico EPA) provides that 'Nothing in this subparagraph shall affect the rights and obligations of the Parties under the United Nations Convention on the Law of the Sea, as may be amended'. The PTAs to which the US is party all contain a hortatory article entitled 'Relationship to Environmental Agreements' that acknowledges the important role of multilateral environmental agreements, and commits the parties to 'continue to seek means to enhance the mutual supportiveness of multilateral environmental agreements to which they are both party and trade agreements to which they are both party',[58] and/or to consult regularly on negotiations in the WTO regarding multilateral environmental agreements and on the extent to which the outcome of such negotiations may affect those PTAs.[59] Several PTAs also provide that their provisions do not apply to tax measures and that, in the event of an inconsistency between the PTA and a tax convention, the tax convention shall prevail to the extent of the inconsistency.[60]

Lastly, it is worth noting that many of the PTAs examined contain certain rules regarding which norm is to prevail in the event of an internal conflict between chapters of the agreement.[61] As regards such conflicts within a PTA, it is quite

55 Article 8.2.3 of that Agreement reads: The framework of rules and disciplines that guide the adoption and enforcement of the sanitary and phytosanitary measures included in this Chapter is deemed to be consistent with the SPS Agreement.

56 Canada–Costa Rica FTA, Article I.4. The three treaties listed are: the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES); the Montreal Protocol on Substances that Deplete the Ozone Layer (Montreal Protocol); and the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal (Basel Convention).

57 Korea–Singapore FTA, Article 4.17(b).

58 US–Morocco FTA, Article 17.8; and AUSFTA, Article 19.8.

59 US–Morocco FTA, Article 17.8; US–Singapore FTA, Article 18.8; US–Chile FTA, Article 19.9; and AUSFTA, Article 19.8. The wording of the relevant provisions in the CAFTA–DR–US differs slightly, but appears to be of similar effect (Article 17.12).

60 CAFTA–DR–US contains one such example in Article 21.3.2.

61 The WTO contains a similar rule in the General Interpretative note to Annex 1A of the World Trade Agreement, which provides: In the event of conflict between a provision of the General Agreement on

common, in those agreements that contain chapters on investment, to include a provision to the effect that in the event of a conflict between the provisions of the chapter on investment and the provisions of any other chapter, the provisions of the other chapter will prevail.[62] In contrast, in those PTAs which contain chapters on telecommunications, it is more common to include a provision that in the event of a conflict between chapters, the chapter on telecommunications shall prevail.[63] Interestingly, Article 57.1 of the Japan–Singapore Economic Partnership Agreement (Japan–Singapore EPA) provides that in the event of a conflict between a Sectoral Annex and the provisions of the agreement dealing with mutual recognition, it is the provisions of the Annex that shall prevail.

B. Recourse to other dispute settlement fora and the consequences of choosing a forum

As mentioned above, when two countries are parties to a PTA as well as WTO Members, the same set of facts or circumstances may be actionable both in a WTO dispute settlement proceeding and using a PTA dispute settlement mechanism. Many PTAs strive to prevent the same dispute from being pursued in different fora, but the achievement of this objective is complicated by difficult questions including: when is a dispute the 'same' if the legal source of the obligations is different or the obligations themselves differ in some respects; and what is the relevance of the priority afforded to multilateral dispute settlement in Article 23 of the DSU when rights and obligations under PTAs are in dispute?

Many PTAs examined contain an express statement to the effect that the PTA does not affect the rights of the parties to the agreement to have recourse to dispute settlement available to them under other international agreements.[64] These often make clear that the choice of forum rests with the complaining party, and that once a particular dispute has been initiated under *either* the PTA or another international agreement, recourse to the other forum is precluded.[65] Notwithstanding this general

Tariffs and Trade 1994 and a provision of another agreement in Annex 1A to the Agreement Establishing the World Trade Organisation (referred to in the agreements in Annex 1A as the 'WTO Agreement'), the provision of the other agreement shall prevail to the extent of the conflict.

62 Japan–Mexico EPA, Article 69; Korea–Chile FTA, Article 10.3.1; US–Morocco FTA, Article 10.2.1; US–Singapore FTA, Article 15.3.1; AUSFTA, Article 11.2.1; and CAFTA–DR–US, Article 10.2.

63 E.g., Korea–Chile FTA, Article 12.8; US–Morocco FTA, Article 13.16; US–Singapore FTA, Article 9.15; US–Chile FTA, Article 13.16; AUSFTA, Article 12.24; and CAFTA–DR–US, Article 13.16.

64 Thailand–Australia FTA, Article 1801.2; EU–Mexico FTA, Article 47.4; Japan–Singapore EPA, Article 139.2; Japan–Mexico EPA, Article 151.1; NZ–Thailand CEPA, Article 17.1.2; and NZ–Singapore CEPA, Article 58.1. The NZ–Singapore CEPA is the only one of those listed that does not also impose a 'single exclusive forum' requirement on parties to a dispute that could be pursued under more than one agreement.

65 Thailand–Australia FTA, Article 1801.4; EFTA–Chile FTA, Article 88.1; EU–Mexico FTA, Article 47.4; Japan–Singapore EPA, Article 139.2; Japan–Mexico EPA, Article 151.2; Korea–Chile FTA, Article 19.3.2; Korea–Singapore FTA, Article 20.3.2; US–Morocco FTA, Article 20.4.1 and 20.4.3; US–Singapore FTA,

rule, some PTAs allow the parties to agree to pursue disputes simultaneously in two fora.[66] The PTAs that preclude the parties from having recourse to two different dispute settlement mechanisms typically define the 'initiation' of a dispute in the WTO context – i.e., the step that, once taken, would block recourse to the dispute settlement mechanism in the PTA – as the complaining party's request for establishment of a panel.[67] Certain PTAs also require a party planning to initiate recourse to dispute settlement under another agreement to first notify the other party of its intention to do so.[68]

PTAs containing such choice of forum clauses vary in their designation of the type of dispute that, once initiated in one forum, would preclude recourse to a second forum. Some refer to disputes on the 'same matter' or on a 'particular matter'.[69] Thailand's PTAs with Australia and New Zealand refer to 'a dispute', but clarify that the bar on having recourse to two distinct mechanisms 'does not apply if substantially separate and distinct rights or obligations under different international agreements are in dispute'.[70]

In apparent acknowledgement of Article 23 of the DSU, several PTAs expressly prohibit panels constituted pursuant to those agreements from making determinations or considering issues regarding the parties' rights and obligations under the WTO Agreement.[71] Certain PTAs seek to have the parties give priority to WTO

Article 20.4.3(a) and (c); US–Chile FTA, Article 22.3; AUSFTA, Article 21.4; CAFTA–DR–US, Article 20.3; NZ–Thailand CEPA, Article 17.1.4; and Canada–Costa Rica FTA, Article XIII.6.1 and XIII.6.4. The choice of forum rules contained in Article 22.3 of the US–Chile FTA and Article 20.3.1 of CAFTA–DR–US apply in circumstances where a dispute arises under the PTA and under 'another *free trade* agreement' (emphasis added), which may suggest that the choice afforded the plaintiff and the ensuing exclusivity of forum rule would not apply where, for example, the other available forum is under a multilateral environmental agreement. Similarly, Article 21.4 of the AUSFTA refers to 'this Agreement and under another *trade* agreement' (emphasis added).

66 Thailand–Australia FTA, Article 1801.5; NZ–Thailand CEPA, Article 17.1.5; and Japan–Singapore EPA, Article 139.4.

67 Thailand–Australia FTA, Article 1801.6; NZ–Thailand CEPA, Article 17.1.6; EFTA–Chile FTA, Article 88.3; EU–Mexico FTA, Article 47.4; Japan–Singapore EPA, Article 139; Japan–Mexico EPA, Article 151.4; Korea–Chile FTA, Article 19.3.3; Korea–Singapore FTA, Article 20.3.3; US–Morocco FTA, Article 20.4.4; US–Singapore FTA, Article 20.4.3(d); US–Chile FTA, Article 22.3.2; and Canada–Costa Rica FTA, Article XIII.6.5. A smaller number of PTAs also define the step which, if taken under the PTA in question, would trigger the 'exclusive forum' rule, which is also the request for establishment of a panel. See, e.g., Japan–Mexico EPA, Article 151.3; Korea–Singapore FTA, Article 20.3.2; US–Morocco FTA, Article 20.4.4; US–Singapore FTA, Article 20.4.3(d); and US–Chile FTA, Article 22.3.2.

68 Thailand–Australia FTA, Article 1801.3; NZ–Thailand CEPA, Article 17.1.3; EFTA–Chile FTA, Article 88.4; US–Morocco FTA, Article 20.4.2; and US–Singapore FTA, Article 20.4.3(b)

69 E.g., EFTA–Chile FTA, Article 88.1; and EU–Mexico FTA, Article 47.4;

70 Thailand–Australia FTA, Article 1801.4, and NZ–Thailand CEPA, Article 17.1.4. Similarly, Article 139.3 of the Japan–Singapore EPA and Article 151.2 of the Japan–Mexico EPA both clarify that the requirement of exclusivity of forum 'does not apply if substantially separate and distinct rights or obligations under different international agreements are in dispute'.

71 E.g., EU–SA TDCA, Article 104.10; and EU–Mexico FTA, Article 47.3. As discussed below, some PTAs also simply exclude disputes relating to certain subject areas – such as safeguards – from the scope of their dispute settlement mechanism and provide instead that such disputes are to be resolved in the WTO.

dispute settlement when WTO obligations or WTO-like obligations are at stake. Thus the EU–Chile AA provides that when one party seeks redress for a violation of an obligation under that agreement that is 'equivalent in substance' to a WTO obligation, then that party must resort to WTO dispute settlement.[72] This rule in favour of WTO dispute settlement can, however, be overcome if the parties otherwise agree. The relevant provision of the EU–South Africa Trade, Development and Co-operation Agreement (EU–SA TDCA) also pulls in opposite directions. It states that arbitration proceedings under that agreement 'will not consider issues relating to each Party's WTO rights and obligations', but allows the parties to refer any such issues to arbitration. It states that the parties 'shall endeavour to settle disputes relating to specific obligations' under the agreement through recourse to the dispute settlement procedures under that agreement, but adds that this is '[w]ithout prejudice to their right to have recourse to WTO dispute settlement procedures'.[73] The Japan–Mexico EPA specifies that nothing in its chapters on Trade in Goods, Investment, or Services shall prevent either party from applying retaliatory measures in accordance with Article 22 of the DSU.[74]

A few agreements contain special rules regarding forum in the case of disputes relating to the environment. The United States–Chile Free Trade Agreement contains a provision suggesting that environmental disputes are to be referred for action under multilateral environmental agreements rather than under that bilateral agreement. However, this is subject to the condition that the parties agree that the matter 'is more properly covered' by such other environmental agreement to which they are party.[75] The agreement between Canada and Costa Rica contains a unique provision that allows the responding party to control the forum for certain types of environmental disputes. Where the respondent's defence is based on Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES), the Montreal Protocol on Substances that Deplete the Ozone Layer (Montreal Protocol), or the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal (Basel Convention), the respondent may, within fifteen days of the complainant's initiation of dispute settlement (e.g., in the WTO), make a written request that the dispute be considered under the Canada–Costa Rica FTA. Upon receipt of such a request, the complainant is required to withdraw from participation in the other proceedings and may initiate dispute settlement proceedings under the bilateral PTA. This agreement is therefore notable because it provides for the norms set out in three listed environmental

72 Article 189.4(c). 73 Article 104.10.

74 Article 167.2 provides: Nothing in Chapters 3, 7 and 8 shall be construed to prevent either Party from taking any necessary action as may be authorised by Article 22 of the Understanding on Rules and Procedures Governing the Settlement of Disputes in Annex 2 to the WTO Agreement, as may be amended.

