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Trade and investment rule-making

The United Nations University institute for Comparative Regional Integration Studies, UNU-CRIS, is a research and training programme of the UNU that focuses on the role of regions and regional integration in global governance. The aim of UNU-CRIS is to build policy-relevant knowledge about new forms of governance and co-operation, and to contribute to capacity building on issues of integration and co-operation particularly in developing countries. UNU-CRIS works in partnership with initiatives and centres throughout the world that are concerned with issues of integration and co-operation. This book presents the findings of a UNU-CRIS research project that was undertaken in association with the International Trade Policy Unit at the London School of Economics. The study looks at the role of regional and bilateral agreements in trade and investment rule-making and is based upon a series of in-depth case studies.



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UNU-CRIS

Programme on Comparative
Regional Integration Studies

Trade and investment rule-making: The role of regional and bilateral agreements

Edited by Stephen Woolcock



**United Nations
University Press**

TOKYO • NEW YORK • PARIS

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United Nations University Press
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Shibuya-ku, Tokyo, 150-8925, Japan
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United Nations University Press is the publishing division of the United Nations University.

Cover design by Mea Rhee

Printed in Hong Kong

ISBN 92-808-1132-0

Library of Congress Cataloging-in-Publication Data

Trade and investment rule-making : the role of regional and bilateral agreements
/ edited by Stephen Woolcock.

p. cm.

Includes bibliographical references and index.

ISBN-13: 978-9280811322 (pbk.)

ISBN-10: 9280811320 (pbk.)

1. Trade blocs. 2. International trade. 3. Foreign trade regulation. 4. Regional economics. I. Woolcock, Stephen.

HF1418.7.T723 2006

382'.9—dc22

2006021198

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Foreword

An essential feature of today's globalized world is that governance and regulation are organized at many different levels. National states have a long tradition in setting rules for trade and investment. With the growth of the international economy there has been a growing demand for such rule-making at the global level as well. GATT and now the WTO have provided the framework for such an economic multilateralism that complements the national frameworks.

But next to the global multilateral agreements under the WTO, regional trade agreements have become more and more important as well. Such RTAs are situated in between the global and the national levels of governance. According to a study issued by the World Bank (2005), the number of RTAs now in force surpasses 200, and it has risen sixfold in just two decades. Preferential RTAs account today for more than one-third of global trade and this is expected to increase.

The rise of RTAs seems to be part of a broader worldwide move towards more regionalism and regional integration. The processes of regional integration are nowadays a booming phenomenon on every continent. Simultaneously with the creation of new regional economic integration agreements, many of those previously established in the 1970s and 1980s are evolving towards further integration, moving through successive stages (customs union, common market) and aiming to reach the point of an economic union. The 1990s were witness to a worldwide birth of "new regionalism". This "second generation" of regionalism is a multidimensional form of integration that includes not only economic but also political, security, social, cultural, scientific and technological co-

operation. It involves not only state governments, but industry and civil society as well.

The relationship between RTAs and the WTO poses a number of intriguing questions. To what extent do RTAs diverge or converge with the multilateral system? To what extent do they go beyond WTO trade rules? What effects do RTAs have on countries outside the agreement?

The United Nations University has tried to provide some answers to such questions because they are of extreme relevance for policy-makers. In 2003 the UNU Institute for Advanced Studies published the book *Regionalism, Multilateralism and Economic Integration: The Recent Experience*, edited by G. P. Sampson and S. Woolcock. The study found that regional processes and rules have been consistent with the multilateral obligations of each party. WTO rules therefore constitute a floor that underpins additional commitments in the regional agreements.

The present volume reports on a study undertaken by the UNU research and training programme CRIS (UNU-CRIS) that builds upon the previous Sampson and Woolcock research. This book aims to contribute to a major and growing area of study by analysing how RTAs shape the international regimes for investment, rules of origin, agriculture, food safety, intellectual property and services.

Until now, analyses covering regional agreements have been predominantly written by trade economists, and as such they have always focused on the effects of preferential tariffs and modelling the systemic effects of large numbers of regional agreements. These works, as well as volumes by political economists, have rarely looked at the detail of recent RTAs. The approach in this volume offers an alternative to the existing literature. Because it is based on the detailed substance of regional or bilateral agreements it is also an approach that aims to cover a much wider readership beyond academic communities, reaching out to practitioners and businesses involved in or affected by regional trade agreements.

A coherent set of case studies regarding the interaction between the different levels of rule-making show that, with the approach developed in this volume, the debate about regional agreements can be advanced. The volume illustrates what type of interaction between levels of rule-making can be broadly positive for the wider international system and which types of interaction should be seen with greater concern.

UNU-CRIS hopes that this study will rapidly become a valuable item on the reading lists for a range of international relations, international political economy, trade and other disciplines that address the issues of regional agreements and regionalism.

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List of acronyms

ABT	Agreement on Basic Telecommunications
ACP	African, Caribbean and Pacific
AFTA	ASEAN Free Trade Area
AGOA	Africa Growth and Opportunities Act
AIA	ASEAN Investment Area
ALADI	Latin American Integration Association
ANZCERTA	Australian-New Zealand Closer Economic Relations Trade Agreement
ANZFSA	Australia-New Zealand Food Standards Agency
AoA	Agreement on Agriculture
APEC	Asia Pacific Economic Cooperation
ARO	Agreement on Rules of Origin
ASCM	Agreement on Subsidies and Countervailing Measures
ASEAN	Association of South-East Asian Nations
BIT	bilateral investment treaty
BOP	balance of payments
BSE	bovine spongiform encephalitis
CAATEL	Andean Committee of Telecommunications Authorities
CAC	Codex Alimentarius Commission
CACM	Central American Common Market
CAFTA	Central American Free Trade Agreement
CAFTA-DR	Central American-Dominican Republic-United States Free Trade Agreement
CAN	Andean Community
CAP	Common Agricultural Policy
CARICOM	Caribbean Community

CCC	Customs Cooperation Council
CEECs	Central and East European countries
CEPT	Common Effective Preferential Tariff
CER	Australian-New Zealand Closer Economic Cooperation
CER-GPA	CER Government Purchasing Agreement
CGE	computable general equilibrium model
CIF	cost, insurance and freight
COMESA	Common Market for Eastern and Southern Africa
CP	contracting party
CRTA	WTO Committee on Regional Trade Agreements
CT	change in tariff classification
CTC	change in tariff classification at chapter level
CTH	change in tariff heading
CU	customs union
CUSFTA	Canada-US Free Trade Agreement
DCMA	US Digital Millennium Copyrights Act
DDA	Doha Development Agenda
DSU	WTO Dispute Settlement Understanding
EA	Europe Agreement
EBA	EU Everything But Arms scheme
ECJ	European Court of Justice
ECOWAS	Economic Community of West African States
ECT	exception to a positive tariff classification rule
EEA	European Economic Area
EFPIA	European Federation of Pharmaceutical Manufacturers and Associations
EFSA	European Food Safety Authority
EFTA	European Free Trade Agreement
EMA	Euro-Med association agreement
EMEA	European Agency for Evaluation of Medicinal Products
EPA	economic partnership agreement
FAO	UN Food and Agriculture Organization
FDA	US Food and Drug Administration
FDI	foreign direct investment
FOB	free on board
FTA	Free Trade Agreement
FTAA	Free Trade Area of the Americas
GATT	General Agreement on Tariffs and Trade
GATS	General Agreement on Trade in Services
GI	geographic indication
GPA	Government Procurement Agreement
GSP	General System of Preferences scheme
HS	Harmonized System of Tariff Nomenclature
HSP	highly sensitive product
IBRD	International Bank for Reconstruction and Development
IDB	Inter-American Development Bank

ILO	International Labour Organization
IMF	International Monetary Fund
IP	intellectual property
IPE	international political economy
IPRs	intellectual property rights
IPPC	International Plant Protection Convention
ISIC	International Standard Industrial Classification
ITO	International Trade Organization
ITU	International Telecommunications Union
JSEPA	Agreement between Japan and the Republic of Singapore for a New-Age Economic Partnership
LAIA	Latin American Integration Agreement
LDC	least developed country
LOTIS	UK Liberalisation of Trade in Services group
MAI	Multilateral Agreement on Investment
MC	import content
MCCA	Mercado Común Centroamericano (Central American Common Market)
MED	Euro-Mediterranean agreements
MERCOSUR	Southern Cone Common Market
MFN	most-favoured nation
MGA	melengestrol acetate
MNC	multinational company
MTS	multilateral trading system
NAFTA	North American Free Trade Agreement
NGO	non-governmental organization
NPA	National Preference Agreement (Australia)
NT	national treatment
OECD	Organization for Economic Cooperation and Development
OEEC	Organization for European Economic Cooperation
OIE	International Office of Epizootics
PCA	Partnership and Co-operation Agreement
PCT	WIPO Patent Cooperation Treaty
PP	public procurement
PPM	processes and production method
QR	quantitative restriction
RAF	risk analysis framework
RCV	regional value content
REIO	regional economic integration organization
RFSA	regional food standards authority
RMI	rights management information
RoO	rules of origin
RTA	regional trade agreement
RVC	regional value-added content
SACU	Southern African Customs Union
SADC	South African Development Community

S&DT	special and differential treatment
SAFTA	South Asian Free Trade Area
SDR	special drawing right
SEM	Single European Market
SP	sensitive product
SPC	supplementary protection certificate
SPS	sanitary and phytosanitary
SSG	special safeguard
STC	specific trade concern
TABD	Transatlantic Business Dialogue
TBR	Trade Barriers Regulation
TBT	technical barrier to trade
TPM	technological protection measure
TR	technical requirement
TRIMs	Agreement on Trade-Related Investment Measures
TRIPs	Agreement on Trade-Related Aspects of Intellectual Property Rights
TRP	Telecommunications Reference Paper
TRQ	tariff-rate quota
UNCITRAL	UN Commission on International Trade Law
UNCTAD	UN Conference on Trade and Development
USDA	US Department of Agriculture
USITC	US International Trade Commission
USTR	US trade representative
VC	value content
VP	value of parts
WCT	WIPO Copyright Treaty
WGGP	Uruguay Round Working Group on Government Procurement
WGTGP	Working Group on Transparency in Government Procurement
WHO	World Health Organization
WIPO	World Intellectual Property Organization
WPPT	WIPO Performances and Phonograms Treaty
WTO	World Trade Organization

1

Introduction

Stephen Woolcock

Introduction

The two major trends in the international economy in the 1990s have been globalization and regionalism, and much has been written on both. The interaction between the two has, however, not yet been subject to a great deal of research. This volume aims to rectify this by looking at the interaction between regional and other levels of rule-making in the international trade and investment regimes.

Much of the work on regional or preferential agreements has tended to avoid discussion of the detail of rule-making or deeper integration. Models of trade creation and trade diversion are based on tariff preferences, other tangible forms of protection or elements of regional or preferential agreements that are reasonably easy to quantify, such as commitments on services. Although there has been an assumption in the economics literature that deeper integration is likely to be less discriminatory than tariffs, there has been little detailed study of the impact of deeper integration at the regional level on the multilateral trading regime. A number of contributions have pointed to the costs of a “spaghetti bowl” of different preferential rules and how these might be seen as “stumbling blocks rather than building blocks” for the wider multilateral system. But the spaghetti bowl analogy was drawn from observation of one area of rule-making, that of preferential rules of origin, and one cannot conclude that all rule-making at the regional level has the same effects. Finally, there are often only very general references to the

linkage between regional and multilateral negotiations, along the lines of the growth of regional agreements following problems in multilateral negotiations, or the threat of regional initiatives being used to pressurize negotiating partners in multilateral negotiations to make concessions.¹

Rule-making may not be a major issue in the Doha Development Agenda (DDA), but it continues to be important in regional and bilateral agreements. It is therefore especially important to look at the interaction between the multilateral level of the WTO and other levels of rule-making. This volume contributes to a better understanding of the issues by looking in detail at the interaction between the regional and other levels of rule-making in a range of policy areas. The volume adopts a horizontal approach in order to be able to analyse the interaction between different agreements. Consideration of past rule-making also enables an assessment of the interaction over a period since the formation of GATT, although for reasons of space this historical treatment is not extensive. The case studies have been chosen to include policy areas important for agricultural trade (agricultural rules such as sanitary and phytosanitary (SPS) measures), for trade in manufactures (rules of origin and public procurement) and for “new” trade issues such as services, intellectual property rights and investment. The selection of case studies also covers cases in which there are few or only partial multilateral rules within the WTO (preferential rules of origin and investment); cases in which there are rules but these are not applied by all WTO members (telecommunications services and public procurement); and cases in which there are strong WTO rules (intellectual property and SPS measures).

This introductory chapter sets out three broad assumptions about the nature of the international trade and investment regimes on which the work is based. First, rule-making is central to the international system and is likely to become more important in the future. Second, rules are – and have always been – the product of a multilevel process. And third, how these levels interact will be of central importance to the future of international trade and investment regimes.

The chapter then offers an analytical framework for assessing the impact of regional/bilateral initiatives and the interaction between levels. This framework essentially breaks down rule-making into component elements. This facilitates an assessment of the impact of RTAs, how agreements on different levels interact and a comparison on the dominant models of RTAs or FTAs, such as those promoted by the United States, the European Union and other “hubs”. This framework provides an opportunity for developing some straightforward hypotheses regarding the interaction between levels of rule-making. For example, greater coverage at the regional or bilateral level is likely to constitute a preference, but

one that is subject to erosion as the coverage of multilateral rules increases. Transparency rules at the regional level are unlikely to cause difficulties and will tend to promote best (or at least better) regulatory practice that will tend to be non-discriminatory. Substantive rules at the regional or bilateral level that go beyond agreed international rules can be beneficial in that they extend the reach of rules that make trade and investment more predictable and thus reduce frictional and other costs. But substantive rules that go beyond existing agreed international norms, such as the WTO rules, can also result in incompatible rules in different regions and therefore need to be looked at more carefully. More efficient enforcement provisions at the regional or bilateral level create no difficulties if there is broad compatibility between the regional and multilateral (or plurilateral) rules. Difficulties may arise, however, when regional or bilateral enforcement results in interpretations of general norms that diverge from those of the WTO or other global bodies. The typical elements common to all rule-making and their potential impact are discussed below in more detail.

The horizontal case studies that follow this chapter illustrate the complex nature of the interaction between different layers of rule-making. These cannot be easily summarized in general conclusions. In some cases there is evidence of a synergy between RTAs/FTAs and other levels of rule-making; in some cases there are signs of divergence between the dominant regional/bilateral approaches that could result in some difficulties ensuring compatibility between bilateral or regional rule-making and multilateral rule-making. Three broad conclusions do, however, emerge from the case studies.

- The interaction between levels of rule-making is an important factor shaping policy outcomes and therefore one that must be considered alongside interest groups, institutional structures and ideas when seeking to explain the evolution of trade and investment policies.
- During the “second phase” of regionalism, namely the phase stretching from roughly the early to mid-1990s until the early 2000s, the interaction between regional and multilateral initiatives and agreements was positive in the sense that the two were synergistic or complementary. But developments since the early 2000s raise some doubt as to whether this will continue to be the case.
- There are important differences between the approaches of the major rule-making “hubs” (i.e. the United States and the European Union) to regional or bilateral agreements, in terms of both the general policy objectives pursued, a point that has been made clear in the existing literature on FTAs, and the detail of rule-making that can have profound implications for future trade and investment.