75 Article 19.6.10. The CAFTA–DR–US contains a similar provision in Articles 16.6.9 (relating to labour) and 17.10.9 (environment).

agreements to prevail in the event of any inconsistency, and allows the responding party to force the interpretation and application of those norms to be carried out in a dispute settlement proceeding under the bilateral trade agreement rather than, for example, in the WTO.[76]

Many of the PTAs examined also contain restrictions on the use of their own dispute settlement mechanism. The substantive areas most frequently excluded from dispute settlement are investment, competition,[77] government procurement[78] and financial services,[79] as well as 'soft' obligations on co-operation and consultation.[80] The PTAs to which the US is party and which contain obligations relating to labour and the environment often limit resort to dispute settlement and provide for special rules relating to remedies for alleged breaches of those obligations in respect of which recourse to dispute settlement is permitted.[81] Such exclusions are sometimes set out in the substantive chapters concerned, sometimes in the chapter on dispute settlement,[82] and sometimes in both. Several PTAs also impose, in specific subject areas, additional requirements of consultation or efforts to reach a mutually agreed solution before allowing recourse to the standard dispute settlement mechanism.[83]

76 Canada–Costa Rica FTA, Article XIII.3, read together with Article I.4.

77 E.g., Thailand–Australia FTA, Article 1208; EFTA–Chile FTA, Article 78; EU–Mexico FTA, Article 180; Japan–Singapore EPA, Article 105; Japan–Mexico EPA, Article 135; Korea–Singapore FTA, Article 15.8.2; Canada–Costa Rica FTA, Article XI.6.3; and Singapore–Australia FTA, Chapter 12, Article 8.2.

78 E.g., Thailand–Australia FTA, Article 1505.

79 Japan–Mexico EPA, Article 109. Although they do not preclude resort to dispute settlement regarding financial services, many PTAs impose additional requirements regarding the composition of panels and the sectors in which retaliation may be undertaken in the event of non-compliance. See, e.g., Korea–Singapore FTA, Article 12.12; US–Morocco FTA, Article 12.17; US–Singapore FTA, Article 10.18; and AUSFTA, Article 13.18.

80 E.g., Japan–Mexico EPA, Articles 138 (with respect to improvement of the business environment) and 148 (with respect to bilateral co-operation); and Korea–Singapore FTA, Article 18.1 (with respect to co-operation). Other examples include: Article 610.2 of the Thailand–Australia FTA, and Article 15 of the Japan–Mexico EPA, which preclude resort to the dispute settlement mechanism under those agreements for SPS matters; Article 1109 of that Agreement, which limits resort to dispute settlement in respect of electronic commerce; and several agreements that impose limitations where the dispute concerns provisions on the entry and temporary stay of nationals for business purposes, including an 'exhaustion of local remedies' requirement (e.g., Japan–Mexico EPA, Article 118; Korea–Chile FTA, Article 13.7.1; Korea–Singapore FTA, Article 13.6.1; US–Singapore FTA, Article 11.8.1; US–Chile FTA, Article 14.6; and Singapore–Australia FTA, Chapter 11, Article 6). Safeguards and trade remedies are also often removed from the reach of PTAs. The Canada–Costa Rica FTA, for example, does not allow its dispute settlement mechanism to be used in respect of safeguards (Article VI.4), anti-dumping measures (Article VII.1.5), and sanitary and phytosanitary measures (Article IX.5.1.2). Instead, the parties agree to use WTO dispute settlement to resolve disputes in these subject areas.

81 US–Morocco FTA, Articles 16.6.5 and 17.7.5; US–Singapore FTA, Articles 17.6.5 and 18.7.5; US–Chile FTA, Articles 18.6.7–18.6.8 and 19.6.8–19.6.9; AUSFTA, Articles 18.6.5 and 19.7.5; and CAFTA–DR–US, Articles 16.6.7–16.6.8 and 17.10.7–17.10.8. For more details on the special remedies that may be awarded in such disputes, see below.

82 E.g., Thailand–Australia FTA, Article 1801.1; and EFTA–Chile FTA, Article 87.3.

83 E.g., Japan–Singapore EPA, Article 52.4 ('Without prejudice to Chapter 21 [on Dispute Settlement], if any problem arises as to the interpretation or application of this Chapter [on Mutual Recognition], the Parties shall, first of all, seek an amicable solution through the Committee.')

C. Preclusion of a private right of action

Several PTAs expressly forbid the parties to provide for a right of action for private parties against the other party to the PTA under its domestic law for failure on the part of the latter to comply with its obligations under the PTA.[84] A number also provide that if an issue of interpretation or application of the agreement arises in a domestic judicial or administrative proceeding of one party, then that party should notify the other, and the two parties should endeavour through the joint administrative body of the PTA to submit an agreed interpretation of the PTA to the relevant court or tribunal failing which either party may, in accordance with the rules of that court or tribunal, submit its own views to that body.[85]

IV. Bringing a complaint

We now turn to several practical issues relating to how a complaint is brought. In this regard, we first offer a general overview of the dispute process. We then discuss the various types of complaints that can be made, followed by a brief consideration of whether 'proposed measures' can be challenged. Next, we examine the requirements for the documents that constitute the initiation of a dispute: the consultations and panel requests. Finally, we discuss the issue of the role of private lawyers in the process.

A. Overview of the first steps in the dispute process

The basic dispute settlement process is similar across PTAs, with several steps that come into play. Disputes always begin with a request for consultations, with consultations between the parties then taking place soon after. However, there is then a split into two groups of agreements, taking different approaches. In the first group, if the consultations do not resolve the complaint, the complaining party may then request a panel on the matter immediately.[86] This process mirrors that of the WTO.

By contrast, in the second group, if consultations fail to resolve the matter, the dispute is referred to a body headed by the parties themselves (referred to as a Joint Committee or Commission or Association Committee in various agreements).[87] The dispute will be referred to a panel only if this body cannot resolve the dispute itself. In a sense, this step forces the dispute to be examined by high-ranking officials of the parties one more time to see if a resolution can be reached. At the very least, it

84 E.g., Korea–Chile FTA, Article 19.17; US–Morocco FTA, Article 20.15; US–Singapore FTA, Article 20.10; US–Chile FTA, Article 22.20; AUSFTA, Article 21.15; CAFTA–DR–US, Article 20.21; and Canada–Costa Rica, Article XIII.20.

85 E.g., Korea–Chile FTA, Article 19.16. 86 See, e.g., Korea–Singapore FTA, Article 20.6, para. 1.

87 See, e.g., US–Singapore FTA, Article 20.4, paras. 2–4; and US–Chile FTA, Article 22.6, para. 1.

delays the process a bit to give the parties time to think more about a negotiated solution. All of the recent US agreements fall into this category.

In addition, many agreements provide for the option of good offices, conciliation or mediation. This is a less formal means of resolving disputes, in which suggestions for resolution are made by a neutral party without a finding of wrongdoing. The possibility of such a process also exists at the WTO, but the procedure has rarely been used,[88] so it is not clear how big a role it will play in PTA dispute settlement. The PTAs do not specify who would preside over the mediation. In the WTO context, the Director-General is mentioned as someone who might provide these services,[89] but there is no counterpart to the Director-General in the context of PTAs. It is possible that the WTO Director-General or someone of a similar stature could preside in the context of PTAs. In general, good offices, etc. may take place before or after the panel process has started.[90] If the parties agree, the two processes may take place simultaneously.[91]

B. Types of complaints

Under the GATT, Article XXIII provides only limited guidance on disputes. With regard to the types of complaints, paragraph 1 states the following:

> If any Member should consider that any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired or that the attainment of any objective of the Agreement is being impeded as the result of:
>
> (a) the failure of another Member to carry out its obligations under this Agreement; or
> (b) the application by another Member of any measure, whether or not it conflicts with the provisions of this Agreement; or
> (c) the existence of any other situation,
>
> . . .

Based on this language, there are a number of possible complaints that could be made under the GATT: the phrases 'any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired . . . as the result of' and 'the attainment of any objective of the Agreement is being impeded as the result of . . . ' can be paired with any of the three sub-paragraphs (a), (b) and (c), leading to six

88 To date, there has been one 'mediation' in the context of the WTO that made reference to DSU Article 5, although the parties stated that the matter was not a 'dispute' in terms of the DSU. WT/GC/66, 16 October 2002, Request for Mediation by the Philippines, Thailand and the European Communities.

89 DSU, Article 5.6.

90 Korea–Singapore FTA, Article 20.5: '[Good offices, conciliation or mediation] may begin at any time and be terminated by either Party at any time.'

91 Singapore–Australia FTA, Chapter 16, Article 3, para. 2. 'If the Parties agree, procedures for good offices, conciliation or mediation may continue while the dispute proceeds for resolution before an arbitral tribunal appointed under Article 4 (Appointment of Arbitral Tribunals)'.

possible complaints. In practice, however, the vast majority of complaints have been that 'any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired ... as the result of (a) the failure of another Member to carry out its obligations under this Agreement'. There have been a few high-profile complaints which refer to 'benefits accruing' as the result of '(b) the application by another Member of any measure, whether or not it conflicts with the provisions of this Agreement' ('non-violation' complaints) and an occasional complaint under (c) related to 'other situations' ('situation' complaints), but there is limited jurisprudence on these other types of complaints.

The PTAs covered here take several different approaches to the types of complaints that can be brought. There are usually some parallels with the GATT language, but the PTA language is never identical.

We begin with the agreements involving the US, as these all use similar language setting out several possible complaints: a measure being 'inconsistent' with the obligations of the agreement, a Party 'otherwise fail[ing] to carry out its obligations' under the agreement, or certain 'benefit[s] the Party could reasonably have expected to accrue to it under [certain designated provisions] [are] being nullified or impaired as a result of a measure that is not inconsistent with this Agreement'.[92] Some agreements have similar language, but do not limit the nullification or impairment remedy to specific provisions, but rather provide this as a general remedy.[93]

The agreements not involving the US also set out a variety of possible complaints, including: 'any matter affecting the implementation, interpretation or application' of the agreement; 'any measure or any other matter that is inconsistent with the obligations of this Agreement'; 'any measure or any other matter that ... causes nullification or impairment of any benefit accruing to it directly or indirectly' under certain provisions or as a general matter; 'any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired as a result of the failure of the Party complained against to carry out its obligations'; 'any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired, or that the attainment of any objective of this Agreement is being impeded, as a result of the failure of the other Party to carry out its obligations under this Agreement'. The various agreements include some or all of these phrases. We set out the following agreements as examples of the language used:

- *Korea–Singapore FTA*: 'any matter affecting the implementation, interpretation or application of this Agreement or whenever a party considers that any measure or any other matter that is inconsistent with the obligations of this Agreement or causes nullification or impairment of any benefit accruing to it directly or indirectly under' certain provisions.[94]

92 See, e.g., US–Morocco FTA, Article 20.2. 93 See, e.g., CAFTA–DR–US, Article 20.2, para. (c).
94 Korea–Singapore FTA, Article 20.4.

- *Singapore–Australia FTA*: 'Any Party which considers that any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired, or that the attainment of any objective of this Agreement is being impeded, as a result of the failure of the other Party to carry out its obligations under this Agreement, may, with a view to achieving satisfactory settlement of the matter, make representations or proposals to the other Party, which shall give due consideration to the representations or proposals made to it.'[95]
- *EFTA–Chile FTA*: 'A Party may request in writing consultations with another Party whenever it considers that a measure applied by that Party is inconsistent with this Agreement or that any benefit accruing to it directly or indirectly under this Agreement is impaired by such measure.'[96]

Thus, many of the elements of GATT legal complaints are also present in the PTA dispute settlements provisions, although the phrasing and order of the provisions vary. In addition, some of the PTA provisions are more general and vague than others, whereas some are more limiting in the scope of the complaints (especially with regard to the scope of non-violation nullification or impairment claims). As with GATT/WTO dispute settlement, the most prevalent form of complaint is likely to be that a party has acted inconsistently with the provisions of the agreement (there are different characterisations of this type of complaint in the various PTAs, but the essence is the same). The various other types of complaints still exist as an option where proving inconsistency is considered difficult, but their precise scope is unclear and will have to be defined through actual disputes. There is a good chance that panels faced with such complaints will look to GATT/WTO practice for guidance.[97]

C. Challengeability of proposed measures

An issue related to the types of complaints that may be brought is the scope of the 'measures' that may be challenged. In the WTO context, this is a broad topic with a number of elements.[98] We focus here on one narrow aspect: the ability to challenge 'proposed measures'. A number of agreements make reference to the term 'proposed measures', in different ways. In some agreements, consultations may be requested for both actual and proposed measures, but a panel request can only be made for actual measures.[99] By contrast, other agreements refer to the possibility of

95 Singapore–Australia FTA, Article 16.2, para. 2. 96 EFTA–Chile FTA, Article 90, para. 1.

97 In this regard, one PTA, the Chile–Costa Rica FTA, makes reference to GATT case law with respect to nullification or impairment: 'To determine the elements of nullification or impairment, the Parties may take into account the principles deriving from case law on Article XXIII, paragraph 1(b), of the GATT 1994' (Chile–Costa Rica FTA, Article 19.03 and Annex 19.03, para. 3).

98 For example, there is a great deal of debate on the scope (and even existence) of the so-called 'mandatory/discretionary' distinction.

99 CAFTA–DR–US, Article 20.4, para. 1: 'Any Party may request in writing consultations with any other Party with respect to any actual or proposed measure or any other matter that it considers might affect

consultations on actual or proposed measures, but do not explicitly exclude claims against proposed measures.[100] In this latter situation, whether a panel may be requested to examine such measures is not completely clear, but there is no express statement that this cannot happen.

In terms of policy considerations, there are a number of arguments that can be made for and against allowing challenges to proposed measures. For example, an argument against such challenges is the waste of resources in having panels consider measures that may never come into effect. On the other hand, examining such measures early on could limit trade damage where the measure would be found in violation, by recommending its removal earlier, and could also help Members ensure that their laws are consistent with trade agreements.

We also note that the scope of the term 'proposed' may be open to interpretation. A question arises as to when in the legislative or executive process a measure has been 'proposed'. Would the suggestion for a measure in a parliamentary speech qualify? Or would there have to be a more formal proposal, such as the introduction of a bill in the US Congress or the submission of regulations by a government agency for public comment? What about a measure that has been adopted by the legislature but has not yet come into force?

D. Requirements for consultations and panel requests

In the context of the WTO, the DSU contains provisions that help ensure clarity in consultations and panel requests. For example, Article 4.4 of the DSU requires that '[a]ny request for consultations shall be submitted in writing and shall give the reasons for the request, including identification of the measures at issue and an indication of the legal basis for the complaint'. Similarly, Article 6.2 of the DSU requires that '[t]he request for the establishment of a panel ... shall indicate whether consultations were held, identify the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly'. These requirements define the mandate of a panel and reflect a due process objective of giving responding parties knowledge of the case to which they are responding.

In the PTAs at issue, most agreements have requirements similar to those in the DSU, either for the consultations request or the panel request, or both. For example, with regard to panel requests, CAFTA–DR–US states that '[t]he requesting Party ... shall set out the reasons for the request, including identification of the

the operation of this Agreement'. Article 20.6, para. 6: 'An arbitral panel may not be established to review a proposed measure'.

100 See, e.g., Canada–Costa Rica FTA, Article XIII.7, para. 1: 'A Party may request in writing consultations with the other Party regarding any actual or proposed measure or any other matter that it considers might affect the operation of this Agreement'.

measure or other matter at issue and an indication of the legal basis for the complaint'.[101] Other agreements use language that is a bit more general, such as the following in the Singapore–Australia agreement: 'The request [for Arbitral tribunal] shall include a statement of the claim and the grounds on which it is based'.[102]

The interpretation and application of these provisions will quite possibly follow the same trend as in WTO dispute settlement, where challenges to panel requests are frequent and a detailed jurisprudence has developed. Given the similarities in the provisions, PTA panels may look to WTO case law for guidance.

E. Role of private counsel

An important aspect of bringing any legal complaint is which lawyers may be involved. The disputes dealt with in this chapter are, formally speaking, between governments. As a result, government lawyers, as well as other officials, are involved in all aspects of the litigation process. By contrast, the role of private lawyers in these kinds of trade disputes is less clear. In most instances, there are commercial entities involved in influencing governments to adopt measures that are the subject of trade disputes, and also in the decision to file a complaint. These commercial entities generally have lawyers advising on them on the relevant legal issues. As a result, it is natural, and perhaps unavoidable, for these lawyers to be involved in some way in the government-to-government litigation, assisting or even leading the process.

In GATT/WTO dispute settlement, private lawyers have long played a role in 'behind-the-scenes' work, such as preparing written submissions and responses to panel questions. In the early years of WTO dispute settlement, several panels and the Appellate Body ruled that these private lawyers could participate in panel meetings and Appellate Body oral hearings as well, thus crossing the 'final frontier' of private lawyer participation in trade disputes.[103] Today, private lawyers can and do play a role in all aspects of WTO proceedings, and are bound by the same rules (e.g., confidentiality) as government lawyers.

For the most part, the PTAs examined here do not address explicitly the issue of the role of private lawyers. It is almost a certainty that the 'behind-the-scenes' type work done by private lawyers is permissible, as there would be no way to monitor or stop it even if that were desired. With regard to the participation of private lawyers in panel hearings, it is probably a safe assumption that this will be permitted, on the basis of the same reasoning used in the context of the WTO. There are occasional

101 CAFTA–DR–US, Article 20.6, para. 1. 102 Singapore–Australia FTA, Article 16.4.
103 See Appellate Body Report, *EC–Bananas III*, paras. 5–12; and Panel Report, *Indonesia–Autos*, paras. 14.1–14.2.

exceptions to this general rule, though. For example, in the Model Rules for the European Union–Mexico Free Trade Agreement, it is stated:

> The following persons may attend a hearing:
> . . .
> (b) advisers to a Party, provided that they do not address the arbitration panel and provided further that neither they nor their employers, partners, business associates or family members have a financial or personal interest in the proceeding;[104]

An 'adviser' is defined in paragraph 1 as 'a person retained by a party to advise or assist the Party in connection with the arbitration panel proceeding'. Thus, this provision appears to limit the role of private lawyers during the hearing, allowing them to attend the hearing but not permitting them to speak to the panel. Presumably, however, they can discuss issues with the government counsel during the hearing and offer advice on what to say. The reasons for the approach taken in this agreement are not clear, and most other agreements do not seem to have similar language.[105]

V. Selection procedures for panels/tribunals

Various names are given to the group of 'judges' who hear complaints under PTAs: Panel, Arbitration Panel, Arbitral Panel, Arbitral Tribunal and Arbitration Tribunal. For ease of reference, we will refer to these bodies using the term 'Panel', the term used at the WTO, except where necessary to distinguish among them. In this section we discuss a number of issues related to the process parties follow when selecting members of these panels.

A basic question at the outset is, how many people serve on a panel? Virtually all PTAs specify that the Panel shall be composed of three members, with one member serving as Chair. However, there are a couple of PTAs involving the US that establish three as the default number but allow the parties to agree on a different number.[106] In addition, a slightly older FTA, from 1997 between Canada and Chile, establishes a five member panel.[107]

With regard to the process of selecting individuals to serve on a panel, there are several key issues, some of which overlap to an extent:

(1) whether a 'roster' or 'list' of possible panellists is to be maintained;
(2) qualifications and requirements for panel service;

104 EU–Mexico FTA, Annex XVI to Decision No. 2/2000 of the EC–Mexico Joint Council of 23 March 2000, para. 25; see also Decision of the Joint EFTA–Singapore Committee No. 2 of 2004, adopted on 26 May 2004, para. 23; and Decision of the EFTA–Mexico Joint Committee No. 3 of 2002, adopted on 22 October 2002, para. 25.

105 In contrast to the limiting language in the EFTA–Singapore and EFTA–Mexico agreements, the EFTA–Chile Model Rules allow for advisers to address the panel. See Annex XVII, para. 20.

106 See, e.g., AUSFTA, Article 21.7, para. 3. 107 Canada–Chile FTA, Article N-11, para. 1.

(3) the appointment process;
(4) procedures to prevent parties from blocking the appointment process.

We discuss each issue in turn.

1. Roster or list

About half of the agreements examined provide for a 'roster' or 'reserve list' or 'contingent list' of people who can serve on panels. These 'rosters' and 'lists' are made up of qualified candidates, and are to be referred to in the panel composition process. Generally speaking, but not in all cases, where the term 'roster' is used the agreement indicates that the panellists are 'normally' to be selected from the roster.[108] In addition, many of these agreements state that a party 'may exercise a peremptory challenge against any individual not on the roster who is proposed as a panellist by the other disputing Party'.[109] By contrast, where a 'contingent' or 'reserve' list is used, the list is used to help fill slots when the parties are having difficulty agreeing on panellists.[110] For these agreements, it is up to the parties to propose candidates for panel service, with no limitations on choosing candidates aside from the various qualifications and requirements described in the next section.

The number of people included on the 'roster' or 'list' ranges considerably, from five[111] to 70[112] in the agreements examined. The duration of the list is usually a specific period, e.g. three years, and the persons on the list may be re-appointed. Often some number of people on the roster/list must be nationals of one of the parties, whereas another group is required to be non-nationals of either party.

2. Qualifications

The panellists chosen must meet certain qualifications. There are three broad categories in this regard: expertise, character and nationality. In terms of expertise, most agreements include a requirement to the effect that panellists have 'expertise or experience in law, international trade, other matters covered by this Agreement or the resolution of disputes arising under international trade agreements'.[113] Others are sometimes more general, such as the Japan–Singapore EPA, which requires only 'relevant technical or legal expertise';[114] or more specific, such as the NZ–Singapore CEPA, which states that, in addition to having 'relevant technical or legal expertise', they 'must be a well-qualified governmental or non-governmental individual, and can include persons who have served on or presented a case to a WTO panel, served in the Secretariat of the WTO, taught or published on international trade law or policy, or served as a senior trade policy official of a Member of the

108 See, e.g., Chile–Costa Rica FTA, Article 19.11, para. 3.
109 See, e.g., Canada–Chile FTA, Article N-11, para. 2.
110 See, e.g., US–Singapore FTA, Article 20.4, para. 4(a).
111 *Ibid*., para. 4(b). 112 CAFTA–DR–US, Article 20.7, para. 1.
113 See, e.g., NZ–Thailand CEPA, Article 17.5, para. 6(a). 114 Japan–Singapore EPA, Article 143, para. 7.

WTO'.[115] This latter provision mirrors Article 8.1 of the DSU. Finally, one agreement prefers a diverse group, noting that '[t]he members shall have sufficiently diverse background and a wide spectrum of experience'.[116]

With regard to character, the provisions do not vary much, usually stating that the panellists be chosen on the basis of factors like objectivity, reliability, sound judgement, independence and impartiality, and requiring that panellists comply with a code of conduct.

Finally, nationality requirements vary considerably. Some agreements include only a general requirement that panellists serving as the Chair 'be independent of, and not be affiliated with or take instructions from, any Party'.[117] This does not appear to make nationality a criterion for service, as it focuses more generally on the panellist's independence from the governments involved. Other agreements, however, do set nationality restrictions, especially with regard to the Chair, requiring, for example, that the Chair not be a national of, and shall not have his or her usual place of residence in the territory of, nor be employed by, either Party.[118]

3. The appointment process

With regard to the appointment process, there are various approaches that have been taken. With most agreements, the disputing parties each appoint a member of the panel. Then, the parties either try to decide jointly on a third member to Chair the panel, or the first two members pick the Chair. For other agreements, by contrast, the parties pick the Chair first. The time frames for appointment vary somewhat.

4. Blocking the appointment process

An important aspect of the appointment process is whether the rules prevent the party complained against from blocking the establishment of a panel by refusing to take required actions. It has been alleged that blocking of the appointment process for a panel was a problem in a NAFTA dispute between the US and Mexico on sugar imports.[119]

Most of the agreements examined prevent blocking, using a variety of means to do so. For example, the following provisions have been used in this regard:

- *CAFTA–DR–US*: If the parties cannot agree on a Chair, the Chair shall be selected 'by lot' from 'among the roster members who are not nationals of a disputing Party'. Similarly, if a party fails to select a panelist within the designated period,

115 NZ–Singapore CEPA, Article 61, para. 5. 116 EFTA–Chile FTA, Annex XVII, para. 49.
117 See, e.g., US–Morocco FTA, Article 20.7, para. 5(b).
118 See, e.g., EFTA–Singapore FTA, Article 60, para. 6.
119 See Mexico's arguments in this regard as part of a WTO proceeding on a related mater. Panel Report, *Mexico–Taxes on Soft Drinks*, para. 4.223.

the panellist 'shall be selected by lot within three days from among the roster members who are nationals of such Party or Parties'.[120]

- *New Zealand–Thailand CEPA*: If within the time periods for appointment 'the necessary appointments have not been made', either Party may invite the President of the International Court of Justice to make the appointments (a less senior member of the ICJ may take on this task if the President is a national of either Party).[121]
- *Korea–Chile FTA*: If the Parties are unable to agree on the Chair, the chairperson of the Commission for the agreement shall select by lot the Chair of the panel from among the roster members who are not nationals of either Party; similarly, if a Party does not select its panellist, the chairperson of the Commission shall select by lot the panellist, from among the roster members who are nationals of that Party. [122]
- *EFTA–Singapore FTA*: If the panel members and Chair have not been appointed within the mandated time periods, 'the necessary designations shall be made at the request of any Party to the dispute by the Director-General of the World Trade Organization'.[123]

Thus, some agreements arrange for automatic appointment of panellists from the 'rosters' and 'contingent/reserve lists' that were created (or in some instances from the candidates proposed), whereas others provide for an outsider to appoint the panellists.