Rule-making and market access are inextricably linked

Trade policy is often conveniently divided between market access issues and rules. This occurs in negotiations such as the DDA, but also in analysis. Market access tends to be about numbers (i.e. tariff levels and bindings, or sectors covered by GATS commitments), with reciprocity driving negotiations. The quantification possible in market access studies also facilitates the use of trade models to estimate the impact of policy options. Rule-making is less amenable to quantification. The impact of any agreement on rules is therefore harder to assess, and changes are likely to provoke significant opposition from domestic interests resistant to a change in the regulatory *status quo*. Negotiating rules also tends to involve more actors, which makes for greater complexity. For developing countries with limited research and negotiating capacity, it has often been easier to reject negotiations on rules issues rather than risk getting involved. The ease of quantifying tariffs and other border measures also leads to arguments favouring liberalization of the remaining tariffs or obvious barriers to trade over negotiations on rules. In short, there are a number of factors favouring leaving rule-making aside and concentrating on further liberalization of market access.

But the distinction between market access and rules is largely artificial. Rules and market access are closely related. For years efforts have been made to establish a framework of rules for technical barriers to trade because non-discrimination/national treatment has proved to be ineffective in removing these barriers to market access. The controversy surrounding trade in products deriving from genetically modified crops illustrates how market access and rule-making are inextricably linked and, as chapter 4 shows, that differences in domestic regulation or rules create major problems for trade. Regulation/rules is *the* issue in market access for investors and cross-border services trade, as illustrated in the cases of telecommunications services (chap. 6) and investment (chap. 8).

The potential for rule-making to influence trade has been present at least since the establishment of GATT. For example, the obligation to provide national treatment under article III of GATT has always had the potential to limit national policy autonomy with regard to how the rules were applied. But until the 1980s there was no political consensus in GATT on the vigorous enforcement of national treatment that encroached into national regulatory sovereignty. More effective enforcement of obligations in the WTO's Dispute Settlement Understanding (DSU) and equivalent regional provisions have, however, brought home the reality of the trading system's intrusive nature.

Rule-making has always been a multilevel process

Rule-making in trade and investment has always occurred on different levels. Whilst GATT 1948 is assumed to be “multilateral”, it was in fact drawn up by only 32 countries under the dominant influence of the United States, which saw to it that US domestic preferences and approaches to regulating markets shaped GATT, even though concessions were made to its negotiating partners. During the 1950s, and especially during the 1960s and 1970s, the plurilateral Organization for Economic Cooperation and Development (OECD) played a leading role in developing agreed models for rule-making. These models were then subsequently introduced into GATT, as shown in the case of public procurement (see chap. 5), but also services and intellectual property rights (chaps. 6 and 7). Efforts to “multilateralize” rules developed at the plurilateral or regional level have not always been successful. Consider, for example, the case of investment, where the North American Free Trade Agreement (NAFTA) combined OECD rules on investment liberalization with investment protection rules from bilateral investment treaties (BITs) in a comprehensive model for investment rules that the United States then sought to “multilateralize” through the Multilateral Agreement on Investment (see chap. 8).

There is thus nothing new in rules being devised or evolving from a multilevel process. What is new is the emergence of the regional level as one of the most important, and the decline in the role of the OECD as a forum for rule-making (as opposed to policy-related research). This multilevel nature of trade and investment policy has been recognized in policy circles. For example, the OECD Ministerial Declaration of 2001 called for efforts to ensure that regional and multilateral regimes are complements and not substitutes for one another, and the Doha Declaration called for work to ensure that regional agreements and multilateral approaches are compatible.

How levels of rule-making interact is now a central concern

Looking through the literature on trade and regional agreements one finds repeated references to the links between regional and multilateral negotiations, but of a very general nature. For example, the Kennedy administration is seen as having pressed for a new round of GATT negotiations in the early 1960s in order to limit trade diversion resulting from the creation of the EEC. When Bill Brock, the US Special Trade Representative, came back from the 1982 GATT Ministerial Meeting frustrated at

the lack of progress, he is reported to have made the strategic decision to press ahead with bilateral/regional negotiations. It has also been argued that NAFTA and the APEC summit in early 1993 were used by the United States to bring pressure on its trading partners to make concessions in the Uruguay Round. The more pronounced articulation of the US policy of “competitive liberalization” (in which regional/bilateral liberalization is to “compete” with multilateral liberalization in the WTO) was seen as a consequence of the failure of the Cancun WTO Ministerial in September 2003.

But these references to strategic linkage between the levels of negotiation or rule-making do not provide us with much of a sense of how the different levels really interact. What is needed, and what this volume addresses, is detailed work on the interaction in each element of rule-making in each policy area. As the regional level assumes a more important role in the multilevel process of trade and investment policy, it is especially important to understand how regional agreements interact with other levels.

Existing research on the impact of RTAs

The increase in numbers of regional or bilateral trade agreements has led to an outpouring of material on the subject. This research has focused on the motivations behind regional agreements and their impact on the multilateral system, but there is little work that has looked at the detail of the interaction between regional agreements and other levels of rule-making.

The work on the motivations behind RTAs or bilateral agreements invariably concludes that there are multiple motivations including foreign/security policy considerations, market access or heading off trade diversion, locking in domestic reforms, “hedging” against uncertainty in multilateral negotiations, attracting foreign direct investment or setting norms and standards for trade and investment (Schott, 2004; World Bank, 2005).

There is a vast literature, build on Vinerian customs union theory, on how regional agreements affect patterns of trade and investment.² This can be divided into work limited to the static effects of regional agreements and that which seeks to assess the dynamic effects. In terms of the static effects there are no unambiguous results on whether regional agreements are, in general, trade-creating or trade-diverting. As Viner (1950) envisaged, they can be both. Generally speaking there tend to be small net trade-creation effects from RTAs, which has raised questions as to why there has been support for such agreements. The “standard discussion of RTAs proceeds as if tariffs were the only barrier” to trade

(Winters, 1999: 7). This may have been a reasonable approximation for what was going on in the RTAs between developed countries up to the 1980s (although this is debatable). It is perhaps still a reasonable approximation for FTAs among developing countries today. But regional or bilateral agreements that involve developed economies, including of course North-South RTAs, will contain a greater or lesser degree of deeper integration or measures that seek to address “non-trade” issues or regulatory barriers to trade.

Deep integration

The static gains from deep integration emanate from the reductions in costs, including cost reductions due to the creation of common rules. In most cases of deep integration within a region, both producers or service providers in the region and suppliers outside benefit, but the degree to which each benefits will vary. For example, if different national technical regulations exist and are harmonized within an RTA this reduces costs for suppliers within the region, because they can supply the whole market using one “pattern” rather than having to comply with a number of differing national regulations. Third-country suppliers will also benefit for the same reason. But the harmonized regional regulation may be more stringent or tougher than at least some of the previous national regulations. When this occurs one could say there is an effect equivalent to trade diversion.³ Regional or bilateral rule-making can be seen as promoting greater predictability and therefore positive even when smaller countries are “obliged” to accept the rules of a dominant “hub”. But the balance of benefits will depend on whether the rules are appropriate to all parties or are simply those dictated by the dominant hub. When rules diverge from agreed international rules they are also less likely to be of benefit, because of the risk of divergent sets of regional rules, or regulatory regionalism (van Scherpenberg, 1998; Isaac in this volume).

In principle if the regulatory barriers addressed by deep integration entail expenditure of real resources (i.e. in compliance with different regulatory norms or standards) rather than the creation of rents, then reducing the barriers saves resources and can be beneficial even if there is some trade distortion (Winters, 1996: 7). “Overall therefore, discriminatory deep integration seems unlikely to be harmful except in the opportunity cost sense of forgoing the greater gains from non-discriminatory integration” (Winters, 1996: 7). The work that has been done on the impact of rule-making, such as in services, tends to confirm that preferences are less evident and may even be impracticable to implement in some cases (Mattoo and Fink, 2002). In general, however, there has been little empirical work done on the effects of deeper integration agreements and

little that has assessed the more systemic or dynamic effects of divergent or competitive approaches to deep integration that could result in “regulatory regionalism”.

Systemic effects

There have been studies of the systemic effect of preferential trade agreements, but like those concerned with the static effects, these have been based on the creation and progressive extension of customs unions and FTAs based on a form of optimal tariff argument (Krugman, 1991). Krugman’s model suggested that if regional integration advanced to the extent that there were three regional blocs, this would be the worst case for world welfare. Various other writers developed the Krugman approach with somewhat differing results (for a summary see Winters, 1996), but the value of these models does not always match their elegance.

Some more elaborate models of “bloc formation” usefully include assessments of the effects of asymmetric bloc size, which is clearly a factor in some of the North-South RTAs that include rule-making. According to such models a regional bloc gains when it attracts members from other continents, because the trade benefits of boosting demand for the bloc’s comparative advantage goods outweigh trade diversion, even if the enlarged bloc does not increase its tariff on other countries. Frankel, Stein and Wei (1995) argue that a continent can increase its welfare by integrating when other continents stick with MFN. Alternatively smaller countries sign up to regional blocs as an “insurance premium” (i.e. to ensure market access), which has negative systemic effects as these countries are then less concerned about multilateralism. Arguably the larger the bloc the greater the incentive to defect, but the threat of retaliation or the effectiveness of multilateral discipline over preferential agreements, which is currently weak in the WTO, will influence the likelihood of countries opting for regional agreements.

More recently the World Bank (2005) has simulated the effects on developing countries of concluding regional/bilateral agreements with the major WTO members. This suggests that there may well be short-term gains in terms of attracting foreign direct investment and guaranteeing access to the market of the “hub”, but that in the long term developing countries are likely to be worse off.

These models are inevitably based on a number of limiting assumptions. For a start they assume unitary rational actors (in national governments) that are able to assess the costs and benefits of any policy choices, such as the costs of trade diversion against the gains from regional preferences. None of the economic models developed to date has been able

to come to more than ambiguous answers to such questions. Second, the models are invariably based on tariffs only and do not say much about the systemic impact of RTAs in the field of regulatory policies/barriers to trade. Third, the models largely discount the role of institutions. This means that the models cannot take account of any regulatory harmonization or regulatory emulation/competition (which is clearly happening to some degree in the multilateral system). Finally, the models are, understandably, based on the impact on economic welfare. Regulatory policies are generally based on a broader range of criteria including, for example, consumer protection, environmental sustainability or prudential security.

Political economy models

There are a number of “political economy” models based on the effects of pressure groups and voters on trade policy options. In these, regional agreements are formed when producers believe they will gain from trade diversion and utility-maximizing governments (seeking reelection or party funding) oblige (Grossman and Helpman, 1994). In other words, “good” politics dictates that regional agreements are more likely to be supported the greater the trade diversion (Krishna, 1999). These political economy approaches, like the optimal-tariff-based approaches, use highly stylized models of reality. They are based on the assumption that governments are clear on how to maximize their political utility and their decisions are essentially based on the balance between sector interests. They do not appear to account for the role of precedent or emulation in policy-making, which the cases discussed in this chapter all suggest plays a role. It is, of course, quite possible that the sector composition of preferences, and in particular the exclusion of specific sensitive sectors from tariff liberalization, are amenable to such interest-based explanations while rule-making aspects of RTAs are more complex.

Such rational-choice-based political economy models also fail to take account of path dependency or policy emulation. Therefore they cannot offer much guidance on whether, for example, the creation of a regional investment regime is a contribution to a wider multilateral agreement on investment or not. Political economy models developed with RTAs in mind, such as Baldwin’s (1996) domino model, appear to have more to offer. Baldwin’s model of RTA enlargement, which draws on European experience, argues that the shock of deeper integration creates pressure to join the bloc from producers and investors in neighbouring non-members. Without equal access to the bloc such producers will be at a disadvantage compared to producers and investors inside. As the bloc enlarges the costs of non-participation become greater as more and more markets are affected; enlargement only stops when the remaining

neighbouring countries face sufficiently high political objections to accession (Baldwin, 1996). This approach appears more applicable to a scenario in which deeper integration widens to include new countries, and could be seen as a driver for regulatory regionalism.

Bhagwati (1999) also addresses the path-dependency question by asking whether preferential trade agreements “provide an impetus for – or detract from – the worldwide non-discriminatory freeing of trade”. In this discussion he assumes that the “path” takes the form of the progressive enlargement of preferential trade agreements. Apart from the fact that the model is again based on progressive tariff liberalization, it also ignores the possibility of a multilateral regime emerging as a result of the emulation of rules or norms. The case of investment, discussed in chapter 8, shows how NAFTA-type rules for investment are being emulated in other regions. In other words, it does not readily fit with our hypothesis that postulates a rather more complicated, multilevel process of regime formation. Of more value for rule-making is Bhagwati’s (1994) discussion of sequential negotiations in which a selfish hegemon negotiates first with smaller and weaker neighbours in order to provide an incentive for others to negotiate and/or set a precedent for wider trade regimes.

In summary, there are a number of general shortcomings in much of the existing literature in terms of its applicability to the interaction between levels of rule-making in international trade and investment. First, it tends to use models developed from first principles with only very generalized references to the substantive provisions of regional agreements. Winters (1996: 50), in his summary of the models, suggests that given the difficulties with the existing models there is a need to consider actual cases. But the discussion of cases in much of the more theoretical literature is at a high level of generality and in most cases still fails to address the detailed substance of agreements. Bhagwati’s (1994) concept of the spaghetti bowl effect of regional agreements begins to address the question of compatibility of different regulatory norms, but this is based on an observation of preferential rules of origin and is not necessarily applicable to other areas of rule-making.

The issue of legal compatibility

Studies have also addressed the relationship between regional agreements and the multilateral trade rules in terms of the compatibility of regional/bilateral agreements with the letter of GATT article XXIV and GATS article V, the enabling clauses that provide exceptions for regional agreements between developing countries and the work of the WTO’s Committee on Regional Trade Agreements (CRTA). Assessing the compati-

bility of RTAs with the WTO provisions has been an important aspect of WTO work (WTO, 1995). But the work of the CRTA has been encumbered by a lack of progress towards agreed interpretations of the WTO provisions on what is substantially all trade under GATT article XXIV and article V of GATS.⁴ Negotiations in the WTO on definitions of substantially all trade have focused on the coverage of agreements in terms of tariff lines or sectors. In terms of the coverage of rule-making in RTAs, the question is to what extent article XXIV 8(a)(i) that requires the removal of “other regulatory restrictions to commerce” applies to deeper integration or rule-making provisions?⁵ A second area of contention is the treatment of regulatory barriers in terms of the requirement that the “general incidence of protection” in the form of duties or “other regulation of commerce” should not be greater after the creation of an RTA than it was for the constituent countries before the RTA was formed. Whilst there has been some clarification of the treatment of tariff protection under this provision in the 1994 Understanding on the Interpretation of Article XXIV, the treatment of “other regulatory restrictions to commerce” remains very unclear. For example, if country A has a higher SPS standard than its RTA partner, country B, and the RTA common standards are harmonized up to this level, does this mean that third-country suppliers will face a higher incidence of “protection” in country B, or does the existence of a single standard for the whole RTA mean that the cost of compliance for third-country suppliers is lower, so the general incidence of protection is lower? How could one go about measuring these compensatory effects?⁶

There is a continuing debate on how the provisions of the WTO might be revised in order to make them more effective and operational in their coverage of RTAs (Trachtmann, 2002). But this has concentrated on sector coverage only. In the future it will be necessary to have some operational criteria to apply article XXIV to rule-making. But before this can happen it is necessary to develop some means of assessing the impact of regional rule-making on the WTO. This in turn requires an analytical framework to facilitate an assessment of the compatibility of RTAs with multilateral rules and thus criteria for the application of article XXIV.

An analytical framework

From the sections above it follows that there is a need for more work on the substance of the regional agreements themselves. In order to be able to compare the provisions of various regional agreements and assess how they affect other levels of rule-making, it is helpful to break down rule-making into its component elements. This can then provide the basis for

comparison and the possible development of criteria for assessing the impact of such agreements and whether they are compatible with the long-term health of the multilateral trading system.