Some agreements do not explicitly provide for a means to prevent blocking. For example, the Korea–Singapore FTA provides: 'Each Party shall appoint a member within thirty (30) days of the receipt of the request under Article 20.6'.[124] Thus, there is no means for ensuring that parties appoint a member (although there is such a means for the selection of the Chair in that agreement). It remains to be seen how language of this sort will be interpreted and applied. It may be possible that the parties will not engage in or allow this kind of blocking even though no explicit language prevents the tactic.

VI. The panel process

Once the panel has been appointed, the next step is to begin the dispute process, which, like any legal process, involves written submissions and a hearing before the panel. In this section, we discuss several aspects of the process: the timetable for reports; the existence of working procedures for the panel; the existence of an interim report; treaty interpretation; the ability of the panel to seek expert advice; external transparency of the panel process, that is, the ability of non-parties to

120 CAFTA–DR–US, Article 20.9, para. 1(b). 121 NZ–Thailand CEPA, Article 17.5, para. 3.
122 Korea–Chile FTA, Article 19.9, paras. 3 and 4. 123 EFTA–Singapore FTA, Article 60, para. 5.
124 Korea–Singapore FTA, Article 20.7, para. 1.

participate and observe; the panel voting process; and the ability of the panel to make recommendations to help resolve the dispute.

A. Timetable for reports

All PTAs attempt to set limits on the length of the panel process, in the interest of a speedy resolution of disputes. Usually, the agreements set out a time period for issuance of the interim report to the parties, a short additional time for issuance of the final report to the parties, and then a shorter additional time for circulation of the report to the public. For example, CAFTA–DR–US establishes time periods of 120 days between panel selection and issuance of the interim report; thirty additional days for issuance of the final report to the parties; and fifteen additional days for circulation of the final report to the public.[125] Some agreements have slightly longer time periods, while some are slightly shorter.

WTO dispute settlement procedures have similar limits. However, at the WTO these limits are not met in many cases. This is largely due to the complexity of many disputes, the increasing number of disputes involving large numbers of claims, and the time needed for translation of reports into all three official WTO languages. While the latter may not be an issue in PTAs, the other issues might lead to similar delays. As a result, it remains to be seen whether these time limits will be respected.

B. Existence of panel working procedures

The dispute settlement provisions of most agreements provide only some basic information on the procedures to be followed in disputes. Most of the agreements surveyed attempt to supplement these rules with detailed procedures to be followed in the form of 'Model Rules of Procedure', available in an Annex to the agreement. However, while many agreements refer to such Model Rules in their text, only a few of these agreements appear to have actually developed such rules at the time of this writing.[126]

In the context of the WTO, both the Appellate Body and panels have working procedures they follow. The Appellate Body has an established set of rules it follows each time,[127] while individual panels adjust theirs for each dispute.[128]

C. Interim report

During the Uruguay Round of GATT negotiations, two innovations were added to dispute settlement in the hopes of improving the quality of reports: issuance of an

125 CAFTA–DR–US, Article 20.14 and 20.15. 126 See, e.g., EFTA–Chile FTA, Annex XVII.
127 Working Procedures for Appellate Review, WTO Doc. No. WT/AB/WP/5 (4 January 2005).
128 Appendix 3 of the DSU sets out basic procedures for panels to follow, but over the years panels have modified these procedures to address a number of issues that have arisen.

'interim report' to the parties, on which they could provide comments; and an appeal mechanism. The use of interim reports gives parties the chance to offer additional insights to the panel before the process is completed, allowing the panel to provide better reasoned opinions. The appellate mechanism gives a new group of judges a chance to review the reasoning of the panellists.

In PTAs, while there is no appeal process, the interim report mechanism has generally been used. This report is normally referred to as the 'initial' report, although it is sometimes called a 'draft'. A short period of time, usually fourteen days, is allotted for the parties to provide comments on the initial report.

In WTO dispute settlement, there has been fairly extensive use of the interim review process. The parties appear to offer quite a few substantive criticisms, as well as more basic suggestions such as corrections of typographical errors. In many instances, panels will offer further explanations of their views in response to the parties' substantive criticisms, but they rarely change their findings. In two disputes, panels have actually changed their findings at the interim review stage.[129]

There have been suggestions that parties in WTO disputes are reluctant to provide too much in the way of substantive criticism of panel reports during the interim review stage, due to the fear that a panel may shore up its reasoning, thus making an appeal of the issue more difficult. There is some logic to this view, although whether it is true as an empirical matter is not clear. Regardless, the situation is different in PTAs, as there is no appeal process. Thus, parties will likely set forth detailed criticisms as part of this process. At the very least, it offers a defending party who expects to lose a chance to extend the process a bit.

D. Treaty interpretation

Article 3.2 of the DSU states that clarification of WTO rules is to be carried out in accordance with 'customary rules of interpretation of public international law'. Virtually everyone agrees, and the jurisprudence clearly establishes, that such interpretation should be based on Articles 31 and 32 of the Vienna Convention on the Law of Treaties (Vienna Convention).[130]

For the PTAs covered here, some, but not all, specify treaty interpretation rules, but there is some variety in the way they do it.[131] Many PTAs state that interpretation is to be 'clarified' under the 'customary rules of interpretation of public international law', or 'interpreted' under the 'applicable rules of international law' or the 'customary rules of interpretation of public international law'. One agreement, the Australia–United States Free Trade Agreement (AUSFTA), refers to the 'rules of interpretation under

129 See Panel Report, *US–Carbon Steel*, paras. 7.24 and 8.133–8.145; and Panel Report, *Korea–Paper AD Duties*, paras. 6.3–5 and 7.108–111.

130 Of course, while the general interpretative principles are agreed upon, the specific application of these rules is often contested.

131 Agreements involving the US and Canada tend not to specify any such rules, whereas most others do.

international law as reflected in Articles 31 and 32 of the Vienna Convention on the Law of Treaties'.[132] On occasion, agreements also refer to the 'objectives' of the agreement as a basis for interpretation and application of the provisions.[133]

With regard to those PTAs that do not specify any such rules, the panels may have a bit more flexibility in terms of the interpretation rules they apply, but most likely they will gravitate towards rules that are the same as, or similar to, those in the Vienna Convention.

E. Expert advice

Like Article 13 of the DSU, most PTAs allow panels to request additional information to help them decide a case. Generally, PTAs state that panels may request this information upon the request of a party or on their own initiative, and the panel's request may be made to any person or body in relation to any information or technical advice.[134] Some agreements do provide limitations, such as requiring that the parties agree to the process[135] and be permitted to submit comments.[136] Others limit the scope of the information at issue to 'scientific information and technical advice from experts'[137] or provide separate, additional provisions on scientific/technical information.[138] Aside from these few limitations, however, these provisions are quite broad in terms of the scope of the information that may be requested.

F. External transparency

'External transparency' is a term that refers to making the procedures of an agreement, both in regard to disputes and other decision-making, accessible to those outside the government of the state parties. In relation to disputes, there are three aspects of this idea that have been included in various agreements: making panel hearings open to the public; making the parties' submissions to the panel available to the public; and allowing non-governmental entities to make *amicus curiae* submissions to the panels.

1. Open panel hearings

The recent PTAs involving the US indicate that the panel hearings shall be open to the public, subject to provisions on protecting confidential information.[139] Agreements to which the US is not party tend not to have explicit provisions of this kind, although it is

132 AUSFTA, Article 21.9, para. 2. 133 See Korea–Singapore FTA, Article 20.2, para. 5.
134 See, e.g., CAFTA–DR–US, Article 20.12: 'On request of a disputing Party, or on its own initiative, the panel may seek information and technical advice from any person or body that it deems appropriate, provided that the disputing Parties so agree and subject to such terms and conditions as such Parties may agree.'
135 *Ibid.* 136 NZ–Thailand CEPA, Article 17.7. 137 EFTA–Singapore FTA, Article 61.
138 Korea–Singapore FTA, Article 20.10, para. 2. 139 See, e.g., CAFTA–DR–US, Article 20.10.

possible that the parties could agree to open panel hearings for a particular dispute if they chose to do so. One agreement states that hearings are to be closed to the public 'unless the Parties decide otherwise', and notes that if hearings are opened to the public 'part of the hearing may ... be closed to the public' and the hearing shall be closed if business confidential information is at issue.[140]

2. Making submissions public

Generally speaking, most PTAs make clear that parties can make their own written submissions to the panel available to the public, provided that they ensure that any confidential information of another Party is not disclosed. For example, the NZ–Thailand CEPA states: 'Nothing in this Article shall preclude a Party from disclosing to the public statements of its own positions or its submissions, but a Party shall not disclose information submitted by the other Party to an arbitral tribunal which the latter Party has designated as confidential'.[141] Agreements involving the US go even further, *requiring* that various submissions be made public (confidential information excepted).[142] Finally, the Korea–Singapore FTA provides that the transcript of the hearing can be made available as well,[143] something that does not occur in WTO dispute settlement.

3. Allowing *amicus curiae* submission

In WTO dispute settlement, the acceptance and consideration of *amicus curiae* submissions has been very controversial. The Appellate Body has ruled that these submissions may be taken into account in appellate proceedings[144] and by panels,[145] but the issue is a sensitive one and most panels and Appellate Body divisions receiving such submissions explicitly make a statement to the effect that they did not find it necessary to take the submissions into account.[146]

Several PTAs provide explicit rules on this issue. For example, CAFTA–DR–US provides that 'the panel will consider requests from non-governmental entities in the disputing Parties' territories to provide written views regarding the dispute that may assist the panel in evaluating the submissions and arguments of the disputing Parties'.[147] All of the other US PTAs contain similar language. The Korea–Singapore FTA also has such language, but instead uses the words 'may consider', giving the panel some additional discretion.[148]

140 EFTA–Chile FTA, Annex XVII, para. 22. 141 NZ–Thailand CEPA, Article 17.7, para. 2.
142 See, e.g., CAFTA–DR–US, Article 20.10, para. 1(c): '[E]ach participating Party's written submissions, written versions of its oral statement, and written responses to a request or questions from the panel shall be public.'
143 Korea–Singapore FTA, Annex 19.10, para. 36(b).
144 Appellate Body Report, *US–Lead and Bismuth II*, paras. 36–42.
145 Appellate Body Report, *US–Shrimp*, paras. 99–110.
146 See, e.g., Appellate Body Report, *Mexico–Taxes on Soft Drinks*, para. 8.
147 CAFTA–DR–US, Article 20.10, para. 1(d). 148 Korea–Singapore FTA, Article 20.9, para. 1(e).

There are two key aspects of these provisions. First, panels need only 'consider' requests to make *amicus* submissions. They are not required to grant such requests, although presumably they must consider the request in good faith and provide some reasoning as to their decision. And second, only entities 'in the disputing Parties' territories' may make these submissions. It is not clear how much of a restriction this will be in practice, as an organisation interested in the issue could probably set up a new office in one of the disputing parties or find an entity located within a disputing party to make the submission on its behalf.

Finally, the EFTA–Chile FTA goes into more detail than other agreements, placing a number of conditions on *amicus* submissions. This agreement requires that such submissions be made 'within 10 days following the date of the establishment of the arbitration panel, that they are concise and in no case longer than 15 typed pages, including any annexes, and that they are directly relevant to the factual and legal issue under consideration by the panel'. Furthermore, the submission must 'contain a description of the person, whether natural or legal, making the submission, including the nature of its activities and the source of its financing, and specify the nature of the interest that that person has in the arbitration proceeding', and 'shall be made in English and Spanish languages'. Even if these conditions are fulfilled, though, the panel 'shall not be obliged to address, in its ruling, the factual or legal arguments made in such submissions'.[149]

Of course, where no rules are provided, it may still be possible for panels to take such submissions into account, as there are no explicit rules on this in the WTO either, and the Appellate Body nevertheless decided, based on various contextual provisions, that these submissions were allowed.

G. Panel voting

As noted above, there are generally three members on a panel, as is also the case at the WTO. As a result of this structure, several questions arise: Should decisions be made by consensus or majority vote? May panellists issue separate opinions? And where separate opinions are issued, are they to be attributed to specific panellists or remain anonymous?

Most agreements have something to say about some of these questions, but rarely are all three covered. Some agreements encourage consensus but allow for majority voting;[150] others simply assume that sometimes the decision will be based on majority voting;[151] still others just require a majority vote.[152]

149 EFTA–Chile FTA, Annex XVII, paras. 34–6.

150 See, e.g., Korea–Singapore FTA, Annex 20a, para. 20: 'The panel shall take its decisions by consensus; provided that where a panel is unable to reach consensus it may take its decisions by majority vote.'

151 See, e.g., CAFTA–DR–US, Article 20.13, para. 5: 'Panelists may furnish separate opinions on matters not unanimously agreed.'

152 See, e.g., Japan–Mexico EPA, Article 154, para. 7: 'The arbitral tribunal shall take its decisions including its award by majority vote.'

Some agreements state explicitly that where members disagree, a separate opinion may be issued.[153] While not all refer to this possibility, it may simply be assumed that this can be done, and it is not prohibited expressly in any agreement. Where separate opinions are to be issued, it is always indicated that the individual opinions are not to be attributed to specific panel members.[154]

H. Recommendations

Most of the PTAs covered make some reference to a panel making recommendations to the parties in the event of a finding of violation. Such a recommendation goes beyond simply 'bringing the measure into conformity'. Rather, this kind of recommendation relates to 'resolution of the dispute' or, in several agreements, 'suggested implementation options for the Parties to consider'.[155] In all agreements, the panel is not required to make such a recommendation, but simply has the discretion to do so. For some agreements, it is up to the panel whether to make any recommendations; for other agreements, a panel may do so only if the parties agree.[156]

VII. Implementation

Once the DSB adopts panel and Appellate Body reports containing findings of inconsistency, the WTO Member whose measure has been found to be inconsistent becomes subject to various obligations with respect to implementation. Article 3.7 of the DSU sets out certain relevant principles, namely that, in the absence of a mutually agreed solution, the withdrawal of a measure found to be inconsistent is the desired outcome, that compensation is to be temporary and only resorted to when the immediate withdrawal of the inconsistent measure is impracticable, and that the suspension of concessions is considered the 'last resort' of a complaining Member and is subject to DSB authorisation. Articles 21 and 22 of the DSU, entitled 'Surveillance of implementation of recommendations and rulings' and 'Compensation and the suspension of concessions', respectively, set out the detailed mechanics of implementation. These include: how the reasonable period of time for implementation is to be determined; the procedure to be followed when the parties to a dispute

153 See, e.g., EFTA–Singapore FTA, Article 61, para. 6: 'Panellists may furnish separate opinions on matters not unanimously agreed.'

154 See, e.g., EFTA–Singapore FTA, Article 61, para. 6: 'No arbitration panel may disclose which panellists are associated with majority or minority opinions.'

155 See, e.g., Japan–Singapore EPA, Article 144, para. 1(d).

156 The Korea–Singapore FTA says that panels are to provide 'recommendations, if any, on the means to resolve the dispute' (Article 20.11, para. 2(c)); by contrast, CAFTA–DR–US provides that the report shall contain 'recommendations, if the disputing Parties have requested them, for resolution of the dispute' (Article 20.13, para. 3(c)).

disagree over whether implementation has occurred; the reporting (by the Member whose measure has been found inconsistent) and monitoring (by the DSB) of implementation; the procedures and principles that are to be followed in the event that compensation or the suspension of concessions is sought; and associated procedures and timeframes.

Articles 21 and 22 of the DSU are often pointed to as containing certain lacunae,[157] and as ripe for improvement. They have been the subject of many proposals and much discussion in the context of the ongoing negotiations on reform of the DSU, as well as of much academic commentary. Interestingly, variants of several of the proposals that have been made during these WTO negotiations have been adopted in some PTAs. Overall, however, most PTAs follow the WTO implementation model fairly closely, with a few additional innovations or improvements.

A. Start of the implementation phase

In WTO dispute settlement, the step that triggers the implementation process and associated obligations is the adoption of a panel and, if applicable, Appellate Body report by the DSB. This step has no equivalent in any of the PTAs examined. The Turkey–Morocco Free Trade Agreement does, however, appear to interject an additional step between the delivery of a panel report to the parties and the triggering of implementation obligations. Paragraph 7 of Article 33 of that Agreement requires the Joint Committee, to which the final panel report is presented, to 'take a decision to settle the dispute on the basis of the final report of the panel' and requires the parties 'to take the necessary steps required to implement this decision'. The following paragraph reinforces that it is the decision of the Joint Committee (rather than the panel report directly) with which the parties must comply, and also implies that such a decision will also set out the measures that may be taken by a complaining party in the event of non-implementation of such decision.[158] In most PTAs, however, the implementation phase begins upon the receipt by the parties of the report of the panel. In many cases it is the receipt of this report that starts the clock for the notification(s) required of responding parties whose measures have been found to be inconsistent. Several PTAs expressly state that the parties are bound by the final report and/or required to take the implementation measures necessary to comply with the ruling, and many also require the parties to consult in an effort to agree on specific implementation

157 In particular the so-called 'sequencing' issue, or the fact that Articles 21 and 22 do not address the temporal relationship between compliance proceedings under Article 21.5, on the one hand, and negotiations for compensation and arbitration proceedings under Article 22, on the other.

158 Turkey–Morocco FTA, Article 33.8 provides that 'If the Party complained against fail[s] to implement [. . .] the decision mentioned in paragraph 7 of this article, the complaining Party shall be entitled to take measures in line with the decision of the Joint Committee'.

measures.[159] Korea's agreements with Chile and Singapore expressly state that a panel's final report shall not be subject to appeal.[160]

B. The period of time allowed for implementation

Many PTAs mirror the DSU in providing that compliance with recommendations and rulings is to be 'prompt'. Like the DSU, most set out a mechanism for determining what the period of time for implementation should be in a specific dispute. In the majority of cases, this period is to be determined either by mutual agreement of the parties to the dispute or through recourse to the original panel.[161] Some envisage a single arbitrator making this determination, with the relevant individual to be selected either on agreement of the parties or by lot among the original panellists.[162] A few PTAs provide that the reasonable period of time is to be notified by the responding party (sometimes subject to guidelines) and that, if such period is not acceptable to the complaining party, then either: that complainant retains the option of referring the issue to the original panel;[163] or the parties are to enter into consultations on the issue.[164] Some PTAs do not prescribe a time within which the reasonable period of time for implementation must be set,[165] and some simply state that, if a party considers prompt compliance impracticable, then the parties must enter into consultations with a view to developing a mutually acceptable resolution and a reasonable period to implement such resolution.[166]

The PTAs to which the US is party are silent on the issue of the period of time for implementation. This may be an issue on which the parties could agree to request the panel to make a determination on in its initial report,[167] even though it is not

159 EU–Mexico FTA, Title VI, Chapter III, Article 46.4; and US–Morocco FTA, Article 20.10.1 (the parties 'shall agree on the resolution of the dispute, which normally shall conform with the determinations and recommendations, if any, of the panel'). See also US–Singapore FTA, Article 20.5.1; US–Chile FTA, Article 22.15.1; AUSFTA, Article 21.10.1; and CAFTA–DR–US, Article 20.15.1.

160 Korea–Chile FTA, Article 19.14.1; and Korea–Singapore FTA, Article 20.13.1.

161 Article 20.13.2(b) of the Korea–Singapore FTA and Article 46.4 of Chapter III of the EU–Mexico FTA require the tribunal to determine the reasonable period of time within fifteen days of a request from a party.

162 See Canada–Costa Rica FTA, Section II, Article XVIII.16, Article 2(b) and footnote thereto.

163 Japan–Mexico EPA, Chapter 15, Article 156.2; EU–Chile AA, Article 188.3 and 188.4; and EFTA–Chile FTA, Chapter X, Article 96.3 and 96.4.

164 Japan–Singapore EPA, Chapter 21, Article 147.1(c).

165 See Turkey–Morocco FTA, Chapter 16, Article 9.1; and Korea–Singapore FTA, Article 20.13.2(b), which sets no time limit for the agreeing of a reasonable period of time, but allows either party to request the original panel to make such a determination and allows only fifteen days for the panel to do so.

166 NZ–Thailand CEPA, Article 17.10.3.

167 The relevant agreements authorise the parties to agree to request the panel to make 'any other determination' or recommendation. This would seem to encompass the possibility of asking a panel to make a determination as to the period of time for implementation – provided that the parties agree. See

expressly identified as such.[168] In the PTA between Korea and Chile, parties are directed to implement the final report of the panel 'within the time-frame that it orders', which implies that the panel is empowered or expected to set implementation deadlines.[169]

As regards the length of the reasonable period of time for implementation, some PTAs follow the DSU in setting fifteen months as an outside guideline, or as the default period which may be modified by mutual consent.[170] The Japan–Singapore EPA provides that the period may 'extend to twelve months only if administrative or legislative measures have to be undertaken' but also allows this period to be extended or shortened if the parties agree that such modification is warranted by special circumstances.[171] The NZ–Singapore CEPA states that the period shall not exceed twelve months unless the responding party advises the complainant that 'primary legislation' is required for implementation, in which case the period is not to exceed fifteen months.[172] Quite a few PTAs are altogether silent on the issue.

C. Notification obligations and surveillance of implementation

Given that very few PTAs contemplate that a joint body will administer dispute settlement, there is little 'surveillance' of implementation that corresponds to the role of the DSB in this regard in the WTO. Yet a large number of PTAs do impose notification obligations on parties whose measures have been found by a panel to be inconsistent. The notification requirements generally attach shortly after receipt of the panel report and, in some cases, once the implementing measure has been adopted. A few PTAs also prescribe in some detail what such notifications must contain.

1. Prior to implementation

Several PTAs require responding parties found to have acted inconsistently to notify their intentions regarding implementation.[173] Some contain fairly specific details as to the required content of such notifications, including the reasonable period of time needed for implementation, the specific implementation measures, and a 'concrete

CAFTA–DR–US, Article 20.10.6; AUSFTA, Article 21.10.1; US–Chile FTA, Article 22.14.1, US–Singapore FTA, Article 20.5.1; and US–Morocco FTA, Article 20.10.1.

168 In contrast, the US–Chile FTA and CAFTA–DR–US expressly identify a finding as to the degree of adverse trade effects caused by a measure found to be inconsistent as an issue on which a party may request a panel to make a finding, and require the panel's terms of reference to reflect such a request. (US–Chile FTA, Article 22.10(6); CAFTA–DR–US, Article 20.10(6)).

169 Korea–Chile FTA, Article 19.14.1. Neither the provisions of that Agreement nor the Model Rules of Procedure annexed to it specifically mention that a panel may, or may be requested to, fix a reasonable period of time for implementation, although Rule 7 of the Model Rules allows a party to request the panel to make findings as to the degree of adverse trade effects of an inconsistent measure.

170 EU–SA TDCA, Article 104.9(e). 171 Chapter 21, Article 147.1. 172 Part 10, Article 65.

173 E.g., Thailand–Australia FTA, Article 1810.2; and NZ–Thailand CEPA, Article 17.10.2.

proposal' for 'temporary compensation' until full implementation has been achieved.[174] A time limit of thirty days following receipt of the panel report is the norm for notifications of implementing action,[175], although only twenty days is typically allowed if the only matter to be notified is the period of time proposed for implementation.[176]

The agreement between Canada and Costa Rica sets out additional notification/reporting obligations. Like Article 21.6 of the DSU, that agreement requires a responding party that has not yet achieved implementation to provide periodic status reports.[177] In addition, if that party has not already notified the other of compliance it is under an obligation, no later than twenty days before the expiry of the reasonable period of time, to provide a written notification of the measures that it has taken or expects to have taken by the end of the reasonable period of time.[178]

2. Upon implementation

A few PTAs require a responding party to notify its implementing measure to the complainant.[179] The Canada–Costa Rica FTA contains rather detailed notification obligations regarding a party's implementation measures. The notification must 'include a detailed description as well as the text of the relevant measures the Party complained against has taken', or the measures that it expects to take before the end of the reasonable period of time.[180]

D. Compliance disputes and the 'sequencing' problem

Within the WTO, the brief two sentences that comprise Article 21.5 of the DSU have raised a number of questions regarding compliance disputes. In the earlier years of WTO dispute settlement, most of the questions related to two broad themes: (1) What is the relationship between compliance proceedings under Article 21.5 and the various proceedings contemplated under Article 22 of the DSU – the so-called 'sequencing' issue, discussed below? and (2) Which aspects of an original dispute settlement proceeding are encompassed by the phrase 'these dispute settlement procedures' and may or must therefore form part of a compliance proceeding?[181]

174 EFTA–Chile FTA, Article 96.3; and EU–Chile FTA, Article 188.3.

175 EU–SA TDCA allows 60 days for such notification (Article 104.9(b)).

176 Japan–Mexico EPA, Article 156.2; and Japan–Singapore EPA, Article 147.1.

177 Canada–Costa Rica FTA, Article XIII.16.4(b), requires such status reports to be provided, beginning six months after the date of the final panel report, until such time as the parties agree, or a compliance panel finds, that compliance has been achieved.