The analytical framework presented in summary form in table 1.1 builds on earlier work and distinguishes between the key elements in any rule-making provisions (Woolcock, 2005). With some exceptions this can be applied to any area of rule-making. For example, when coverage goes beyond that of the WTO, such as in the use of generalized negative listing in sector schedules, or when subcentral government or secondary instruments are covered at the regional level, a preference is created analogous to a tariff preference. In terms of principles a regional agreement that offers national treatment only to signatories clearly also creates a preference.

Regional transparency requirements, on the one hand, tend not to represent much of a preference as the information is likely to be made available to all parties. Transparency rules will also tend to promote good regulatory practice, which is likely to mean more regulation based on clear criteria and non-discrimination. On the other hand, where transparency rules in an RTA include “due process” commitments only *vis-à-vis* regional partners, as is the case in most RTAs apart from NAFTA, one could say there is a degree of preference.

Substantive rules such as full or partial harmonization or mutual recognition help reduce or remove regulatory barriers to market access, but, as noted above, can result in higher regional regulatory standards. Even then common regional rules may have a range of benefits for signatories and third parties. Much will depend on the details of the specific case. An important factor in assessing the impact of substantive rules will be whether regional rules are based on agreed international standards, such as in the case of RTA provisions on telecommunications that tend to use the WTO’s 1997 Telecommunications Reference Paper (see chap. 6), or whether they seek to change or reinterpret existing rules, as is in part the case with SPS rules (see chap. 3) and IPR rules (see chap. 7). The degree of preference with mutual recognition depends on whether agreements are open – in other words whether mutual recognition is also available to bodies or sectors in third countries that meet the same requirements as the signatories to any mutual recognition agreement.

There are often rules on cooperation. General wording and an overarching RTA committee as the forum are unlikely to have much impact, but sector or policy-level cooperative machinery tends to include exchange of expertise and more resources. This can in turn help to establish or strengthen regulatory capacity or promote regulatory emulation, which can be important in spreading rules, especially in agreements between developed and developing countries.

As with market access commitments, rule-making generally also provides for a regulatory safeguard that allows regulators discretionary powers or the right to regulate to defend “legitimate” policy objectives. Some systems of rules then seek to limit the scope for such discretion by requiring discriminatory measures to be proportionate, or the use of “least trade-distorting measures” to satisfy the legitimate policy objective. If regional regulatory safeguards provide less scope for discretion than the WTO then the agreement could be said to go beyond the WTO. The issue then becomes whether these tighter rules apply only to signatories to the RTA or to all parties. If greater discretion is possible *vis-à-vis* third parties then a form of discrimination or preference is established.

Rules mean little unless they are enforced, and all trade and investment agreements contain some degree of ambiguity that requires interpretation. Dispute settlement provisions, review procedures and the scope for non-state actors to bring cases of non-compliance are therefore important elements in rule-making. For example, some RTAs offer investor-state-type dispute settlement rules that go beyond the WTO, and some offer extensive access to review procedures for legal persons. More effective enforcement at the regional level can promote market opening and better regulatory practice. Regional interpretations of rules may, however, set precedents for wider multilateral rules and thus challenge WTO rules.

By breaking down rule-making into the elements illustrated above it is therefore possible to assess how rule-making initiatives at the regional level interact with other levels. The framework also facilitates a comparison between regional rules and between RTAs and established international regimes, such as in particular with WTO rules. The framework therefore provides a point of reference for assessing the impact of RTAs that may be useful in policy prescription (see chap. 9).

Who shapes rule-making?

As noted above, RTAs are initiated for a combination of different reasons, which cannot be discussed in detail here. Very often foreign policy interests lie behind the launching of an agreement, such as in the case of the EuroMed association agreements or the US-Israel FTA. Other times commercial interests wishing to gain a competitive advantage or to neutralize an advantage gained by competitors will make a strong business case for an RTA, such as in the case of the EU-Mexico agreement in order to neutralize the disadvantageous position of EU business interests *vis-à-vis* US competitors in Mexico.

Table 1.1 An analytical framework for assessing RTAs

Element of rule	Typical provisions	Likely impact	Typical WTO provision	Degree of preference
Coverage	(a) Sector schedules	More extensive coverage implies greater “liberalization”	Generally a positive list approach Limited to coverage of central government as a rule with some secondary instruments	Third parties do not benefit from WTO-plus coverage Analogous to tariff preference
	(b) Type of entity subject covered			
	(c) Central, state, local, independent regulator or private entities			
	(d) Regulatory instruments covered			
Principles	(a) National treatment	Precludes discrimination against foreign suppliers No discrimination between third-party suppliers	WTO embodies national treatment and MFN principles but with exceptions, specifically for customs unions and FTAs	Third parties do not benefit from non-discrimination
	(b) MFN status			
Transparency	(a) Notification of legislation and possibly secondary provisions	Promotes regulatory best practice	General transparency provisions in all areas Some agreements also require (c)	Third parties not provided with information Third parties have no access to consultations
	(b) Opportunity for parties to comment	Facilitates compliance and guards against capture		
	(c) Obligation on regulator to explain decisions			
Substantive measures	(a) Harmonization	(a)–(c) Eliminates or reduces “frictional” costs (d)–(e) Reduces costs but retains regulatory autonomy	Selective harmonization Encourages but does not require mutual recognition or equivalence	Preference for regional norms or rules over international rules Preference for partners in mutual recognition
	(b) Partial harmonization			
	(c) Approximation as a general aim			
	(d) Equivalence			
	(e) Mutual recognition of regulations or test results			

Cooperation	(a) Common decision-making institutions	Promotes convergence on rules and/or best practice	Cooperation difficult with large membership	Third parties not involved in more intensive cooperation within the RTA
	(b) Intergovernmental committee to oversee agreement	Helps identify regulatory barriers	Mostly general provisions and technical assistance thinly spread	Third parties excluded from assistance
	(c) Specialist bodies for specific policy areas	Helps less developed economies develop best practice		
	(d) Technical cooperation and capacity-building			
Regulatory “safeguard”	(a) Exemptions from obligations	Tight discipline promotes predictability	Generally broad exceptions that offer considerable scope for regulatory discretion but some tightening, e.g. SPS Agreement	Potential for greater discretion <i>vis-à-vis</i> third parties
	(b) “Right to regulate” provisions	Loose wording limits allow discretion		
	(c) Proportionality in use of “safeguard”			
	(d) Required use of least or less trade-distortive measure			
Implementation	(a) Legal persons have standing in regional/ bilateral dispute settlement	Effective implementation promotes confidence and thus trade and investment flows	State-to-state dispute settlement only, focuses on national legislation (rather than secondary legislation)	Third parties have no recourse to tougher and more immediate remedies and reviews
	(b) Independent reviews of secondary instruments			
	(c) Remedies (e.g. financial penalties)			

Once negotiations are engaged, the interests of actors shape the scope and content of rules. There will be the offensive and defensive sector interests, the interests of various (often) competing central government departments, the interests of subcentral governments, independent regulatory bodies, consumers and various non-governmental organizations. The interests shaping rule-making will vary from case to case, but some general hypotheses about the respective roles of interests can help set the scene for the specific cases that follow.

Offensive interests seeking greater market access will favour greater coverage. In terms of sector coverage the balance between offensive and defensive sectors is likely to be central. Coverage of entities becomes more complex. Offensive sectors will favour greater coverage because they wish to have greater transparency or predictability in rule-making, but some domestic commercial interests may also stand to gain from the better regulatory practice. Likewise domestic consumers may stand to benefit from more transparent regulation and less discretionary powers in the hands of regulators or government. On the other side of the debate regulators are likely to oppose rules that constrain their regulatory autonomy and add to compliance costs. Extending coverage of rules to subcentral government includes similar issues, but with the added complication of political or constitutional questions about the allocation of powers between federal and state authorities. States may resist inclusion of rule-making at the multilateral level if this is linked to negotiations, such as trade in which federal government has competence. For example, chapter 8 shows how investment is excluded from EU-centred RTAs because this does not fall under European Community competence. Finally, on coverage, extension of rules to secondary instruments is likely to be favoured by those seeking greater openness and predictability, but opposed by regulators who must carry the often considerable cost of ensuring there is *de facto* and not just *de jure* compliance with rules.

National treatment and non-discrimination in general tends to be relatively straightforward and uncontroversial. Defending a “level playing field”, as it is often put, is relatively easy. The difficulty arises when there is *de facto* discrimination or perceived *de facto* discrimination when national laws are *de jure* non-discriminatory. In such instances offensive business interests will seek a deeper integration in the form of policy approximation, harmonization or mutual recognition in order to ensure *de facto* non-discrimination. National governments or regulators wishing to retain regulatory autonomy or control, liberal economists and defensive sector interests are then likely to oppose policy approximation or convergence.

Transparency is generally favoured by those interests seeking more open markets, and also those desiring more open and predictable regula-

tion. The latter need not necessarily lead to increased trade, as the case of public procurement in chapter 5 shows. It is therefore difficult for defensive interests that may benefit from opaque rules or regulation to argue against it. The governments, entities or regulatory bodies that have to implement transparency rules are, however, likely to argue that compliance costs, especially for secondary instruments, necessitate limited coverage. This is also illustrated in the case of transparency rules in public procurement. But in reality those who gain rents from opaque rules, such as established (uncompetitive) suppliers of public contracts, not to mention those who get kickbacks from such suppliers, will have a significant interest in blocking transparency rules.

Substantive rules tend to be favoured by those who see national treatment as inadequate. These will include sectors seeking access to specific markets. Harmonization or mutual recognition, at least outside the European Union, is something that only tends to occur in specific sectors or policy areas. Thus coalitions or sector interests may press for policy approximation, such as in telecommunications services or for that matter in intellectual property rights. As noted above, harmonization will be opposed by those who wish, for different reasons, to retain national regulatory autonomy. While there may be protectionist interests involved in opposing approximation or harmonization of rules, it is often a reluctance to accept the costs of domestic adjustment that is the more important factor.

When it comes to cooperation governments may see this as a means of both promoting their own approaches to regulation and assisting governments elsewhere that have less developed regulatory procedures or cultures. Independent regulators are likely to favour cooperation as a means of exchanging information and again promoting their own approaches. Developed country regulatory agencies will see promotion of better regulatory practices in developing economies as a means of promoting economic development. Developing country governments and regulatory agencies will also tend to see regulatory cooperation as a means of gaining useful expertise and as a form of technical assistance. But cooperative machinery will only be supported if there is a genuine dialogue. As cooperation provisions generally entail no binding commitments, the only opposition comes when it is seen as unproductive or costly.

All governments and regulators will tend to favour the introduction of regulatory safeguards because, from experience, they will have learned the value of being able to make exceptions to get around unforeseen problems. This is the case even when there is a general desire to promote liberalization. Defensive interests will also always want to see a safeguard because it holds out the possibility of protection if the industry or sector

concerned is threatened by intense competition. Civil society groups favour flexibility because they wish to ensure that public health, consumer safety, environmental protection or other legitimate objectives can be safeguarded. Opposition to safeguards is generally much less specific and probably weaker. It will come from those, including offensive interests, who are concerned that these will be used as a means of protection. These interests therefore press for balancing rules that seek to preclude the abuse of regulatory safeguards, including effective enforcement rules.

Finally, provisions on effective enforcement are supported by those who stand to gain from the agreement as a whole. Business and possibly civil society NGOs may favour enforcement mechanisms that allow rapid remedies and the ability to initiate procedures themselves. Governments are often viewed as holding back from rapid and effective enforcement for diplomatic reasons. More generally, enforcement provisions may be seen as a means of achieving through the interpretation of any agreement what was not or was only partially achieved in negotiation on the rules. Those with offensive interests will therefore tend to favour more effective enforcement, while defensive interests will oppose it. Regulators and their sponsoring departments will resist rigorous enforcement provisions if these open the way for judicial activism, while government departments with more general, liberal interests will favour effective enforcement as a means of promoting predictable and credible rules and thus trade and investment.

Comparison of the main approaches to deep integration

The European Union and the United States are the main actors promoting deeper integration and the inclusion of rule-making at all levels. It is therefore important to understand how the approaches used by these two “hubs” compare. A close similarity between the two approaches will mean that third countries will not have too much difficulty complying with both sets of rules. Divergence between the approaches will mean additional costs for third parties and could result in “regulatory regionalism” (van Scherpenberg, 1998).

The general motivations of the United States and the European Union in their RTA policy are not the subject of this volume. As discussed elsewhere, the initiation of RTAs is likely to have a number of motivations (Schott, 2004; Aggarwal and Fogarty, 2004). US policy on FTAs is shaped by a combination of commercial/market access issues, foreign policy objectives and a desire to “lock in” domestic reform in partner countries. EU policy is equally shaped by foreign policy and commercial interests. The European Union, like the United States, is also affected by

a range of domestic factors. EU policy towards RTAs is shaped by the European Union's own positive experience with regional integration. This underlies EU policy and leads it to view regional integration elsewhere in the world as a means of promoting economic development and peace, hence the EU policy of pursuing region-to-region agreements or agreements between the European Union and other regional groups.

The United States came relatively late to an active FTA policy, but since adopting a multilevel approach to trade in the 1980s it has been more aggressive than the European Union. This is reflected in the US approach to negotiations and in the use of clearly defined models for FTAs. After the conclusion of NAFTA, the NAFTA text was used as the starting point for US FTA negotiations. Subsequent improvements on the model in the form of, for example, the US-Singapore FTA then tend to be the starting point for any further FTA negotiations. In comparison the European Union does not appear to have a single model agreement in the drawer ready for any FTA or region-to-region negotiation. The agenda for agreements varies depending on the circumstances, the negotiating partner and domestic EU constraints.

At a more substantive level the US and EU approaches vary in terms of their general structure as well as on detailed provisions in the respective policy areas. In terms of general structure the US approach to FTAs can be characterized as "policed non-discrimination". In other words the United States tends to limit deeper integration to selected areas in which it will pursue policy harmonization and rely on national treatment provisions with extensive enforcement procedures. The preference for national treatment may reflect a desire on the part of the US Congress to avoid loss of policy autonomy. The enforcement provisions often involve a right to initiate actions by legal persons (i.e. companies or non-state actors), such as in the case of investor-state dispute settlement. An illustration of the importance placed on such enforcement provisions and procedures can be found in the investment rules in US-centred FTAs, in which the enforcement provisions account for more than half of the text of investment agreements.

The EU approach to rule-making is based on an expectation of policy approximation or harmonization. The scope for policy approximation varies between potential accession states that are expected to adopt the existing body of EU rules, the *acquis communautaire*, including the case law regarding its interpretation developed in the European Court of Justice (ECJ). Agreements with other countries will include some degree of policy harmonization, but not across the board. For example, the association agreements with the EU's Mediterranean partners include the aim of the EU's partners moving towards the adoption of European competition rules over an indefinite period.

Finally, with regard to the detailed rules in a range of policy areas US and EU approaches can differ. These differences are discussed in the case studies in this volume. Differences in detail can be of major importance. Transatlantic cooperation has been an important feature of trade and investment rule-making, especially since the European Union emerged as a major actor in its own right with a distinct approach to rule-making. During the 1980s and 1990s the transatlantic duopoly shaped the evolution of rules on agriculture, rules of origin, public procurement services, investment, intellectual property rights, technical barriers to trade etc. This close, but not always harmonious, cooperation was broadly successful in bridging differences between the US and EU approaches. In some cases differences were only papered over, such as in the case of how to regulate biotechnology, but transatlantic cooperation ensured that the rules on most policy areas embodied in the US- and EU-centred RTAs were compatible with each other and with the common multilateral rules that emerged from this cooperation.