178 Canada–Costa Rica FTA, Article XII.16.(c)(ii). 179 E.g., EU–Chile AA, Article 188.5.

180 Article XIII.16.4(c)(iii).

181 Thus, in the early years of WTO dispute settlement Members expressed differing opinions as to whether consultations on an implementing measure were required before the consistency of that measure could be referred to a compliance panel, and as to whether an appeal was possible in proceedings under Article 21.5 of the DSU.

Over time, WTO Members have managed to conduct their disputes notwithstanding the apparent lacunae or ambiguous language in the relevant DSU provisions, often on the basis of bilateral agreements between the parties. Yet, in what seems probably the result of a heightened awareness of the uncertainties associated with Articles 21 and 22, several recent PTAs include provisions that seem designed to clarify the sequence of and steps involved in compliance proceedings. More recently within the WTO, a number of compliance proceedings have raised issues relating to possible limits that may apply to the scope of proceedings under Article 21.5 of the DSU, and concerning the relationship between Article 21.5 proceedings and original panel proceedings. So far, such issues have arisen in specific disputes and been decided as necessary by panels and the Appellate Body. Such issues have not been expressly dealt with in the text of the PTAs examined.

1. Compliance procedures

A few of the less detailed PTAs make no express reference to the issue of compliance.[182] This is also true of the Korea–Chile FTA, even though that agreement has a more elaborated dispute settlement mechanism. It is not clear on the face of the agreement whether implementing measures alleged to be inconsistent would be subject to new dispute settlement proceedings or whether the authority which the agreement gives to a panel asked to determine 'whether the level of benefits suspended by the complaining Party is excessive' would imply authority, as well, to examine the consistency of an implementing measure.[183]

A small number of PTAs explicitly address the issue – which has been controversial in the WTO context – of whether it is necessary to engage in consultations before referring a compliance measure to a compliance panel. The Canada–Costa Rica FTA states that while consultations are 'desirable, they are not required prior to a request for a compliance panel'. [184] Thailand's agreements with Australia[185] and New Zealand,[186] along with the Japan–Singapore EPA, however, appear to make consultations a pre-requisite to recourse to a compliance panel.[187] Virtually all of the PTAs with some provisions on compliance proceedings provide expressly for, or appear to contemplate, that it is the original panel that will hear the compliance dispute.

The time afforded a compliance panel to complete its work varies among the agreements, and may be 30,[188] 45,[189] 60,[190] or 90[191] days from the date of the request or date of which the compliance panel is established or composed. The PTAs which provide for a single panel to decide both compliance issues and the level of

182 E.g., Turkey–Morocco FTA; EU–Israel AA; EU–SA TDCA; and India–Sri Lanka FTA.
183 Article 19.15. 184 Article XIII.17.3. 185 Article 1810.3. 186 Article 17.10.3.
187 See paragraphs 3 and 4 of Article 147.
188 Japan–Mexico EPA, Article 156.8; and Korea–Singapore FTA, Article 20.14.6.
189 EU–Chile AA, Article 188.5.
190 EU–Mexico FTA, Article 46.5; Korea–Chile FTA, Article 19.15.5; and Singapore–Australia FTA, Article 9.2.
191 Canada–Costa Rica FTA, Article XIII.17.7.

suspension of concessions simultaneously (see below) typically provide two time limits: 90 days if the panel is asked to address compliance *or* the appropriate level of suspension of concessions, and 120 days if the panel is asked to address compliance *and* the appropriate level of suspension,[192] although this is not always the case.[193] One PTA expressly states that when an implementing measure is found by a compliance panel to be inconsistent, the respondent is not entitled to any further period of time for implementation.[194]

The wording of some PTAs may suggest that the scope of *measures* that a compliance panel may examine is intended to be different than is the case under the DSU. For example, it is possible, under a few PTAs, to request a compliance panel to make a determination as to the conformity of a *proposed* implementing measure,[195] even if that measure is not yet in force. A second example is that the wording of certain PTAs might restrict the implementing measures that may be referred to a compliance panel to measures that are adopted *during the period of time for implementation*.[196] Whether such a restriction is created is unclear, and it is also uncertain what the purpose of such a restriction might be – for example to preclude a compliance panel from examining implementing measures adopted once that period of time has expired, to preclude 'serial' compliance proceedings as has happened in a few instances in the WTO context,[197] or for some other reason.

2. The 'sequencing' problem

The so-called 'sequencing' problem is rooted in the lack of any express indication, in the text of the DSU, of the relationship between Article 21.5, dealing with

192 US–Morocco FTA, Article 20.11.3; US–Singapore FTA, Article 20.5.5; AUSFTA, Article 21.11.3; and CAFTA–DR–US, Article 20.16.3.

193 Thailand's PTAs provide that the panel shall be reconvened within thirty days of a request and present its determination within ninety days after it reconvenes (Thailand–Australia FTA, Article 1811.3; NZ–Thailand CEPA, Article 17.11.3).

194 Canada–Costa Rica FTA, Article XIII.17.9.

195 EU–Chile FTA, Article 188.4; and EFTA–Chile FTA, Article 96.4. Other PTAs authorise the complainant to request consultations with respect to a proposed implementing measure and further allow the complainant to seek the suspension of concessions in the event that such consultations do not lead to a mutually acceptable resolution. If the responding party objects to the level of the proposed suspension, then the resulting panel examination may cover both the level of suspension of concessions as well as the conformity of the proposed measure (see, e.g., Thailand–Australia FTA, Articles 1810.3 and Article 1811, as well as NZ–Thailand CEPA, Articles 17.10.3 and 17.11).

196 For example, Article 9.2 of the Singapore–Australia FTA, which closely follows Article 21.5 of the DSU in most respects, contains the additional qualifying phrase 'within the reasonable period of time' to its introductory phrase: 'Where there is a disagreement as to the existence or consistency with this Agreement of measures taken *within the reasonable period of time* to comply with the recommendations . . . ' (emphasis added).

197 There were two consecutive Article 21.5 proceedings in each of the *US–FSC* and *Canada–Dairy* disputes. In addition, an Article 21.5 panel is currently considering Ecuador's claims against the European Communities' modified banana import regime, eight years after adoption of the first Article 21.5 panel's report and nearly ten years after the adoption of the report in the original proceedings.

compliance disputes, and Article 22, dealing with compensation and the suspension of concessions. This is compounded by the time limits imposed for the initiation of negotiations on compensation and for a request for authorisation to suspend concessions set out in Article 22.2 of the DSU. Both deadlines are calculated with reference to the date of expiration of the reasonable period of time for implementation, and make no allowance for a longer period of time in the event that a compliance proceeding is ongoing. The issue first came to a head in the *EC–Bananas III* dispute. Since that time, most disputing parties who are involved in compliance proceedings under Article 21.5 of the DSU have concluded bilateral procedural agreements between themselves. Typically, these stipulate that the complaining party will request both the establishment of a compliance panel under Article 21.5 of the DSU and the suspension of concessions under Article 22. Such agreements further provide that the DSB will both establish the compliance panel and refer the level of suspension of concessions to an arbitral panel, but that the latter proceeding will be suspended until the former has been completed. These arrangements have the consequence that the complaining party may have to wait much longer than the expiry of the reasonable period of time before obtaining DSB authorisation to suspend concessions.

A few PTAs follow the DSU structure quite closely and may, therefore, contain their own sequencing issues. The agreement between Chile and Korea appears to eliminate sequencing issues by omitting altogether the possibility to refer compliance disputes back to the panel.[198] A number of PTAs, however, include provisions that appear designed to avoid the sequencing problem. The Korea–Singapore FTA, for example, authorises a complainant to begin suspending benefits thirty days after it has given notice of its intention to do so or after delivery of a panel report on the issue of compliance, 'whichever is later'.[199] The Singapore–Australia FTA contains a provision that closely resembles Article 21.5 of the DSU,[200] along with a subsequent provision that links the deadlines for requesting compensation and arbitration on the level of suspension of concessions to the date of circulation of the compliance panel report, rather than to the expiration of the reasonable period of time.[201]

A significant number of the PTAs examined sidestep the sequencing problem by combining the functions that, in the WTO, are dealt with separately in Article 21.5

198 Article 19.15 of that allows the complainant to suspend benefits if there is no implementation of the panel report within thirty days following the expiration of the implementation period, but does not address the issue of a possible disagreement over whether such implementation has occurred.

199 Article 20.15.6. 200 Singapore–Australia FTA, Chapter 16, Article 9.2.

201 Chapter 16, Article 10.1. This type of mechanism seems to imply that a complaining party must have recourse to a compliance panel even when there is no disagreement as to whether or not implementation has occurred (e.g., if the responding party has taken no action) because, at least on the face of the relevant provision, compensation negotiations can only be initiated *after* the report of the compliance panel and the suspension of concessions can, in turn, only be sought twenty days after a request for such negotiations has been made.

and paragraphs 2–6 of Article 22. Such mechanisms differ in two significant respects from the DSU. First, under the DSU compliance disputes are conducted separately from arbitrations on the level or nature of suspension of concessions, whereas many PTAs assign to the same panel both the task of assessing the conformity of an implementing measure as well as the task of determining the appropriate level of suspension of concessions in the event of non-implementation. Secondly, in contrast to Article 21.5 of the DSU, pursuant to which responsibility for referring a matter to a compliance panel rests primarily – if not exclusively[202] – with the complaining party, many of the PTAs examined assign to the responding party the responsibility of referring compliance issues to a panel. This is achieved by allowing a complaining party dissatisfied with an implementing measure to request consultations and, if those consultations do not yield a mutually acceptable resolution, to notify its intention to suspend concessions. At that point, the responding party may refer issues of compliance and/or the level of suspension to the original panel. Five of the agreements which allow a responding party to refer compliance issues and the level of suspension of concessions to an original panel contain an additional, separate provision that allows a responding party to request the original panel to determine the consistency of an implementing measure even in the absence of a request by the complainant to suspend concessions,[203] although others do not.[204]

E. Remedies available in the event of non-compliance

As indicated, most PTAs indicate that implementation of the recommendations and rulings of the panel (or the resolution agreed by the parties upon receipt of such report) is the preferred outcome in the event that a panel finds that a measure does not conform to a party's obligations under the PTA. At the same time, nearly all provide for other remedies which are, in most cases, expressly characterised as 'temporary' pending implementation. In those PTAs which provide some explanation of the available remedies, these tend to replicate those found in the DSU,

202 WTO Members have in the past debated whether the DSU allows a responding party to refer its implementing measure to a panel to determine its consistency with the covered agreements. Such a referral was made, in one instance, by the European Communities. In that case, however, the panel determined that the implementing measure was not consistent with the European Communities' obligations, and neither the European Communities nor any other WTO Member put the report on the agenda of the DSB for adoption. Thus, the Report in *EC–Bananas III (Article 21.5–EC)* remains the only panel report never to have been adopted by the DSB.

203 CAFTA–DR–US, Article 20.18; AUSFTA, Article 21.13; US–Chile FTA, Article 22.17; US–Singapore FTA, Article 20.8; and US–Morocco FTA, Article 20.13. As discussed below, such provisions provide a means for a respondent to terminate the suspension of concessions or its duty to pay an annual monetary assessment in the event that it has achieved implementation after the imposition of such measures.