The interaction between levels of rule-making

This volume is above all interested in the nature of the interaction between the different layers of rule-making in trade and investment policies. In this introduction it may therefore be helpful to set out possible types of interaction. The following are some types of interaction that might be found. No doubt there are more.

- *Synergistic interaction* could be said to occur when rule-making on different levels interacts in an iterative, two-way process, with techniques or approaches developed at one level applied on other levels and improved upon.
- *Liberal forum shopping* might be said to occur when parties switch between levels (forums for negotiation) in order to overcome insurmountable barriers to the progression of liberal policies. For example, if negotiations on rule-making at the multilateral level are blocked due to the willingness of some WTO members to use their veto powers, efforts might switch to the plurilateral, regional or bilateral levels. This kind of interaction is liberal if the aim is to establish rules that have widespread benefits.
- *Mercantilist forum shopping* would apply if countries or actors switch between levels of rule-making in order simply to further their own narrow national or sectoral interests. Clearly it may be difficult to tell when rule-making is pursuing mercantilist and when liberal ends. But again the analytical framework helps. If a country switches levels in order to push ahead with substantive rules that differ from agreed in-

ternational rules, this might be seen as the action of the selfish (regional) hegemon seeking to use the greater asymmetric power it has in bilateral or regional negotiations in order to further its own narrow self-interest and enhance its relative gains. If, on the other hand, a party uses an alternative level or route in order to push rules that enhance transparency and promote good regulatory practice, it could be said to be liberal forum shopping.

- *Exporting domestic rule-making* would apply when regional/bilateral layers are used to extend the prevailing domestic or regional approach. In this case the main driving force could well be precedent rather than sectoral interests. When globalization results in a tension between the domestic rules and those in other countries or regions, the least-cost route to resolving such tensions is to seek to export one's own domestic rules. Here the main power at work is that of precedent and the heavy hand of established practice. Whilst the established practice in one country is unlikely to be optimal for other countries, established domestic systems of rules are generally based on a balance of sector and other interests. So one must differentiate between the mercantilist forum shopping in which specific interests seek to frame rules in their narrow self-interest, and the effort to export a domestic model of rule-making that has achieved a balance between, for example, liberal aims and other legitimate policy objectives. In terms of North-South regional agreements, the problem is that few Northern countries have had to worry much about development objectives in recent decades.

Governance issues

The debate on levels of rule-making is of central concern for (global) governance, because it addresses the global subsidiarity issue. In other words, at which level should rule-making take place or at which level should policies be harmonized, if at all? The layer at which rules are decided may also have a bearing on who participates in decision-making.

In terms of the *global subsidiarity* debate there is much controversy surrounding the question of whether there should or should not be policy harmonization or approximation. On the one hand, liberal economists as well as those who question the feasibility of policy harmonization argue that policy competition should prevail. It is argued that policy competition (or competition among rules) facilitates experimentation that will ultimately result in better rule-making. In other words, competition among rules reduces or removes the risk of policy failure. "Non-trade" issues should therefore be left to competition between jurisdictions. There is also opposition to harmonization from those wishing to protect develop-

ing country interests against what they see as the effort of developed countries to impose inappropriate Northern norms or standards on the South.

Harmonization is also opposed by those sceptical of the feasibility of significant or meaningful cooperation. This is particularly relevant for any discussion of rule-making at the multilateral level in the WTO. With 150 members of the WTO, progress at this level is seen as posing major problems. This line of argument leaves open the path for cooperation or harmonization of policies to be pursued on other levels. This can mean the use of greater asymmetric power relationships to impose national rules on others at other levels, such as bilateral, regional or plurilateral levels. Blocking the Singapore issues in the WTO does not mean they are not being pursued through FTAs and RTAs.

The alternative view is that harmonization or at least approximation of rules is necessary because markets are global. Rule-making cannot therefore remain within the confines of national jurisdictions and still be effective in addressing failures or imperfections in global markets. This view is held by those who are more concerned about market failures than government (or governance) failures and who wish to see sustainable economic development, address global problems such as global environmental threats or establish certain common minimum standards or collective preferences.

The case for harmonization or approximation can also be made on the grounds that policy competition may result in regulatory regionalism and the emergence of divergent rules that will undermine multilateralism. On the pretty safe assumption that the United States, the European Union and other major trading entities will continue to include rule-making in the bilateral, regional or plurilateral agreements they conclude, a point illustrated in all the chapters in the volume, there also remains a danger that North American, EU and possibly other approaches to deep integration will diverge. When this occurs it threatens multilateral approaches and creates added costs for third parties, because the latter have to comply with, for example, both the US and European rules of origin or food safety measures if they wish to trade, rather than one agreed set of rules.

The case for policy approximation or harmonization is also made by those who believe that the only effective means of achieving and maintaining market access is through common approaches to regulatory policies. Where tariff barriers are insignificant, as is the case with much trade between developed economies, or of diminishing relative importance, as in the case of developing country exports to developed economies, non-tariff and especially regulatory barriers have become or are becoming a central issue in trade and investment relations.

In practice there are no clear dividing lines between those interests fa-

vouring harmonization and those favouring policy competition. In terms of overarching ideologies, liberalism would tend to favour policy competition over harmonization, but then so would realists or economic nationalists who do not believe national governments can be bound by international rules. At the same time those who support multilateralism could argue for stronger multilateral rules as a means of preventing the erosion of the existing multilateral element in trade and investment regimes by bilateral and regional agreements. And mercantilists could argue that policy harmonization is necessary to ensure effective market opening.

Unsurprisingly, the current picture in terms of rule-making is one that includes elements of both harmonization and competition among rules. More relevant to the issues discussed in this volume is not so much whether harmonization of rules occurs, but at which level? The analytical framework may help define *subsidiarity* or the division of labour in rule-making. For example, there could be agreed common principles at a multilateral level but more far-reaching harmonization of substantive provisions or procedures at the regional or bilateral level. The case of public procurement can be used to illustrate this point. Whilst multilateral agreement on all aspects of public procurement is probably not feasible because of the diversity of practice and the complexity of the issues, agreed multilateral rules may be possible on transparency and possibly on provisions that prohibit explicit *de jure* discrimination. More detailed policy harmonization on contract award procedures, effective enforcement measures and other rules could then be left to plurilateral or regional levels.

An analysis of the complex interactions between rule-making at different levels on the basis of the above framework might then provide more operational guidelines for policy prescription than has been offered to date in harmonization or policy competition debate.

Governance also concerns questions of who participates in rule-making and thus the *political legitimacy of decision-making*. The issue of interaction between levels of rule-making is relevant here because, as the case studies in this volume show, there may be forum shopping by governments and interest groups in order to find the path of least political resistance. As some of the case studies show, rule-making used to be a largely technocratic process conducted by a relatively small policy élite consisting of government officials and – mostly business – experts. This is perhaps most clearly shown in the case of investment, where bilateral and plurilateral rule-making proceeded throughout the period from 1950 to the mid-1990s without close scrutiny by public and NGO opinion. Investment was politicized towards the end of the 1990s in the debate on the Multilateral Agreement on Investment (MAI). This also led to the politicization of the debate on investment within the WTO, but only partially

to the discussion of investment in regional-level agreements. To date investment at bilateral or regional level has been less politicized than at the level of the WTO, but as the case study suggests this may be changing. In intellectual property, the politicization of the issue in the WTO has led to some increased activity at the regional or bilateral levels, possibly as a result of efforts to regain ground lost at the multilateral level.

Conclusions

This chapter has set out the assumptions on which the following chapters are based, provided an analytical framework for assessing the interaction between levels of rulemaking and set out some general hypotheses relating to the interaction between levels of rule-making. The following chapters provide case studies in rule-making that apply the broad framework set out here.

Notes

1. Some clarification of terminology is needed. This volume addresses rule-making at different levels. Multilateral rule-making is essentially rule-making that takes place within the World Trade Organization (WTO), although there may be cases of multilateral rule-making in other more or less global membership bodies such as UNCTAD or other UN bodies. Plurilateral rule-making occurs when groups of “like-minded” countries come together to adopt common rules regardless of their geographic locations. The Organization for Economic Cooperation and Development (OECD) is the main plurilateral rule-making body discussed in this volume. But there are forms of plurilateral rule-making within the WTO, both formal, in the shape of plurilateral agreements such as the 1994 WTO Government Purchasing Agreement, and less distinct forms of plurilateralism, such as in the sector agreements under the General Agreement on Trade in Services (GATS), which only a selected number of WTO member countries apply. Regional rule-making is that which occurs in regional agreements, i.e. agreements between contiguous countries. Free trade agreements may be regional in nature but are more often bilateral between countries that are not necessarily congruous. In the text the term regional trade agreements (RTAs) is used to describe both regional agreements and free trade agreements. In some cases, however, it is necessary to differentiate between regional, free trade and bilateral trade agreements.
2. See Bhagwati, Krishna and Paragariya (1999) for a valuable collection of the key contributions to this literature.
3. This is an area addressed by GATT article XXIV, which states that RTAs and FTAs must address “other restrictions or regulation of commerce” and that the general incidence of protection should not increase as a result of the creation of an RTA. There is, however, no agreed interpretation of these provisions, especially on how they may relate to deeper integration.
4. In fact the CRTA has three tasks: to provide legal analysis of the RTAs (and their compatibility with the rules); to make horizontal comparisons (inventories of RTA provisions

- covering non-tariff barriers and TBTs and SPS measures have been made); and to debate the context and economic aspects of RTAs.
5. See, for example, a discussion of whether TBT and SPS measures should be included in substantially all trade provisions in Trachtmann (2002).
 6. In the 2005 discussions of this topic in the CRTA some developing country WTO members maintained that the introduction of common regional rules or standards constitutes an increase in the incidence of protection, whilst the European Union and others that have introduced deeper integration see them as liberalizing.

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Rule-making in agricultural trade: RTAs and the multilateral trading system

Charles Tsai

Introduction

This chapter addresses the context and manner in which differing levels of rule-making governing trade in agriculture interact. Rules governing international trade in agricultural products have a history distinct from those governing industrial products. While industrial products have been covered by the multilateral trading system (MTS) established under the General Agreement on Tariffs and Trade (GATT) for well over half a century, similar progress for agriculture has been lacking. The implementation of the Agreement on Agriculture (AoA) in tandem with the establishment of the WTO in 1995 better incorporated agriculture within the MTS, but clear room for progress remains. This chapter addresses rule-making with regard to agricultural subsidies and rules affecting market access directly, such as coverage and safeguard measures. It does not cover the equally controversial topic of sanitary and phytosanitary measures (SPS measures), which is covered in chapter 3.

While rule-making and experience at the level of regional trade agreements (RTAs¹) provided the basis for bringing agriculture under the MTS, rapid growth in RTAs covering agriculture suggests that rule-making on trade in agriculture remains dynamic at the regional level. Prior to 1995, international rules governing trade in agriculture had been *de facto* limited to those in such RTAs as the North American free trade agreement (NAFTA) and the European Union, but in the last 10 years the number of RTAs covering trade in agricultural products has more than doubled from 53 to 133.² In addition one estimate suggests

that more than half of total international trade could be covered under RTAs by 2005 (OECD, 2003: 12).

These RTAs are geographically and economically diverse, ranging from EU-Mexico to New Zealand-Singapore and Korea-Chile. They also include economies that have traditionally been strong supporters of the MTS and disinclined to negotiate RTAs, such as Japan and Korea. A recent member of the WTO, China, is now engaged in negotiations for RTAs and in the case of the China-ASEAN framework agreement has already implemented a “down payment” containing important liberalization in agricultural trade.

Thus provisions in RTAs help provide the basis for multilateral agreements, but growth in RTAs has occurred in part because of difficulties in the MTS. In other words, there appears to be a complex interaction between levels in agriculture, with difficulties surrounding progress on agriculture at the multilateral level having supported the growth of RTAs in the first place. This chapter first describes multilateral rules governing trade in agriculture and compares these with the RTA provisions with regard to coverage, domestic support and contingency protection, and then analyses the manner and context of the interaction between levels of rule-making.

Key features of agricultural treatment within the MTS

This section provides an overview of the multilateral rules in the AoA and thus sets the stage for considering how agriculture is treated in RTAs. Coverage in the AoA was determined by market access provisions requiring WTO members to list and adhere to tariffs on imported agricultural products. It also involved the process of “tariffication” under which non-tariff barriers³ to trade in agricultural products were converted into value-based tariffs (*ad valorem*), quantity-based tariffs (specific duties) or – in a limited number of cases – tariff-rate quotas (TRQs).⁴ This process not only dramatically enhanced transparency in agricultural trade,⁵ but also set the stage for commitments on trade liberalization.

Trade liberalization commitments to be applied at the end of the tariffication process of the Uruguay Round included simple average reductions of 36 per cent over a 6-year period for developed economies, with a minimum of 15 per cent reduction for each product, and 24 per cent over a 10-year period for developing countries, with a minimum reduction of 10 per cent. Least developed economies were exempt from any liberalization commitment.

Subsidies provisions in the AoA are focused not on subsidies as a whole but on those that distort trade in agricultural products. Under the AoA subsidies connected with agriculture were placed into three negoti-

ated categories: an “amber box” for subsidies considered to be trade-distorting, a “green box” for subsidies considered to have little or no effect on trade and a “blue box” for subsidies which would normally be in the amber box but are not included because they are tied to limiting production. Levels of amber-box subsidies being applied by each WTO member were then assessed and, similar to the approach in the case of market access liberalization, the AoA required the reduction of amber-box subsidies by 20 per cent over 6 years for developed economies and 13.3 per cent over 10 years for developing economies. Least developed countries were not obliged to make any reductions. In the related area of export subsidies, the AoA similarly provided a methodology for recording the level of export subsidies granted by relevant WTO members, and specified commitments reflecting S&DT treatment both in the level of reductions and in the implementation periods.

Contingency protection within the AoA was conditioned by a “peace clause” provision supporting “due restraint” in the application of anti-dumping, countervailing and non-violation actions against trade in agricultural products, but not in the application of safeguards. Although the peace clause provision expired at the end of 2003, there is still some ambiguity about whether it continues to be applied in practice to restrain these three contingency measures to trade in agriculture (Steinberg and Josling, 2003). Conversely, it is notable that beyond leaving safeguard provisions off the list of contingency measures over which restraint should be exercised in agricultural trade, the AoA established a special safeguards (SSGs) mechanism which can be applied to a narrow list of sensitive agricultural products by certain WTO members. While the AoA contains provisions conditioning application of most contingency measures, it does not reduce recourse to safeguards and SSGs.

The AoA introduced a distinct set of multilateral disciplines for agriculture. It provides both a framework for trade in agricultural goods and a basis for negotiating further liberalization. Having described the multilateral trading rules on agriculture contained in the AoA, the following sections will illustrate rule-making with regard to coverage, domestic support and contingency protection in 18 selected RTAs. Following these three thematic sections, global conclusions are produced that analyse and assess the evolving context and manner in which rules governing trade in agriculture at the MTS and RTA levels interact.

Coverage of agriculture within the 18 RTAs under study

The coverage of agriculture in RTAs is typically a reflection of the situation prevailing at the multilateral level, but also an expansion (albeit discriminatory) of progress achieved multilaterally. Although the issue of

sector treatment is not addressed here, it is clear that contours of sectors which have been resistant to liberalization at the multilateral level are often traced by liberalization commitments at the regional level. Yet RTAs generally do reflect some progress in difficult sectors. Where several RTAs contain liberalization commitments in the same sensitive sector, increasing trade volumes between RTA members resulting from declining barriers to trade may make MFN-based liberalization in those sectors less difficult in the long run. On the frontier of this process is the potential for progress in non-tariff issues such as relaxation of stringent rules of origin in noteworthy sectors, e.g. as reflected with respect to cotton within the US-Morocco Free Trade Agreement (FTA), which is not covered in this study. This exception (para. 15 of art. 4.1) would allow Moroccan textile products woven with limited quantities of cotton from several efficient West African cotton producers to be imported preferentially into the United States.

The quality of coverage

Assessments of coverage that are comparable across different agreements are difficult, particularly where liberalization commitments under positive list approaches have been established at different levels of detail under the Harmonized System (HS). For this reason and the fact that details of special treatment for certain products are sometimes highly technical, figures contained in table 2.1 and the more detailed annex 2.1 reflect best estimates.

No simple conclusions may be drawn from table 2.1⁶ regarding patterns in the coverage of agriculture within RTAs. Although the sample of 18 RTAs demonstrates large variations in both the depth and breadth of coverage (i.e. number of tariff lines subject to total liberalization and those subject to varying forms of non-zero preferential treatment), averaged by economy the number of tariff lines appearing in the two columns “tariff lines not completely liberalized at the end of the transition period” and “tariff lines excluded from any liberalization commitments” are 74.4 and 60.3,⁷ respectively. The relatively minor difference between these two figures suggests that completely excluding tariff lines from any liberalization commitments is a more common approach than providing for less-than-zero preferential treatment (i.e. tariff preferences and TRQs). The large standard deviations behind each of these two averages, 255.4 and 249.3 respectively, demonstrate large variations in the breadth of coverage across the agreements.⁸ It should be noted that actual figures for coverage-related averages would have been substantially higher had data for several of the agreements been available and reflected. In short, the completeness of coverage suggested by the table is overstated. Fur-

Table 2.1 Coverage of agriculture within RTAs^a (Harmonized System 1–24)

Agreement	Approach for listing concessions ^b	Tariff lines not completely liberalized at end of transition period ^c	Tariff lines excluded from any liberalization commitments ^d
AFTA (ASEAN 6) ^e			
Brunei	Negative list	14	0
Indonesia		4	0
Malaysia		73	0
Philippines		62	0
Singapore		0	0
Thailand		5	0
ANZCERTA	Negative list	0	0
APEC	N/A	N/A	N/A
ASEAN-China Framework Agreement ^f (HS 1–8)			
China	Negative list	0	0
Brunei		0	0
Indonesia		0	0
Malaysia		N/A	N/A
Philippines		N/A	N/A
Singapore		0	0
Thailand		0	0
Canada-Chile			
Canada	Negative list	94	94
Chile		88	73
Canada-Costa Rica			
Canada	Comprehensive list	153 90	153 90
Costa Rica			
COMESA	Data not available	Data not available	Data not available
EU-South Africa			
EU	Negative list	495	282
South Africa		120	104
EU-Tunisia ^g			
EU	Positive list	(60)	N/A
Tunisia		(54)	N/A
EFTA-Turkey ^h	Positive list	N/A	N/A
European Union (EU)	Negative list	0	0
JSEPA			
Japan	Positive list	1,657	1,657
Singapore		0	0
Korea-Chile ^o			
Chile	Comprehensive list	40 39	40 15
Korea			
MERCOSUR	N/A	0	0
NAFTA			
Canada	Comprehensive list	70 85	51 70
Mexico			
United States		16	0

Table 2.1 (cont.)

Agreement	Approach for listing concessions ^b	Tariff lines not completely liberalized at end of transition period ^c	Tariff lines excluded from any liberalization commitments ^d
New Zealand-Singapore	Negative list	0	0
US-Australia	Comprehensive	0	0
Australia	list	196	83
United States			
US-Chile	Comprehensive	N/A	N/A
Chile ⁱ	list	0	0
United States			

Source: Agreement texts and national tariff schedules.

- a. In accordance with the approach of this study, the table deals only with qualitative and not quantitative aspects of coverage (i.e. trade weighting or trade flow analysis). Unless otherwise specified, data reflect regional liberalization commitments at the end of the implementation period for HS 1–24 at the 8/9 digit level.
- b. Under a negative list approach, tariff lines are completely liberalized unless identified for different treatment. Conversely, under a positive list approach, no liberalization commitments are made unless tariff lines are identified and liberalization commitments are listed. The designation “comprehensive list” appears where the concessions data appear to list the entire HS tariff tables of the member economies.
- c. Unless otherwise specified, the figures represent agricultural tariff lines not eligible for complete liberalization (including those subject to TRQs) at the end of the transition period. Figures appearing in parentheses “()” represent the number of tariff lines eligible for total liberalization at the end of the period.
- d. Figures represent tariff lines excluded under the agreement from any type of liberalization commitment.
- e. Products in the data appearing in the “Tariff lines not completely liberalized at end of transition period” column are products appearing on the SP and HSP lists on which tariff preferences, quantitative restrictions (QRs) and TRQs may be applied only during the transition period.
- f. Bilateral negotiations between China and the Philippines/Malaysia remain incomplete and are omitted from this table.
- g. The EU-Tunisia agreement relies on a complicated positive list approach which identifies commitments at the 4, 6, 7, 8 and 9 digit HS tariff line levels, meaning that the figures provided are inconsistent. See note i in annex 2.I for further details.
- h. The EFTA-Turkey agreement relies on a complicated positive list approach which identifies commitments at the 4, 6, 7, 8 and 9 digit HS tariff line levels. Meaningful data cannot be developed from the agreement text for the “Tariff lines not completely liberalized at end of transition period” and “Tariff lines excluded from any liberalization commitments” columns. This is due to the fact that article 5 of protocol A of EFTA-Turkey specifies that the agreement partners will treat agricultural imports from one another at least as favourably as in the case of their respective agreements with the European Union. Assessment of the relevant concessions in that agreement is beyond the scope of this study.
- i. See note 1 in annex 2.1.

ther details on the depth of coverage across these agreements may be found in annex 2.1, which contains data regarding the use of non-zero preferential tariffs as well as TRQs within these agreements.

Transparency of concessions

There are generally three approaches to establishing liberalization commitments within RTAs, including the negative, positive and comprehensive list approach employed by the AoA. Of these, the negative list approach is widely considered to be the most concise and transparent method. Under this approach, RTA members identify only products not subject to liberalization within the agreement. In contrast, RTAs employing a positive list approach identify only products on which liberalization commitments are made. The comprehensive list approach is self-explanatory, as all products and treatments are listed. Individual RTAs rely on positive, comprehensive or negative list approaches. In some instances, such as EU-Tunisia, different approaches are used for industrial as opposed to agricultural liberalizations within the same agreement.

The data in table 2.1 show that ASEAN and ASEAN-China both apply the negative list approach, North American RTAs tend towards comprehensive list approaches and those involving the EU/EFTA reflect a combination of negative and positive list approaches. In assessing the breadth and depth of agricultural coverage by RTAs, the European Union stands out as an RTA that has no exclusions, with NAFTA a close second. However, EU/EFTA agreements with non-EU/EFTA economies tend to have lower levels of ambition than North American agreements between NAFTA and non-NAFTA members. This relative lack of ambition may be assessed in terms of the average number of products excluded from total liberalization at the end of the transition period (breadth) as well as the restrictiveness of residual protection at the end of the transition periods (depth). Non-EU/EFTA/North American agreements tend to have very ambitious coverage, including the ASEAN agreement and the ASEAN-China Framework Agreement – the latter has no recorded exclusions at the HS 1–8 level (table 2.1). The outlier of Japan-Singapore is a large exception.

Relatively transparent and ambitious agreements such as Canada-Chile and Canada-Costa Rica take similar approaches to product coverage and preferential treatment, but may nonetheless reflect the use of agricultural concessions to gain concessions in other sectors. Reflecting ambitious breadth and depth, neither agreement relies on non-zero tariff preferences, and whereas Canada-Chile provides for a limited number of permanent TRQs, Canada-Costa Rica does not contain any. Both rely on complete exclusion from any liberalization commitments as the mainstay

for addressing sensitive products. Canada-Costa Rica reflects cross-sector linkages of liberalization commitments, as it makes a fair proportion of the liberalizations contingent on Costa Rica's removal of a free-zone regime.

MFN clauses and the MTS

US-Chile reflects several variations of product-specific "MFN clauses" that appear in North American RTAs where preferences provided for specified products are protected from more preferential trade concessions granted to future RTA partners. First, this RTA incorporates two MFN clauses that operate in the RTA on wheat and wine. Regarding wheat, a variable levy applied by Chile on wheat imports may never be higher than "the lesser of the prevailing customs duty applied on an MFN basis, or the customs duty applied to any other imports under any preferential arrangement" (para. 3 or annex 1 of annex 3.3). Second, a mutual MFN clause regarding wine specifies that if any wine-related concession granted by an RTA member to a non-RTA member is more favourable than that existing between the members, the same concession will be automatically applied to the other RTA member (para. 4 of app. A of s. I of annex 704.2 of chap. 7). Finally, the RTA members generally grant duty-free treatment for a quantity of sugar imports equal to the imports from the other member based on the most recent data available.

EFTA-Turkey reflects the complex trading relationships which foster the use of "blanket-style" MFN clauses reflected in EU/EFTA RTAs with non-members, and the convoluted trading relationships they introduce to the MTS. EFTA-Turkey represents an RTA between one member and a subset of RTA members which already have RTAs with another RTA containing multiple members and multiple additional RTAs. First, the EFTA-Turkey agreement contains separate lists of liberalization commitments provided by each of the EFTA members to Turkey and a single list of concessions provided by Turkey to the EFTA members as a whole. Then, for agricultural products not handled specifically within the EFTA-Turkey agreement "but not listed in the Annex to the Treaty Establishing the European Economic Community", EFTA members are to provide treatment to Turkey equivalent to that which EFTA members provide to the European Union, and Turkey is to do likewise (art. 5 of protocol A). Special considerations inherent in RTAs involving multiple members with differing levels of trade commitments *vis-à-vis* one another are reflected in the EU-Tunisia agreement, which contains an MFN clause providing that goods imported from Tunisia into the European Union shall not enjoy more favourable treatment than goods produced and traded between EU members (art. 21).

NAFTA and Korea-Chile both represent cases in which a synergistic relationship between multilateral and regional treatment in agriculture may be observed. While NAFTA came into force before the AoA, the provisions of the agreement anticipated the tariffication process that would become part of the AoA. NAFTA contains an MFN provision (para. 4 of app. A of chap. 7) requiring that any reductions in out-of-quota tariff rates for TRQs negotiated as part of the multilateral trade negotiations that are lower than NAFTA rates will be applied to other NAFTA members. Taking this concept a step further, Korea-Chile contains a liberalization commitment designated “DDA” for a number of agricultural products under which “tariff elimination schedule[s] shall be negotiated after the end of the Doha Development Agenda negotiations of the WTO” (s. A of app. 2 of the Tariff Elimination Schedule of Korea). Both agreements highlight that some sectors may be more pliable to liberalization at the multilateral level than at the RTA level.

Reverse tariff escalation: A model for special and differential treatment?

EU-Tunisia and EFTA-Turkey are interesting in several respects. As RTAs between developed and developing economies, both face difficulties liberalizing agricultural trade due to large differences in price levels for basic agricultural products within their respective domestic markets. In addressing this difficulty, these two agreements distinguish “agricultural” from “industrial” components in the liberalization commitments for a limited positive list of final products. Resembling an inverse tariff escalation mechanism, provisions contained in these agreements allow for liberalization commitments to be made on the industrial component of final products but not on the value of the basic agricultural goods from which the final products were derived. This trade policy mechanism allows for the domestic price levels of sensitive agricultural products to be insulated from liberalization commitments on imports of final products in which they are incorporated. While this mechanism allows for liberalization commitments which would otherwise not have been possible, it is an imperfect substitute for complete liberalization. Where EU-Tunisia bases the calculation of the agricultural component on the difference between the domestic price of the basic agricultural product and that in a third economy, EFTA-Turkey specifies that the difference is to be calculated based on the world price. Both agreements allow the application of multiple trade policy tools to adjust for the agricultural component in trade, including quantitative restrictions. Operating under a similar underlying principle, NAFTA addresses the difficult sugar sector with a provision allowing for duty-free imports of processed sugar products from

Mexico on the condition that the raw sugar incorporated into the final product originated from the United States (para. 8 of app. B of s. I of annex 704.2 of chap. 7).

Addressing difficulties involved in liberalization of seasonal agricultural products, the treatment of avocados in the US-Chile agreement is worth noting. Under US-Chile, a two-tiered seasonal TRQ is applied on avocado imports from Chile into the United States, with lower quantities during the US production seasons and higher quantities during the US off-season. Both TRQs are subject to elimination following a 12-year implementation period.

Highlights from non-EU/NAFTA-centred RTAs

APEC is a forum reliant on peer pressure and “open regionalism” under which liberalization negotiated at the regional level is implemented on an MFN basis outside the regional grouping. In 1994 APEC leaders agreed in Bogor, Indonesia, to the “Bogor Goals” under which leaders from member economies would work towards achieving the liberalization of trade in industrial goods and agricultural products by 2010 for developed members and 2020 for developing members. The approach of APEC in the area of agriculture is to develop a foundation for liberalizing trade in agricultural products throughout the region. A work-stream titled the APEC Food System is composed of technical cooperation activities and projects focusing on developing rural infrastructure, promoting free trade in food products and disseminating technological advances in food production and processing.

Among developing economy RTAs, the ASEAN Free Trade Area is interesting in that very few exclusively agricultural products are excluded from the Common Effective Preferential Tariff (CEPT) scheme which requires members to eliminate barriers to trade among the ASEAN 6 members by 2010. Excluded products registered by members under the sensitive products (SPs) and highly sensitive products (HSPs) lists must be reduced to at least 5 per cent and 20 per cent, respectively, by 2010. At that time, any quantitative and other non-tariff restrictions on trade in SPs and HSPs must be removed to bring them in line with rules for CEPT products.

Although the China-ASEAN Framework Agreement is not an RTA but an agreement to negotiate an RTA, it creates an “Early Harvest” category of products consisting of HS chapters 1–8 under which liberalization will eliminate duties between China and ASEAN members following a transition period. Malaysia and the Philippines have yet to complete negotiations with China under this agreement, but it is notable that none of the remaining ASEAN 6 members has listed any products under

the exclusion list of the Early Harvest programme. This is significant in that Thailand has reserved five SPs from the CEPT programme which it has not reserved from the Early Harvest programme, thus suggesting that the Early Harvest programme might eventually play a role in bringing these products under the CEPT. Although uncertainties remain, this may represent an example of interlocking RTAs making progress on difficult products.

Reflecting a set of agriculture-related policy objectives differing from contemporary RTAs, COMESA sets the goal of liberalizing internal trade in goods while recognizing that the “overall objectives of cooperation in the agricultural sector are the achievement of regional food security and rational agricultural production within the Common Market” (art. 129).

Conclusions on coverage of RTAs

This discussion of coverage may be considered within the context of market access and novel rule-making. In terms of market access, wide divergences in the quality of coverage reflected in the RTAs under study may nonetheless bring pressure to bear on existing restrictions in sensitive agricultural sectors. Such pressures may lead to the achievement of market openings in difficult sectors, as suggested by progress within the context of ASEAN-China which has not yet been achieved in ASEAN itself. In terms of rule-making, two significant variations of RTA-based MFN clauses applying at the product level and between entire RTAs should be the focus of increased attention. In addition, EU RTAs with developing countries establish what could be described as an inverse tariff escalation mechanism, which allows for trade in final goods produced from sensitive basic agricultural products that would otherwise not have been possible in the short run.