204 NZ–Thailand CEPA; Korea–Singapore FTA; Thailand–Australia FTA; and Japan–Singapore EPA.

namely agreed compensation (meaning the grant by the responding party that is not yet in compliance of additional benefits or concessions under the agreement) or the suspension of concessions by the complaining party. The PTAs to which the US is party contain a third remedy, namely the possibility for the responding party to pay an annual monetary assessment. Some PTAs contain no express reference to remedies that might be available in the absence of implementation, although their terms often contain language that might allow a variety of such remedies to be adopted.[205]

1. Compensation

Although a few of the PTAs examined contain no express reference to compensation as a possible remedy,[206] a large majority clearly indicate that it is an option. Among these, many also make clear that, as under the DSU, compensation is a temporary measure pending the preferred outcome of implementation of the panel report. The principal differences among the agreements with respect to compensation include: whether there is a specified time for initiating negotiations on compensation and, if so, whether it is calculated with reference to the date of delivery of the final panel report or the date of the expiration of the period of time for implementation; whether the onus is on the complaining party or the respondent to initiate discussions on compensation or present a proposal; and whether compensation is to be negotiated or proposed by the complainant and then subject to a panel determination in the event that the respondent does not agree, and to the deadlines for the various steps in the process. The PTAs typically provide that a complaining party may proceed to the suspension of concessions if no agreement on compensation is reached and, in some cases, if an agreement is reached but subsequently breached by the responding party.

Like the DSU, several PTAs link the initiation of discussions on compensation to the end of the reasonable period of time for implementation.[207] In contrast, the EU–Mexico FTA authorises the complainant to request consultations on compensation if the respondent has failed to notify its implementing measure before the end of the reasonable period of time *or* if a compliance panel has ruled that the implementing measure is inconsistent.[208] The two PTAs to which Thailand is party make clear that compensation discussions can occur within an implementation period, but do not necessarily tie such discussions to dates calculated in relation to the panel's final ruling. These agreements require 'consultations with a view to developing a mutually acceptable resolution, such as compensation or any

205 Turkey–Morocco FTA, Article 33.8 allows a complaining party to take measures 'in line with the decision of the Joint Committee' but provides no indication of what those might be.

206 Korea–Chile FTA; and EU–SA TDCA.

207 Canada–Costa Rica FTA, Article XIII.18.1; Korea–Singapore FTA, Article 20.14.1; Japan–Mexico EPA, Article 156.3; and EU–Mexico FTA, Article 46.4.

208 EU–Mexico FTA, Article 46.6.

alternative arrangement and agreeing on a reasonable period to implement such resolution' whenever the responding party considers that prompt compliance is 'impracticable' or if the complaining party considers that a proposed or adopted implementing measure does not constitute implementation. They provide for direct recourse to an arbitral panel (which may also determine the consistency of an implementing measure) in the event that such consultations do not lead to a mutually acceptable resolution.[209] These agreements make clear that compensation is to be temporary and that full implementation is a preferred resolution.[210]

Several PTAs provide for consultations on compensation within twenty,[211] thirty[212] or forty-five[213] days of the date of delivery of the final panel report. These then afford the parties a period of twenty[214] or thirty[215] days after which, if there is no agreement on compensation, the complaining party may notify its intention to suspend concessions.[216] Several of these agreements also allow a complaining party to make such a notification if an agreement on compensation has been reached but the complaining party subsequently considers that the responding party has failed to comply with the terms of such agreement.[217]

Chile's agreements with both the EU and EFTA place the onus on the party whose measure has been found inconsistent to notify the other party of, *inter alia*, 'a concrete proposal for a temporary compensation until the full implementation of the specific measures required for compliance with the ruling'.[218] The notification must be made within thirty days of the ruling of the panel and, in the event of a disagreement on the content of such notification, the complainant shall request that the original panel rule on 'whether the compensation proposal is manifestly disproportionate'.[219] This ruling is to be made within forty-five days.

209 NZ–Thailand CEPA, Article 17.10.3; and Thailand–Australia FTA, Article 1810.3.

210 The two Thai agreements provide for such consultations in the event that *prompt* compliance is impracticable. In contrast, Article 147.2 of the Japan–Singapore EPA calls for consultations on a mutually acceptable resolution 'through compensation or any alternative arrangement' when the implementing party considers that 'compliance with the original award is *impracticable*'. The Japan–Singapore EPA does not contain any statement to the effect that compensation is temporary. The significance of these differences – if any – is unclear.

211 Singapore–Australia FTA, Article 10.1. 212 Korea–Singapore FTA, Article 20.14.1.

213 AUSFTA, Article 21.11.1 and 21.11.2; US–Singapore FTA, Article 20.6.1 and 20.6.2; and US–Morocco FTA, Article 20.11.1 and 20.11.2.

214 Singapore–Australia FTA, Article 10.1; Korea–Singapore FTA, Article 20.14.1; Japan–Mexico EPA, Article 156.3; and EU–Mexico FTA, Article 46.4.

215 AUSFTA, Article 21.11.1 and 21.11.2; US–Singapore FTA, Article 20.6.1 and 20.6.2; and US–Morocco FTA, Article 20.11.1 and 20.11.2.

216 AUSFTA, Article 21.11.1 and 21.11.2; US–Singapore FTA, Article 20.6.1 and 20.6.2; and US–Morocco FTA, Article 20.11.1 and 20.11.2.

217 AUSFTA, Article 21.11.1 and 21.11.2; US–Singapore FTA, Article 20.6.1 and 20.6.2; US–Morocco FTA, Article 20.11.1 and 20.11.2; and Japan–Singapore EPA, Article 147.2.

218 EU–Chile AA, Article 188.3(c); and EFTA–Chile FTA, Article 96.3(c).

219 EU–Chile AA, Article 188.4; and EFTA–Chile FTA, Article 96.4.

2. Suspension of concessions

Nearly all of the PTAs with more elaborate dispute settlement mechanisms follow the WTO model on suspension of concessions fairly closely. Key differences include the fact that, under the PTAs, there is no need for the authorisation of a body equivalent to the DSB in order to suspend concessions. In addition, some PTAs – in particular those that do not incorporate the notion of a reasonable period of time for implementation – appear to allow for benefits to be suspended more quickly following the issuance of the panel report than would generally be the case in the WTO.

PTAs which expressly include the possibility of suspending concessions typically authorise a complaining party to initiate the use of this remedy. In most instances the complainant does so by notifying its intention to suspend concessions, although in some agreements it does so by directly requesting the original panel to determine the appropriate level of suspension of concessions.[220] The complainant may take the relevant step either upon expiration of the time allowed for negotiations on compensation,[221] or where an agreement on compensation or resolution of the dispute has been reached but the complainant subsequently considers that the respondent has failed to observe such agreement.[222] Examples include:

- The Japan–Singapore EPA allows a complaining party to notify its intention to suspend concessions within thirty days of the determination of a compliance panel that implementation has not been achieved or within thirty days of the expiration of the implementation period.[223]
- Chile's agreements with the EU and EFTA authorise a complainant to notify its intention to suspend concessions in the event that the responding party has failed to notify implementing measures before the expiration of the implementation period, or, in the event that an implementing measure does not constitute implementation, if there is no agreement on compensation.[224]

The agreements that provide for the complaining party to first notify its intention to suspend concessions provide a period – five,[225] ten[226] or thirty[227] days – within which a responding party may, if it objects to the proposal, refer the matter to the original panel.

Most PTAs prescribe a time limit within which the panel must complete its assessment of the appropriate level and/or nature of suspension of concessions, for

220 See, e.g., Singapore–Australia FTA, Article 10.2. 221 *Ibid.*, and Korea–Singapore FTA, Article 20.14.2.
222 See, e.g., the PTAs to which the US is party; and Korea–Singapore FTA, Article 20.14.2.
223 Paragraphs 5 and 6 of Article 147.
224 EU–Chile AA, Article 188.6; and EFTA–Chile FTA, Article 96.6. 225 EU–Chile AA, Article 188.8.
226 Canada–Costa Rica FTA, Article XIII.18.3 and XIII.18.4.
227 Singapore–Australia FTA, Article 10.2; see also the PTAs to which the US is party.

example in thirty,[228] forty-five,[229] sixty[230] or ninety[231] days, although some are silent on the permissible duration of such proceedings.[232] Many also stipulate that the complainant must await the decision of that panel before proceeding to suspend concessions,[233] although some are silent on this issue. In contrast, the Korea–Chile FTA appears to allow a complaining party to suspend benefits at any time once thirty days after the time-frame for implementation fixed in the panel report has elapsed.[234] The wording of that agreement appears to assume that a panel will be activated only *after* the complaining party has suspended benefits.[235] Similarly, the two PTAs examined to which Thailand is party allow the complaining party to suspend benefits thirty days after it has given notice of its intention to do so *even if* panel proceedings are ongoing relating to compliance or the level of suspension.[236]

Most PTAs do not contain detailed rules regarding the procedures that are to be followed by a panel that has been asked to make a determination regarding the appropriate level and/or nature of suspension of concessions, although the Model Rules of Procedure annexed to some PTAs do address this issue. The Annex to the Korea–Chile FTA, for example, sets time limits for the first submissions of each party and provides that the panel may, unless the parties decide otherwise, decide not to convene a hearing.[237]

As for substantive principles governing the suspension of concessions, nearly all of the PTAs provide rules regarding the *level* of suspensions. They typically convey, although not always with the same language, the general principle that the level of suspension of concessions should be equivalent to the level of nullification and impairment caused by the measure found to be inconsistent.[238] As mentioned

228 Korea–Singapore FTA, Article 20.14.6.

229 Canada–Costa Rica FTA, Article XIII.18.5(c); EU–Chile AA, Article 188.8; and EFTA–Chile FTA, Article 96.8.

230 Korea–Chile FTA, Article 19.15.5.

231 NZ–Thailand CEPA, Article 17.11.3; and Thailand–Australia FTA, Article 1811.3. The PTAs to which the US is party allow a panel 90 days in the event that it is only making a determination regarding the level of benefits to be suspended, but 120 days in the event that it is asked, at the same time, to make a determination regarding the conformity of a measure taken to comply with the panel report.

232 See, e.g., Singapore–Australia FTA, Article 10.

233 Japan–Mexico EPA, Article 156.6(a); Japan–Singapore EPA, Article 147.4(a); EU–Chile AA, Article 188.8; and EFTA–Chile FTA, Article 96.8.

234 Article 19.15.

235 Korea–Chile FTA, Article 19.15.4: ' . . . the original panel shall determine whether the level of benefits *suspended* by the complaining Party is excessive.'

236 NZ–Thailand CEPA, Article 17.11.3; and Thailand–Australia FTA, Article 1811.3.

237 Annex 19.10, Rule 42.

238 Thus, for example the NZ–Thailand CEPA refers to 'benefits of equivalent effect to the non-conformity found' (Article 17.11.1 and 17.11.2(c)); the PTAs to which the US is party as well as the Korea–Singapore FTA refer to 'benefits of equivalent effect'; the Canada–Costa Rica FTA directs the panel to determine 'whether the level of such suspension is equivalent to the level of nullification or impairment' (Article XIII.18.5); and the Japan–Mexico and Japan–Singapore EPAs refer to 'level of nullification or impairment that is attributable to the failure to comply' with the panel report (Articles 156.5(c) and 147.4(c), respectively). Although the Singapore–Australia FTA contains no explicit requirement of

above, the PTAs to which Thailand is party authorise the suspension of concessions even while panel proceedings to determine the appropriate level of such suspension are ongoing. However they also each contain a unique provision which seems to be designed to impose some discipline on such unilateral action. These provisions allow a panel, in fixing the appropriate level of suspension of concessions, to adjust the level of 'equivalent' benefits 'to reflect any loss sustained' by a respondent 'as a result of excessive suspension'.[239]

Many of the PTAs also set out rules governing the *nature* of the concessions which may be suspended, and these tend to follow the WTO model in specifying that the complaining party should first seek to suspend benefits in the same sector or sectors as those affected by the inconsistent measure, and that only if it is not practicable or effective to suspend benefits in the same sector should recourse be had to other sectors.[240] Most of the PTAs which contain such provisions appear to also allow a panel to pronounce on whether or not these principles have been respected,[241] although some appear to limit the role of the panel to determining simply the *level* of the benefits that may be suspended.[242] Other PTAs are silent on the issue of whether a panel is to address the nature of the concessions to be suspended,[243] and one expressly prohibits a panel from doing so.[244] As explained below, several agreements have special provisions regarding the suspension of concessions when the dispute relates to financial services.