The hierarchy of preferential treatment has become an issue in some cases involving agricultural products, as reflected in “MFN clauses” appearing in some RTAs. These MFN clauses appear in two forms: those typically found in NAFTA that include product-specific MFN clauses contained in RTAs that prohibit earlier members from conferring more favourable treatment to new members in subsequent RTAs; and those typically found in EU-centred agreements that include blanket MFN clauses under which EU (and EFTA) members are guaranteed treatment no less preferential among EU and EFTA members than in RTAs with non-members. It should be noted that these MFN clauses are applicable to all concessions and not just those regarding agriculture. This practice limits the ability of new RTAs to make progress on liberalization beyond that achieved under earlier subsets of agreements.

To facilitate trade liberalization between developed and developing members in sensitive basic agricultural products, some RTAs apply trade policy mechanisms aimed at increasing trade in processed goods. RTAs with such mechanisms differentiate between liberalization commitments on the value added to sensitive basic agricultural products and those on basic agricultural products themselves. Although this mechanism remains a second-best alternative to complete trade liberalization, it enables trade in certain types of agricultural products that would otherwise be impossible. The economic effect of this trade policy mechanism is similar to that of inverse tariff escalation, and allows for increasing levels of value added within developing RTA members for an expanded range of agricultural goods. Although limited in scope, it might be seen as a model for wider liberalization of sensitive agricultural products in the context of S&DT provisions within the WTO.

Treatment of domestic support and export subsidies

As one of the most difficult topics in the AoA negotiations, it is not surprising that few of the 18 regional agreements considered address domestic subsidies (table 2.2). The general absence of provisions concerning domestic support within RTAs appears to defer potential disputes concerning them to multilateral trading rules. Only two RTAs take up the issue of harmonizing domestic support. The European Union integrates domestic support among its members through the Common Agricultural Policy (CAP), a subject that is beyond the scope of this study. The second exception is COMESA, which promotes rationalization and specialization. The COMESA objectives include the establishment of a common agricultural policy; regional food self-sufficiency; increased agricultural production and exports within and beyond the region; and the replacement of imports through production on a regional basis.

The fact that subsidies cannot be reduced preferentially (except export subsidies) has led to a second-best approach to addressing the trade-distorting results of domestic subsidies on internal RTA trade. Some RTAs aim to reduce subsidies for products that specifically impact on internal trade. For example, a continuing process of negotiations following the establishment of ANZCERTA has resulted in an RTA that restricts domestic subsidies on products which are intensively traded at the regional level (OECD, 2003: 135). Echoing ANZCERTA, Canada-Costa Rica contains mandatory consultation procedures designed to address situations in which domestic subsidies are considered to be affecting internal trade (art. III.13(3)). NAFTA contains best-endavour wording that recognizes the legitimacy of domestic support measures in agriculture

Table 2.2 Provisions on agricultural domestic support and export subsidies in RTAs

Agreement	Domestic support	Harmonization of domestic support	Applicability of export subsidies to internal trade	S&DT or technical cooperation
AFTA (ASEAN 6)	NP	NP	NP	NP
ANZCERTA	Not permitted if impacts internal trade	NP	Not permitted	NP
APEC	N/A	N/A	N/A	N/A
ASEAN-China Framework Agreement	Identified for further negotiation	NP	NP	NP
Canada-Chile	Institutional provisions	Institutional provisions	Not permitted*	NP
Canada-Costa Rica	Cooperation in WTO negotiations	NP	Not permitted	NP
COMESA	Cooperation through CAP	Cooperation through CAP	NP	Cooperation through CAP
EU-South Africa	NP	NP	NP	NP
EU-Tunisia	NP	NP	NP	NP
EFTA-Turkey	NP	NP	NP	NP
European Union (EU)	Cooperation through CAP	Cooperation through CAP	Not permitted	Cooperation through CAP
JSEPA	NP	NP	NP	NP
Korea-Chile	NP	NP	NP	NP
MERCOSUR	NP	NP	NP	NP
NAFTA	Best endeavour for reduction	NP	Not permitted*	NP
New Zealand-Singapore	NP	NP	Not permitted	NP
US-Australia	NP	NP	Not permitted*	NP
US-Chile	NP	NP	Not permitted*	NP

Source: Agreement texts.

NP signifies no provision found.

* Indicates that the prohibition on export subsidies in internal trade is waived for products which have received export subsidies when exported from non-RTA members into RTA members.

while supporting the evolution of domestic agricultural policies in a manner that reduces trade-distorting effects or is exempt from multilateral trading rules (art. 705).

In terms of cooperation provisions many RTAs establish special committees or institutions to govern the operation of the RTA, and some have special committees or institutions for agriculture. Among these, Canada-Chile stands out as one that places particular attention on the issue of domestic subsidies by establishing the independent Committee on Anti-dumping and Countervailing Measures with a mandate to “consult with a view to defining subsidy disciplines further and eliminating the need for domestic countervailing measures on trade between them” (art. M-05).

The approach to dealing with domestic subsidies in agriculture through cooperation in international negotiations is also reflected in Canada-Costa Rica and NAFTA. Canada-Costa Rica contains precise wording on objectives that the RTA members will pursue in WTO negotiations for rules on domestic agricultural subsidies at the multilateral level. These objectives include the maximum possible reduction of trade-distorting domestic support; establishing an overall limit on domestic support of all types; a review of the criteria for “green-box”⁹ subsidies; and agreement that green-box support should not be countervailable (art. III.13).

In the area of export subsidies, Canada-Chile contains a provision supporting multilateral negotiations on the elimination of export subsidies. Many of the RTAs surveyed contain provisions prohibiting export subsidies on intraregional trade, but a number of these allow export subsidies to be applied on internal trade where specific products also imported into the RTA from non-RTA members have benefited from export subsidies.

With the notable exceptions of the European Union (on national subsidies as opposed to EU subsidies) and COMESA, there is therefore a general absence of provisions concerning domestic support within RTAs. Although RTAs rarely contain binding obligations regarding domestic subsidies, some have taken creative policy approaches. At least one RTA (ANZCERTA) supports the removal of domestic subsidies in agricultural sectors on internal trade. This approach may perhaps have negative externalities by leading to a relative increase of subsidies in sectors that are not traded internally. Similarly, North American RTAs tend to ban the use of export subsidies on internal trade, although a portion of those allow their use to counterbalance export subsidies that have been applied to imports from non-RTA members. EU-centred (and EFTA-centred) RTAs are on the other hand silent on this issue. The potential for the trade effects of subsidies to be shifted outside RTAs provides a strong rationale for progress on domestic subsidies at the multilateral level.

Institutional mechanisms have been established under some RTAs with a mandate to facilitate the reduction of trade-distorting domestic support affecting internal trade. In the clearest indication of RTA provisions defining interaction with the MTS, several RTAs have provisions specifying cooperation to address trade-distorting agricultural subsidies in multilateral trade negotiations.

Contingency protection affecting agriculture

There have been a number of studies of contingency protection measures in RTAs¹⁰ that have focused primarily on anti-dumping, countervailing actions and general safeguards. The results of these are summarized in table 2.3 for the 18 RTAs studied. This section will seek to build on previous work by going into greater detail regarding the topics of transitional safeguards, SSGs and structural adjustment as they relate to agricultural liberalization within RTAs.

Transitional safeguards take different forms, but the most common type is that associated with NAFTA. The NAFTA safeguard was developed with a philosophy that safeguards should not be applicable to internal NAFTA trade following the transition period. During the transition period, NAFTA requires a technical test very similar to that contained in the WTO Agreement on Safeguards in order to apply a safeguard. Once the technical test is met, the level to which the tariff may be raised is capped. The duty applied under a NAFTA transitional safeguard may not exceed either the MFN duty rate of the product at the time the safeguard is being applied or the MFN duty rate of the product on the day before that RTA came into force. Finally, and most important, the RTA member applying the safeguard must negotiate compensation in the form of tariff concessions equal to the amount collected under the safeguard measure. Thus the NAFTA transitional safeguard measure has an inbuilt incentive for phase-out by the RTA member applying the measure. Other RTAs in the Americas (see table 2.3) apply similar transitional safeguards.

Both EU-South Africa and EU-Tunisia include a “transitional safeguard measure” that serves as an S&DT provision and may be applied only by the developing member. Significantly, the measures may be applied for the express purpose of assisting “infant industries or sectors facing serious difficulties” caused by increased imports from the European Union. Duties applied under this provision may not exceed the lower of 20 per cent *ad valorem* or the MFN duty rate of the product, and must maintain an element of preference for imports from the European Union.

Some RTAs have modelled SSGs on those in the AoA, providing them

Table 2.3 Applicability of contingency protection affecting agriculture in RTAs

Agreement	Anti-dumping	Counter-vailing actions	Safeguards ^a	Transitional safeguards ^b	Special safeguards ^c
AFTA (ASEAN)	Yes*	Yes*	NP	Yes*	Yes
ANZCERTA	No	Yes*	NP	No	NP
APEC	N/A	N/A	N/A	N/A	N/A
Canada-Chile	No	No	No*	Yes*	NP
Canada-Costa Rica	Yes*	NP	No*	Yes*	NP
China-ASEAN Framework Agreement ^d	Yes*	Yes*	Yes*	Yes*	NP
COMESA	Yes*	Yes*	Yes*	Yes	NP
EU-South Africa	Yes*	Yes*	Yes*	Yes	Yes
EFTA-Turkey	Yes*	Yes	Yes	NP	NP
EU-Tunisia	Yes*	NP	Yes	Yes	NP
European Union (EU)	No	No	No	Yes	NP
JSEPA	Yes*	Yes*	Yes*	Yes**	NP
Korea-Chile	Yes*	Yes*	Yes*	Yes**	NP
MERCOSUR	NP	NP	No	No	NP
NAFTA	Yes*	Yes*	No***	Yes**	Yes
New Zealand-Singapore	Yes*	Yes*	No	NP	NP
US-Australia	NP	NP	No***	Yes**	Yes
US-Chile	Yes*	NP	No***	Yes**	Yes

Source: Agreement texts.

NP signifies no provision found.

* Reference to WTO rules or use of similar rules.

** NAFTA-style rules; see text for explanation.

*** The safeguard may only be applied as part of a global action.

- This heading refers to general safeguards applicable on a global level and on internal trade which are often based on WTO rules.
- Transitional safeguards are normally applicable only during the transition period of the agreement, and rules governing their application are generally less stringent than those governing general safeguards.
- Some agreements contain "special safeguards" which are normally applicable only to a specified subset of particularly sensitive agricultural products. Rules governing their application are normally even less stringent than those governing transitional safeguards.
- All entries pending negotiation of rules as part of the RTA negotiations.

for a limited number of highly sensitive products. But the SSGs in RTAs depart from those in the AoA when it comes to the detailed provisions. NAFTA designates lists of products subject to SSGs, but unlike the AoA

does not specify the conditions that must be met to trigger their application, thereby providing discretion in their application. There are rules that then constrain the options available by specifying that SSGs may only be applied as TRQs, cannot be applied simultaneously with transitional safeguards and may only be applied during the transition period (paras 4 and 5 of art. 704). US-Chile, on the other hand, provides rules similar to AoA SSGs, such as pre-specifying the quantity or price levels of identified goods that will trigger the SSG, as well as capping duties at levels that provide preference for imports from RTA members. Notably, SSGs may not be applied to increase a zero in-quota duty for goods imported within that allotment. US-Australia provides what is probably the most sophisticated example of an SSG, under which triggers based on both quantity and price are specified for activating an SSG on beef imports. While the general SSG under US-Australia mirrors that of US-Chile, the restriction against the application of SSGs to zero-duty in-quota imports under TRQs is enhanced to include any in-quota imports.

EU-South Africa provides for an agriculture SSG with a less stringent technical test for application than the general safeguard clause. While the general safeguard clause in that agreement contains wording similar to that of the WTO Agreement on Safeguards, the agricultural safeguard relaxes the technical requirements for applying the safeguard but requires consultations with the Cooperation Council established under the agreement for an appropriate solution (art. 16).

Nearly all RTAs preserve recourse to anti-dumping and countervailing actions. For these types of contingency measures, most RTAs either contain technical requirements similar to those appearing in the corresponding WTO agreements or specifically refer to WTO rules. Trends and novelties uncovered in detailed analysis include the fact that North American FTAs tend to ban safeguards on internal trade after the transition period. All RTAs under study are free of SSGs by the end of their transition periods, with an infant industry safeguard available only to the developing country members. In North American RTAs banning safeguards following the transition period, there is a transitional mechanism designed to facilitate adherence to liberalization commitments that contain an inbuilt disincentive for application of safeguards; this also acts to hasten phase-out once the safeguard is applied. These safeguard mechanisms require the negotiation of compensation in terms of new trade concessions equivalent to the duty revenues collected from the transitional safeguard.

Rather than exclude particularly sensitive products from liberalization commitments, some RTAs employ SSG¹¹ provisions which mirror those provided under the AoA to a limited number of agricultural products. Importantly, SSGs appearing in the 18 RTAs under study are subject to

phase-out at the end of specified transition periods, thus locking in liberalization.

EU FTAs contain an S&DT transitional safeguard in RTAs between developed and developing economies that provides differentiated treatment to the developing member in a number of ways. First, only the developing member of the RTA may have recourse to this S&DT safeguard. Second, the technical requirements for the application of the S&DT safeguard are less stringent than for the general safeguard under the same agreement. Finally, these safeguards may be applied explicitly to assist “infant industries or sectors facing serious difficulties”, thus marking a novel application of safeguards in comparison to more common rationales for safeguards appearing at the multilateral and regional levels.

Global conclusions

The interaction between the RTAs and the MTS in agricultural matters tends to take the form of increased market access through non-MFN liberalization for RTA members linking with multilateral liberalization and experimental rule-making within the RTAs. The coverage section of this chapter certainly demonstrates that RTAs deliver some agricultural liberalization that would otherwise be unlikely or impossible at the multilateral level in the short run. However, attention should be paid not only to global welfare but also to the political economic implications of these increases in trade. From an economic perspective, an assessment of whether an RTA is on balance more trade-creating or trade-distorting provides a clear response to the overall question of whether RTAs interact with the MTS in manner that is welfare-enhancing at the global level.

However, progress in non-MFN liberalization in agriculture in RTAs must be balanced against the potential that such liberalization will create foreign as well as domestic constituencies against multilateral trade liberalization. This issue is salient to the current Doha round of trade negotiations. A related political economy issue is the negotiating power that preference-giving countries have *vis-à-vis* preference-receiving countries. The potential for the use of such negotiating power is reflected in Canada-Costa Rica, where liberalization by Canada on specified agricultural products was explicitly linked to concessions in an unrelated sector. In short, even where RTAs make progress compared to the MTS thanks to net trade-creating effects, it is still important to consider the impact on the MTS of creating constituencies against further multilateral liberalization and the redistribution of negotiating power.

Interaction between levels of rule-making can be considered in terms of explicit wording linking the two levels of agreement, *de facto* interaction and innovations at one level that may be taken up at the other. In terms of explicit interaction, several North American RTAs contain language requiring their signatories to take specific, common positions in multilateral agricultural negotiations. RTAs may also explicitly link progress in multilateral negotiations to concessions between signatories, such as in the Canada-Costa Rica and Korea-Chile RTAs. These types of interaction are generally worth noting, but should be the subject of more focused reflection.

In terms of *de facto* interactions between RTAs and the MTS, the employment of MFN clauses is an issue that should receive more consideration than it has until present. Product-specific MFN clauses, such as those existing with respect to wine and sugar in the case of US-Chile, serve to protect the relative level of preference on specific products. Worthy of more focused consideration, however, is the existence of blanket MFN clauses which protect core EU/EFTA members from the potential of trade concessions to RTA partners outside the European Union or EFTA being more favourable than those to EU/EFTA members. Blanket MFN clauses appear to establish hierarchies of access to preferential trade which set MFN (in the WTO sense) trade as a floor, non-core RTA members as an intermediate and core RTA members at the pinnacle of a multilayered regime of preferential trade. From this perspective, RTAs with blanket MFN clauses create a system of non-MFN trade that is based on the MTS and yet establishes a system of incentives against MFN liberalization at the non-core as well as the core RTA member levels.

In terms of innovations in rule-making, EU/EFTA RTAs with developing countries allow for partial liberalization of trade in sensitive agricultural products that otherwise could not have been liberalized. The EU/EFTA RTAs also offer an S&DT-type safeguard mechanism accessible on more lenient conditions for the developing country RTA signatories than the standard safeguard for protecting infant industries. These mechanisms that are not available under multilateral rules may provide a model for the DDA in agriculture or more broadly. The reverse tariff escalation mechanism addresses increasing levels of value added to agricultural exports from developing country RTA members. This mechanism facilitates more trade in agricultural products in which a developing country RTA member is likely to have comparative advantage while protecting sensitive agricultural commodities in the developed country RTA member. This might be seen as a way of addressing sensitive agricultural sectors that are at present holding back progress in agricultural negotiations. This type of provision might find its way into S&DT negotiations in

order to address concerns that liberalization will reduce “policy space” for development and regarding the difficulty of applying safeguards in developing countries due to capacity limitations. Such an S&DT-type safeguard could thus enhance confidence to engage in tariff liberalization by making safeguard actions more accessible to developing countries.

The coverage of international trade in agriculture by the MTS over the 10-year history of the AoA has seen increasing levels of international agricultural trade flows under RTAs. Rule-making for agricultural trade began in RTAs and set precedents for the AoA, and the RTA level continues to be vigorous and dynamic. This study has illustrated that some RTA rules on agriculture support the MTS while others weaken it. The political economy effect of preferential trade liberalization may therefore have two opposing influences on the future of MFN-based agricultural liberalization. It may prepare sensitive sectors for MFN liberalization through incremental non-MFN liberalization, or it may create additional foreign constituencies concerned with preference erosion and thus opposed to MFN liberalization. The outcome of the current DDA round of trade negotiations will shed further light on the evolving relationship between the MTS and RTAs.

Notes

1. The span of RTAs considered here is deliberately wide, in terms of the type of arrangements discussed and their status. Additional considerations such as the level of economic development between the members and geographic dispersion also played a role in the selection of RTAs. RTAs considered include APEC, a forum based essentially on peer pressure rather than binding rules; traditional free trade areas, such as NAFTA, without a common external tariff and with preferential rules of origin to avoid trade diversion from third parties; customs unions, such as MERCOSUR, with a common external tariff; and the European Union, an economic and monetary union entailing supranational authority and deep integration going well beyond trade. Within the four topical sections of this chapter, two agreements over which negotiations have already been completed but are not yet ratified by their respective governments have been included to keep the study as current as possible. In addition, reference is made in some places to agreements containing interesting initiatives which are still under negotiation.
2. These figures include RTAs notified under article XXIV of GATT 1994 covering goods (including agriculture) and the Enabling Clause covering RTAs between developing and least developed economies, but not those notified under GATS article V regarding services.
3. Including quantitative restrictions, variable levies, outright import bans and others.
4. A TRQ is two-step tariff under which the tariff applied on a type of goods increases from a lower to a higher level when imports of those goods rise above a quantitative threshold.
5. The 40 WTO members that actually completed the tariffication process had applied non-duty-based import measures on a collective average of 22 per cent of tariff lines prior to the tariffication process (WTO, 1999: 53).

6. It should be borne in mind that table 2.1 seeks to reveal purely qualitative as opposed to quantitative aspects of coverage (e.g. weighting liberalization commitments in terms of trade flows and others). It should also be noted that the data provided here are uneven due to the differing approaches that are taken within RTAs to the coverage of agricultural products.
7. Average based on data available by economy and may include the same economy more than once (depending on the number of RTAs in which it is involved). Total economies = 45. The following RTAs and individual economies are not reflected in the average due to incomplete data or as indicated: APEC (N/A), ASEAN-China Framework Agreement (due to the fact that it represents only HS 1–8), COMESA, EC-Tunisia, EFTA-Turkey and Chile (as part of US-Chile; US data are included).
8. See note 7 above for details on the data within this exercise.
9. Under the AoA, subsidies connected with agriculture were placed into three negotiated categories: an “amber box” holding subsidies considered to be trade-distorting; a “green box” holding subsidies considered to have little or no effect on trade; and a “blue box” containing subsidies which would normally be in the amber box but are not included because they are tied to limiting production.
10. For example, the contingency protection chapter of OECD (2003).
11. See the section above on “Key features of agricultural treatment within the multilateral trading system” for an explanation.

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Annex 2.1 Detailed coverage of agriculture within RTAs^a

(Harmonized System 1–24)

(A = B + C + D)

	A	B	C	D
Agreement	Tariff lines not completely liberalized at end of transition period ^b	Tariff lines excluded from any liberalization commitments ^c	Non-duty-free preferential tariffs ^d	TRQs not subject to complete liberalization at end of transition period
AFTA (ASEAN 6) ^f				
Brunei	14	0	14	NP ^g
Indonesia	4	0	4	NP
Malaysia	73	0	73	NP
Philippines	62	0	62	NP
Singapore	0	0	0	NP
Thailand	5	0	5	NP
ANZCERTA	0	0	0	0
APEC	N/A	N/A	N/A	N/A
ASEAN-China Framework Agreement ^h (HS 1–8)				
China	0	0	0	NP
Brunei	0	0	0	NP
Indonesia	0	0	0	NP
Malaysia	N/A	N/A	N/A	NP
Philippines	N/A	N/A	N/A	NP
Singapore	0	0	0	NP
Thailand	0	0	0	NP
Canada-Chile				
Canada	94	94	0	0
Chile	88	73	0	15 ^{b,c}

Canada-Costa Rica	153	153			
Canada	90	90	0	0	0
Costa Rica			0		0
COMESA					
EU-South Africa					
EU	495	282	170	43 ^a	0
South Africa	120	104	0	16 ^a	0
EU-Tunisia ⁱ					
EU	(60)	N/A	147	71 ^{b c}	0
Tunisia	(54)	N/A	107	39 ^{b c}	0
EFTA-Turkey ^j	N/A	N/A	N/A	N/A	N/A
European Union (EU)	0	0	0	0	0
JSEPA					
Japan	1,657	1,657	0		0
Singapore	0	0	0		0
Korea-Chile ^k					
Chile	40	40	0	0	0
Korea	39	15	359 (DDA)	6 ^c 18 (DDA)	0
MERCOSUR	0	0	0	0	0
NAFTA					
Canada	70	51	19	0	8
Mexico	85	70	15	0	16
United States	16	0	16	0	7
New Zealand-Singapore	0	0	0	0	0
	A	B	C	D	
US-Australia					
Australia	0	0	0	0	0
United States	196	83	0	113 ^a	95
US-Chile					
Chile ^l	N/A	N/A	N/A	N/A	N/A
United States	0	0	0	0	197

Source: Agreement texts and national tariff schedules.

- a. Unless otherwise specified, data reflect regional liberalization commitments at the end of the implementation period for HS 1–24 at the 8/9 digit level.
- b. Unless otherwise specified, the figures represent agricultural tariff lines not eligible for complete liberalization (including those subject to TRQs) at the end of the transition period. Figures appearing in parentheses “()” represent the number of tariff lines eligible for total liberalization at the end of the period.
- c. Figures represent tariff lines excluded under the agreement from any type of liberalization commitment.
- d. Includes all types of preferential partial liberalization except for TRQs.
- e. Products appearing under the data appearing in the “Tariff lines not completely liberalized at the end of the transition period” column are products listed as sensitive and highly sensitive products in the respective agreements on which tariff preferences and quantitative restrictions may be applied only during the transition period.
- f. Products in the data appearing in the “Tariff lines not completely liberalized at end of transition period” column are products appearing on the SP and HSP lists on which tariff preferences, QRs and TRQs may be applied only during the transition period.
- g. NP signifies that no provision was found.
- h. Bilateral negotiations between China and the Philippines/Malaysia remain incomplete and are omitted from this annex.
- i. The EU-Tunisia agreement relies on a complicated positive list approach which to varying degrees identifies commitments at the 4, 6, 7, 8 and 9 digit HS tariff line levels. Data provided under the “Preferential tariffs” heading should be relatively accurate due to consistency in the HS digits used to specify commitments. However, the TRQ data provided are flawed as they identify tariff line commitments at varying HS digit levels.
- j. The EFTA-Turkey agreement relies on a complicated positive list approach which identifies commitments at the 4, 6, 7, 8 and 9 digit HS tariff line levels. Meaningful data cannot be developed from the agreement text for the “Tariff lines not completely liberalized at end of transition period” and “Tariff lines excluded from any liberalization commitments” columns. This is due to the fact that article 5 of protocol A of EFTA-Turkey specifies that the agreement partners will treat agricultural imports from one another at least as favourably as in the case of their respective agreements with the European Union. Assessment of the relevant concessions in that agreement is beyond the scope of this study.
- k. Tariff lines marked in the Korean liberalization schedule for tariff elimination negotiations following the conclusion of the Doha Development Agenda negotiations are marked “(DDA)” in this annex.
- l. The US-Chile agreement identifies 172 tariff line items for special treatment specified in Spanish. They were not analysed.

The interaction between levels of rule-making in international trade and investment: The case of sanitary and phytosanitary measures

Grant E. Isaac

Introduction

An enduring issue in the study of economic diplomacy is the role of rules in regional trade agreements (RTAs) that exist between national rules determined unilaterally and multilaterally agreed rules (Winters, 1996, 2000; World Bank, 2000; Ethier, 1998; Krishna, 1998; Bhagwati and Panagariya, 1996; Arndt, 1994; Bhagwati, 1991, 1994; Baldwin, 1993).

From a practical perspective this is indeed an important issue. While the member states of the World Trade Organization (WTO) have faced difficulties launching and sustaining multilateral trade negotiations, there has also been an increased emphasis upon regional trade liberalization. For example, through its policy of “competitive liberalization” the United States has pursued bilateral agreements with countries in Central and South America as part of the broader effort to create the Free Trade Area of the Americas (FTAA). Similarly, its recent expansion to include Central and Eastern European countries has solidified the dominance of the European Union as a regional arrangement. Similar regionalization efforts are under way in the Pacific Rim as well as in Africa under the leadership of South Africa.

While RTAs are a reality, there is little consensus on the *drivers* for these agreements and their subsequent *impact* upon other levels of governance or rule-making – especially at the multilateral level – in the international trading system. With respect to drivers, there appears to be an interaction between RTAs and the multilateral trade rules, but the

causation is not clear. Is the rise of RTAs driven by a desire to kick-start multilateral action, or is the rise of RTAs causing multilateral inaction (Hoekman and Kostecki, 2001; Bagwell and Staiger, 1998; Baldwin, 1997; WTO, 1995; Kirkpatrick, 1994; Krugman, 1993; Whalley, 1993)? The former suggests that RTAs provide states with the experience and confidence to multilateralize their trade liberalization efforts. From such a perspective, the recent lack of success at the multilateral level can be explained as a temporary retreat to allow countries to deal with market access liberalization on a smaller scale first and then to commit to multilateral disciplines. The latter perspective suggests that the emphasis on RTAs indicates a decreased commitment to multilateralism in response to a perception that it has reached its limits. This perspective thus implies a permanent retreat from top-down multilateral rules, which may be domestically inappropriate, towards clusters of like-minded groups. Therefore, explaining the drivers for RTAs is a crucial if we are to understand the interaction between RTAs and other levels of rule-making in the international trading system.

Following from this discussion on drivers is the issue of the *impact* of RTAs upon other levels of rule-making. Consider the first perspective. In the short run RTAs may divert trade, but experience gained with rule-making at a regional level will enhance countries' confidence to accept multilateral rules. In other words, the impact of RTAs would be to facilitate convergence of domestic rules with those specified by the multilateral trading system. From the second perspective RTAs entrench particular rules or institutional, legal and regulatory path dependencies that result in a structural divergence in rule-making, rendering common multilateral rules much more difficult, if not impossible, to achieve.

Unsurprisingly, these two perspectives result in very different policy conclusions regarding the role of RTAs in the efficacy, governance and accountability of the international trading system. This chapter therefore argues that in order to judge which of these perspectives is closer to reality, and thus understand the interaction between regional and multilateral levels, it is necessary to assess both the *drivers* and the *impact* of regional rule-making in each particular policy area, as well as the trajectory and resiliency of the regional policies. This contextualization is crucial, because what drives RTAs and their impact is likely to vary with policy area and over time.

SPS measures: From regional to multilateral to regional rule-making

In this chapter the interaction of regional and multilateral levels of rule-making is examined in the context of sanitary and phytosanitary (SPS)

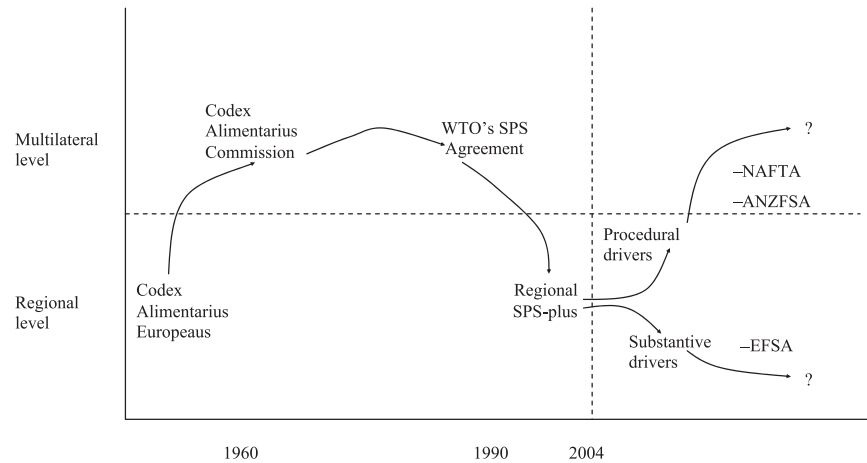


Figure 3.1 Evolution of SPS measures/dynamic nature of the interaction

measures. These are food safety measures pertaining to human, animal and plant health. As non-tariff market access barriers, SPS rules have proved to be particularly difficult because they represent a form of deeper integration in which rules and norms are inextricably linked with domestic political economy conditions. As these conditions differ, regulatory market access rules differ, becoming trade barriers for products approved as safe in one jurisdiction yet not approved as safe in another jurisdiction.

Figure 3.1 illustrates the evolution of SPS measures over the past 40 years, and reveals that the dominant level of rule-making has shifted from the regional level to the multilateral level and back to the regional level. The internationalization of SPS measures began with the development of a regional food code in Europe – the Codex Alimentarius Europeus – following the Second World War. This success with regional rule-making prompted the establishment of a multilateral food code – the Codex Alimentarius – in the early 1960s. The Codex was established under the auspices of the UN Food and Agriculture Organization and the World Health Organization. Hence, rule-making for sanitary measures shifted from a regional level to being a multilateral exercise in which leading international scientists – an epistemic community of experts – participated. From 1963 until 1995 the multilateral Codex Alimentarius Commission essentially operated below the radar in its science-based rule-making activities (Isaac, 2002).