Many PTAs contain a statement to the effect that only benefits accruing or obligations owing under that specific agreement may be suspended,[245] and that the suspension of benefits is to be temporary.[246] A few also contain a provision analogous to Article 22.9 of the DSU, making clear that the suspension of concessions may be undertaken in disputes where the non-conformity of the measure derives from measures taken by regional or local government entities.[247]

equivalency, this is in all likelihood implicit in the provision that the panel is to determine the 'appropriate' level of suspension of benefits, Article 10.2.

239 NZ–Thailand CEPA, Article 17.11.3, and Thailand–Australia FTA, Article 1811.3, provide: 'If the tribunal determines that the level of benefits proposed to be or actually suspended is excessive, it shall determine the level of benefits it considers to be of equivalent effect to the non-conformity found by the tribunal, adjusted to reflect any loss sustained by a Party as a result of excessive suspension'.

240 See, e.g., Singapore–Australia FTA, Article 10.4; Korea–Singapore FTA, Article 20.14.4; Korea–Chile FTA, Article 19.15.1; Japan–Mexico EPA, Article 156.6; NZ–Thailand CEPA, Article 17.11; Thailand–Australia FTA, Article 1811.2; and EFTA–Chile FTA, Article 7. The EU–Chile AA refers to the suspension of benefits in 'the same Title or Titles of this Part of the Agreement as that affected by the measure' (Article 188.7). The relevant Part of the agreement dealing with trade is Part IV, and it is divided into eight titles. Thus, for example, Title II deals with trade in goods, Title III with trade in services, and Title V with intellectual property rights.

241 See EU–Chile AA, Article 188.8; and EFTA–Chile, Article 96.8.

242 See, e.g., Korea–Chile FTA, Article 19.15.

243 See, e.g., the PTAs to which the US is party; and the Korea–Singapore FTA.

244 Canada–Costa Rica FTA, Article XIII.18.5. 245 See, e.g., Singapore–Australia FTA, Article 10.3.

246 *Ibid.*, Article 10.5; Canada–Costa Rica FTA, Article XIII.18.6; Japan–Singapore EPA, Article 147.7(b); Japan–Mexico EPA, Article 156.6(b); EU–Chile AA, Article 188.9; and EFTA–Chile FTA, Article 96.9.

247 See, e.g., Canada–Costa Rica FTA, Article XIII.18.9.

3. Monetary assessments

Among the PTAs examined, all of the ones to which the US is party contain an additional potential remedy which has no current equivalent in the WTO, namely monetary assessments.[248] Pursuant to these agreements, in the event of non-implementation, a complaining party has a right to suspend benefits either within thirty days after having notified its intention to do so, or twenty days after a panel's determination of the appropriate level and nature of suspension, *unless* the responding party provides written notice that it will pay an annual monetary assessment within that twenty or thirty-day period. A complaining party that receives such a notice is then precluded from suspending benefits – at least until the responding party has failed to pay the monetary assessment. The amount is to be fixed by agreement of the parties or, failing such agreement, shall be equal to 50 per cent of the level of benefits that either: (1) a panel has determined to be of equivalent effect to the nullification and impairment or, if the level of suspension has not been referred to a panel; (2) the level that the complaining Party proposed to suspend. The monetary assessment is to be paid in quarterly instalments beginning sixty days after the responding party gives notice that it intends to pay an assessment. Although the default rule is that the monetary assessment will be paid to the complaining party, each of these PTAs also provides that, if the relevant Commission or Joint Committee under the PTA so decides, the assessment is to be paid into a fund established by that Commission or Joint Committee, and may be spent by that body 'for appropriate initiatives to facilitate trade between the Parties, including by further reducing unreasonable trade barriers or by assisting a Party in carrying out its obligations under the Agreement'. The agreements impose no limit on the length of time for which such monetary assessments may be paid.

4. Special remedies for disputes related to specific subjects

Several PTAs to which the US is party contain a special provision relating to non-implementation in disputes where a panel has determined that the responding party is not enforcing its domestic environmental or labour laws as required under the PTA.[249] These agreements specify that the general provisions on non-implementation do not apply. Instead, a separate article, entitled 'Non-Implementation in Certain Disputes', sets out the only remedy that may be available in the event that, following delivery of the final panel report, the disputing parties are unable to reach agreement on a resolution of the dispute, or the parties do reach such agreement but the complaining party considers that the responding party has breached that agreement. In such circumstances, the relevant PTAs authorise the complaining party to request that the panel be reconvened to impose an annual monetary assessment on the other

248 See US–Morocco FTA; AUSFTA; US–Chile FTA; US–Singapore FTA; and CAFTA–DR–US.
249 See US–Morocco FTA; AUSFTA; US–Chile FTA; US–Singapore FTA; and CAFTA–DR–US.

party. The panel is then to reconvene as soon as possible and, within ninety days thereafter, determine the amount of the assessment. In making its determination, the panel is instructed to take into account six listed factors,[250] and its determination may not exceed a ceiling of $15 million US dollars annually, adjusted for inflation. Once the panel has determined the amount of the annual assessment or at any time thereafter, the complaining party is entitled to provide notice in writing demanding payment. The assessment is payable in equal quarterly instalments beginning sixty days after the later of the panel's determination or the delivery of the notice demanding payment.

The monetary assessment is not, however, payable to the complaining party. Instead, it is to be paid into a fund established by the relevant Joint Committee/Commission of the relevant PTA, and may be spent by that body 'for appropriate labour or environmental initiatives, including efforts to improve or enhance labor or environmental law enforcement, as the case may be, in the territory of the Party complained against, consistent with its law'. The PTAs further provide that, in 'deciding how to expend monies paid into the fund, the [Commission or Joint Committee] shall consider the views of interested persons in the disputing Parties' territories.'

In the event that a monetary assessment is not paid, the relevant PTAs also authorise the complaining party to take 'other appropriate steps to collect the assessment or otherwise secure compliance'. Such steps may include the suspension of tariff benefits under the Agreement, as necessary to collect the assessment, while bearing in mind the Agreement's objective of eliminating barriers to bilateral trade and while seeking to avoid unduly affecting parties or interests not party to the dispute. Three of the five agreements which contain these special rules for non-implementation in specific environmental or labour related disputes also provide that, in the event of non-payment of a monetary assessment the complaining party shall, before having recourse to any other measure, seek to obtain the funds from an escrow account, if one exists and has been funded by the other party to ensure payment of any assessments against it.[251]

In addition, although some PTAs exclude trade in financial services altogether from the dispute settlement mechanisms they contain,[252] others authorise the resolution of disputes, but set out special provisions relating to disputes concerning financial services. Insofar as the remedies are concerned, such PTAs provide specific rules regarding the type of benefits that may be suspended in the event of non-implementation. More

250 These are: the bilateral trade effects of the Party's failure to effectively enforce the relevant law; the pervasiveness and duration of the Party's failure to effectively enforce the relevant law; the reasons for the Party's failure to effectively enforce the relevant law; the level of enforcement that could reasonably be expected of the Party given its resource constraints; the efforts made by the Party to begin remedying the non-enforcement after the final report of the panel; and any other relevant factors.

251 US–Morocco FTA, Article 20.12.5; US–Singapore FTA, Article 20.7.5; and AUSFTA, Article 21.12.5.

252 E.g., Japan–Mexico EPA, Article 109.

specifically, they provide that when a measure has been found by a panel to be inconsistent with the PTA, the complaining party: may suspend benefits in the financial services sector if the measure affects *only* the financial services sector; may suspend benefits in the financial services sector that have an effect equivalent to the effect of the measure in that party's financial services sector if the measure affects *both* the financial services sector and any other sector; and may *not* suspend benefits in the financial services sector if the measure affects *only* a sector other than the financial services sector.[253]

5. 'Appropriate' measures

Lastly, we mention briefly two agreements to which the EU is party and their reference to the possibility for one party to the agreement to take 'appropriate measures'. The EU agreements with Israel and Chile each provide that, in the event that one party considers that the other has failed to fulfil an obligation under the agreement, then the party 'may take appropriate measures'.[254] However, before doing so, the party which considers the other party not to have fulfilled an obligation must supply the Association Council with all relevant information required to enable the Association Council to undertake a thorough examination of the situation with a view to seeking a solution acceptable to the parties. The agreements do not define what may constitute 'appropriate measures', but do specify that, in the selection of such measures priority must be given to those which least disturb the functioning of the agreement.[255] Such measures must be notified to the Association Committee and are to be the subject of consultations within that Committee if the other party so requests.

The EU–Chile AA contains two further provisions '[b]y way of derogation from' the above. One of these restricts the potential scope of application of such 'appropriate measures' by clarifying that, when the obligation alleged to have been breached is contained in Part IV of that agreement – which deals with trade and trade-related matters – then the party which considers the other party to be in breach must 'exclusively have recourse to, and abide by, the dispute settlement procedures' contained in that Part of the agreement.[256] The second derogation authorises a party to 'immediately' take 'appropriate measures in accordance with international law' in two circumstances: (1) denunciation of the agreement that is

253 E.g., Korea–Singapore FTA, Article 12.12.5; US–Morocco FTA, Article 12.17.4; US–Singapore FTA, Article 10.18.4; US–Chile FTA, Article 12.17.6; and CAFTA–DR–US, Article 12.18.5. The AUSFTA has a similar provision in Article 13.18.4.

254 These agreements each impose a requirement on the parties to adopt any general or specific measures required to fulfil their obligations under the agreement and to ensure that they comply with the objectives in the agreement. (EU–Israel AA, Article 79.1; EU–Chile AA, Article 200.1)

255 EU–Israel AA, Article 79.2; and EU–Chile AA, Article 200.2.

256 EU–Chile AA, Article 200.4. The other Parts of the agreements deal with: General and Institutional Provisions (Part I); Political Dialogue (Part II); Co-operation (Part III); and Final Provisions (Part VI).

not sanctioned by the general rules of international law;[257] and (2) violation 'of the essential elements' of the agreement.[258]

F. Post-retaliation proceedings

Certain PTAs, in particular those to which the US is party, contain provisions allowing for post-retaliation compliance proceedings.[259] Such proceedings enable a respondent that did not implement and was subjected to the suspension of concessions to seek to have those sanctions lifted in the event that it subsequently achieves implementation. This is a concept that has been proposed in the context of the negotiations on the clarification and improvement of the DSU, but which does not currently exist in the WTO. This lacuna arguably explains the *raison d'être* of the *Canada–Continued Suspension (EC–Hormones)* and *US–Continued Suspension (EC–Hormones)* disputes.[260]

The PTAs that include post-retaliation proceedings provide that, if the disputing parties disagree on whether implementation has been achieved, the respondent can request a compliance panel to make a ruling on this issue. If the panel finds that there has been compliance, then the complaining party must lift its sanctions and/or, in the PTAs to which the US is party, the respondent is relieved of its obligation to pay a monetary assessment. Panels are to make such determinations within thirty,[261] forty-five[262] or ninety[263] days.

257 EU–Chile AA, Article 200.3(a).

258 EU–Chile AA, Article 200.3(b). The 'essential elements' are defined as those contained in paragraph 1 of Article 1 of that agreement, which reads as follows: Respect for democratic principles and fundamental human rights as laid down in the United Nations Universal Declaration of Human Rights and for the principle of the rule of law underpins the internal and international policies of the Parties and constitutes an essential element of this Agreement.

259 CAFTA–DR–US, Article 20.18; AUSFTA, Article 21.13; US–Chile FTA, Article 22.17; US–Singapore FTA, Article 20.8; US–Morocco FTA, Article 20.13; Canada–Costa Rica FTA, Article XIII.18.10; EU–Chile AA, Article 188.8; and EFTA–Chile FTA, Article 96.10.

260 These disputes were initiated by the EC, the respondent in an earlier dispute, *EC–Hormones*, against the two complaining parties in those earlier disputes, the US and Canada. Both had – with the authorisation of the DSB and following an arbitration on the level of suspension – suspended concessions *vis-à-vis* the EC. Subsequently, the EC considered that it had implemented the DSB's recommendations and rulings. However, because the US and Canada disagreed with this assessment, they declined to remove the sanctions or to seek compliance proceedings under Article 21.5 of the DSU. Accordingly, the EC initiated a new dispute claiming that the continued suspension of concessions by the US and Canada was inconsistent with the DSU.

261 EFTA–Chile FTA, Article 96.10. 262 EU–Chile AA, Article 188.10.

263 CAFTA–DR–US, Article 20.18.1; AUSFTA, Article 21.13.1; US–Chile FTA, Article 22.17.1; US–Singapore FTA, Article 20.8.1; and US–Morocco FTA, Article 20.13.1.

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