Trade liberalization efforts in the Uruguay Round led to the establishment of the Agreement on Sanitary and Phytosanitary Measures (SPS Agreement), which explicitly identified the Codex as the credible international scientific organization for establishing both food standards and

the legitimate procedures for setting standards. Rather than being the final step in the process of multilateralization, this integration of food standards under trade disciplines has led to some particularly complex trade tensions and disputes (Marceau and Trachtman, 2002; Perdakis, Kerr and Hobbs, 2001; Mansour and Bennett, 2000). That is, while the intended objective of the agreement was to discipline the use of SPS measures in order simultaneously to ensure human, animal and plant safety while preventing such measures from becoming disguised agri-food protectionism, the actual effect has been to illustrate just how difficult it is to establish universal trade liberalization rules governing the deep integration of domestic safety and health regulations.

In response, the focus of SPS rule-making has essentially returned to the regional level as countries have sought to remedy their perceived disaffections with the multilateral rules through additional disciplines established in regional arrangements. However, as illustrated in figure 3.1, the additional disciplines seem to fall into two categories: procedural disciplines and substantive disciplines that go beyond existing multilateral interpretations of the rules. As figure 3.1 suggests, regional procedural disciplines can be multilateralized while substantive regional disciplines may entrench departures from multilateral rule-making.

Given the complex interaction between the multilateral and regional levels of SPS rule-making, the notion that the multilateralization of SPS measures represents only an *experiment* with deeper integration cannot be ignored – indeed, it is the focus of this chapter. The research question explored in this chapter is thus: what are the drivers for and the impacts of the shifts in the levels of SPS rule-making (regionalization, multilateralization, regionalization) shown in figure 3.1?

This first requires a thorough understanding of the SPS rule-making at the WTO, which is the subject of the following section. This will argue that several important ambiguities in the multilateral rules, such as those pertaining to the appropriate use of the risk analysis approach and the precautionary approach, have been behind the re-emergence of the regional level in SPS rule-making. In the section that follows, the *drivers* and *impacts* of the regionalization of SPS measures are examined. Here the challenge is to disentangle factors associated with the SPS case from those that also shape other policy areas, such as investment, services, etc. The final section draws together some conclusions and explores some implications.

SPS measures: Multilateral rules and regional pressures

The modern international trading system was intended to be a principles-based regime built on the national treatment (NT) provisions of GATT

1948 article I, which requires foreign products to be treated like domestic products, and the most-favoured nation (MFN) provisions of article III, which requires non-discrimination between like products originating from different countries. In order to operationalize these two concepts, products were grouped together into “like” categories based on their end-use characteristics and not on the processes and production methods (PPMs) used.¹ The focus on like products was to prevent the often significant differences in levels of technological development between trading partners from being used as a barrier to market entry.² Hence, the like-products concept has emerged as a *de facto* third principle of non-discrimination whereby all like products of domestic or foreign origin are to be treated the same regardless of the PPMs used in their production.

Non-discrimination may be considered as a baseline or default principle for domestic policies to meet in order to remain trade-compliant. That is, if a country puts in place a policy that treats all foreign like products the same as domestic like products in terms of market access approvals, the policy is likely to be found trade-compliant.

Non-discrimination has worked well for manufactured industrial goods, but was never really applied to rules affecting trade in food because GATT 1948 was unclear on the interface between trade rules and domestic food safety measures. Signatory countries retained significant discretion to establish their own food safety and food quality regulations in accordance with articles XI and XX(b) of GATT, provided these were not applied in such a manner as to cause arbitrary or unjustifiable discrimination between countries or disguised restrictions on trade.³ The multilateral rules therefore provided little discipline on the use and abuse of SPS measures.

The SPS Agreement: Background, disciplines and controversies

Efforts to find a better balance between non-discrimination and the pursuit of legitimate public health objectives were driven by a range of interests frustrated with the discretionary and arbitrary food safety measures applied under GATT 1948.⁴ These efforts found expression in the SPS Agreement of 1994, which requires countries to adhere to the principle of non-discrimination unless they have sufficient scientific evidence of food, animal or plant safety and health risks.⁵ If the SPS Agreement was going to focus on sufficient science, it had to be linked to credible scientific rule-making organizations, preferably at the multilateral level. The Codex Alimentarius Commission was identified as such an organization for food safety measures, while the International Office of Epizootics

(OIE) was identified for animal safety and the International Plant Protection Convention (IPPC) was identified for plant safety.

Such an alignment of trade disciplines with these multilateral scientific organizations was consistent with the increasing “scientification” of public policy occurring within many developed countries. For example, in 1983 the US-based National Academy of Sciences published its “Redbook” on science and public policy in which it was argued that science should be brought into rule-making for two reasons (National Academy of Sciences, 1983). First, scientific analysis has long striven to disentangle normative values from scientific discovery, creating a “universality” to scientific procedures and results not present in social beliefs, morals and ethics. Second, while scientific disagreement does occur, the analytical methodology of science essentially permits a dispute resolution mechanism whereby conflicting results are evaluated across methodologies and experimental protocols. This elevated role for science in public policy was solidified through the Redbook’s three-part risk analysis framework (RAF) for regulatory oversight: risk assessment, risk management and risk communication. The objective in a risk assessment is to develop – to the extent possible – objective, neutral and transparent information about the risks of a particular innovation, including hazard identification, exposure assessment and risk characterization according to accepted scientific methods and statistical inference techniques. The objective of risk management is risk reduction and prevention through policy decisions based on the objective risk assessment information. The Redbook specified that the risk assessment and risk management functions should be institutionally separated. Finally, the objective of risk communication is the two-way flow of information between the risk assessors and risk managers as well as the stakeholders in the regulatory procedure, including the general public. It is clear from the above that this elevated role for science in the public policy process requires an elevated role for scientists as well, hence rule-making or the setting of norms and standards becomes a function of qualified and accredited scientists. The SPS Agreement draws heavily upon the nomenclature of the RAF, and the standards and standards-setting procedures of its credible scientific affiliates – the Codex, the OIE and the IPPC – fit well with this scientification of public policy.

The SPS Agreement contains a regulatory safeguard that grants WTO members the right to restrict or prevent imports through the use of mandatory SPS measures to protect human, animal or plant safety and health⁶ if a *legitimate justification* exists.⁷ In fact, there are three provisions that permit discriminatory unilateral action. First, WTO members may discriminate against imports when risks are specific to the products of a particular country (art. 2:3). In this the agreement recognizes that different regions with different geographical conditions and agronomic

practices face different incidences of pests and disease. As a result, it may not be possible or necessary to establish uniform SPS measures to apply to products from all regions. WTO members are therefore not required to grant NT or MFN status to agricultural exporters whose products may contaminate the domestic food supply. It is explicitly recognized in the SPS Agreement that these two fundamental concepts of non-discrimination cannot apply in a general fashion when the issue is food safety measures.

Second, WTO members may also establish domestic SPS measures higher than the accepted international standard if there is *legitimate justification* for doing so (SPS Agreement, art. 3:3). Generally, international trade agreements commit members to adopt international standards if available; however, the SPS Agreement, in a form of “right to regulate” provision, permits members to establish even higher standards. That is, the SPS Agreement creates a regulatory floor but not a regulatory ceiling. Here, it is recognized in the agreement that domestic food safety regulations are not easily standardized to an international norm due to – often quite disparate – political economy factors within particular jurisdictions, such as experiences with failures in the domestic food safety system.

Third, WTO members may establish provisional SPS measures based on precaution in the event that there is insufficient scientific evidence to conduct an appropriate risk assessment.⁸ That is, members are permitted to establish temporary trade barriers based on the precautionary approach. These barriers can remain in place until enough scientific evidence about the risk has been compiled. In the SPS Agreement it is recognized that science has its limits, and so a precautionary trigger is included to deal with situations in which there is insufficient scientific information to make a proper risk assessment.

The SPS Agreement is thus an incredibly powerful international agreement. It allows a member country with a *legitimate justification* for an SPS-related measure the unilateral right under the WTO to impose trade barriers that cannot be challenged by other members. As figure 3.1 suggests, it appeared that by 1995 the multilateralization of SPS measures was completely codified in an international trade agreement. Moreover, the agreement itself was backed by credible multilateral scientific organizations committed to the RAF in setting standards and the development of standards-setting procedures.

“Unconstructive” ambiguities and regionalization pressures

Optimistically, it had appeared that a significant win-win for both public safety and international commerce had been achieved through the

science-based SPS Agreement. But considerable ambiguity surrounded how the SPS Agreement could be appropriately interpreted and applied. Different countries interpret their rights and obligations differently when it comes to implementing the multilateral agreement in domestic rules, resulting in major trade controversies. These ambiguities, which take three major forms, have led to disaffections with the multilateral systems and hence a shift to the regional level of rule-making, and cannot therefore be considered as “constructive”, to employ the term sometimes used to describe ambiguous wording in the text of trade agreements.

Ambiguity number one: Legitimate justification

The first, and perhaps most important, ambiguity lies with the interpretation of a “legitimate justification”. Given that the unilateral market access power of the SPS Agreement can be wielded by member states with such a justification, it is crucial at this point to define what is meant by a legitimate justification. According to the agreement, a legitimate unilateral SPS measure must be “based on scientific principles” and cannot be maintained “without sufficient scientific evidence” unless it is a temporary, precautionary measure (SPS Agreement, art. 2:2). The science-based measures adopted must be proportional to the risk that is being targeted.

As mentioned above, the WTO does not determine the sufficiency of scientific evidence. Instead, it defers to the Codex Alimentarius Commission (CAC) for food safety, the OIE for animal safety and the IPPC for plant safety (SPS Agreement, art. 5:1). Sufficient scientific evidence is evidence that conforms to the standards or standard-setting procedures of these three organizations, which have all adopted the nomenclature and intent of the RAF.⁹ In other words, scientific justification is crucial in supporting the legitimacy of the domestic measure in the event of a trade challenge.¹⁰ In a trade dispute a WTO panel is likely to seek scientific advice from the CAC, and without an acceptable scientific justification it is unlikely a WTO panel or the appellate body would support a unilateral SPS measure. In this sense, even if WTO members have not adopted the Codex or other international standards, it is important that their domestic food safety measures remain congruent with the international risk analysis approach of the CAC.¹¹

At first glance it may appear that, due to the apparently widespread adoption of the RAF in domestic food safety regulations, the similarly constructed multilateral rules and provisions in the SPS Agreement are well specified and leave little room for controversy.¹² According to the RAF, the regulatory challenge is to maximize the benefits of technological progress while minimizing the risks through technological precaution.

Table 3.1 Regulatory trajectories for biotechnology

	The risk analysis framework	
	Scientific rationality	Social rationality
<i>General regulatory issues</i>		
Belief	Technological progress	Technological precaution
Type of risk	Recognized Hypothetical	Recognized Hypothetical <i>and</i> speculative
Substantial equivalence	Accepts substantial equivalence	Rejects substantial equivalence
Science or other in risk assessment	Safety Health	Safety Health Quality “Other legitimate factors”
Burden of proof	Traditional: innocent until proven guilty	Guilty until proven innocent
Risk tolerance	Minimum risk	Zero risk
Science or other in risk management	Safety or hazard basis: risk management is for risk reduction and prevention only Science <i>makes</i> the regulatory decision	Broader socio-economic concerns: risk management is for social responsiveness Science only <i>informs</i> the regulatory decision
<i>Specific regulatory issues</i>		
Precautionary principle	Scientific interpretation	Social interpretation
Focus	Product-based, novel applications	Process- or technology- based
Structure	Vertical, existing structures	Horizontal, new structures
Participation	Narrow, technical experts Judicial decision-making	Wide, “social dimensions” Consensual decision- making
Mandatory labelling strategy	Based on safety or hazard	Based on consumers’ right to know

Source: Isaac (2002).

But while the RAF is widely viewed as the appropriate approach, two quite distinct trajectories have come to be used to implement it: the scientific rationality trajectory and the social rationality trajectory (table 3.1). In these circumstances what constitutes a legitimate scientific justification can differ significantly from country to country (or region to region) depending on what trajectory is used, even though the rules look similar in intent.

At the heart of the difference between the scientific rationality and the social rationality trajectories is a fundamental difference in the belief about the appropriate role of science and technology in society, which shapes the respective risk-benefit analysis. Consistent with the previous discussion on knowledge-based growth, scientific rationality holds that technology yields innovations and enhances efficiency; enhanced efficiency leads in turn to economic development and growth, producing higher incomes. As incomes go up, demand increases for more stringent social regulations such as for food safety and environmental protection. The result is a regulatory race to the top made possible by scientific advancements.¹³

This scientifically rational commitment to technological progress gives rise to the scientific rationality regulatory trajectory (middle column in table 3.1). Regulatory intervention requires a scientific justification of risk, either recognized risks (for which there are data for determining risks) or hypothetical risks (for which there are no data, but accepted analytical methods for determining risks). Substantial equivalence is used as a “gateway” regulatory principle to determine whether or not applications using the new technologies have the same risks as similar applications using old technologies. If yes, then the new technology is deemed “substantially equivalent” and regulated in the same manner as old technologies. If no, then the new technology is deemed “novel” and regulated according to new regulations designed to identify and assess novel risks. The risks that are assessed primarily involve safety (short-term) and health (long-term) risks, rather than issues of quality or socio-economic “risks” from the new technology. Accordingly, the regulatory burden of proof is that the technology is considered safe if – at this point – it has not been shown to be unsafe. Moreover, risk and safety are probabilistic terms; there is no such thing as either *zero risk* or *perfectly safe* under the scientific rationality trajectory. The objective of risk management is limited to the reduction and prevention of actual risks identified through scientific risk assessments, and not assuaging unsubstantiated public risk perceptions. As such, the information gathered in the risk assessment stage essentially determines the outcome, and little or no additional, non-scientific information is considered to be relevant.

In contrast, the social rationality trajectory of the RAF views technology very differently (right-hand column in table 3.1). Science and technology are viewed not as “drivers of economic development” but as one facet of society, where society is a normative construct composed of the preferences and concerns of all constituents. In this light, science is not an abstract exercise in discovering universal facts. Instead, the very questions asked are inextricably linked with the normative construct. Moreover, science and technology bring change, yet change disrupts the pre-

vailing normative construct. Given this perspective, the social rationality approach supports regulatory policies that ensure technological precaution (Hathcock, 2000). If science is going to bring change, it is important to make sure that *all* impacts of this change are dealt with in a socially responsive manner and are not left to the competitive forces of the market.¹⁴ This focus on technological precaution drives the rest of the social rationality regulatory trajectory.

The problem arises when two member states of the WTO both support the RAF in general, but support the opposing regulatory trajectories. What constitutes a legitimate justification to one member would not be considered legitimate to another. The WTO's Committee on Sanitary and Phytosanitary Measures tracks specific trade concerns (STCs) which are brought to its attention by one member concerned about the SPS-related market access rules established by another. Since January 1995 154 STCs have been raised: 26 per cent relate to food safety concerns, 30 per cent to plant health concerns, 40 per cent to animal health and zoonoses and 4 per cent to other issues such as certification requirements or translation (WTO, 2003).

In some cases the STC cannot be resolved and becomes a trade dispute. This was, for example, the case in perhaps the best-known dispute associated with the SPS Agreement – the Canadian and US complaint against the European Union over the ban on hormone-treated beef. This case illustrates the differences between the more social rationality trajectory used by the European Union and the more scientific rationality trajectory used in North America (Redick, 2000). In this case the WTO panel, backed by the WTO appellate body, ruled against the EU ban and the European Union's use of a social interpretation of the precautionary principle, recommending that the European Union bring its measures into conformity with its SPS obligations.

With respect to the regulatory trajectories assessed in table 3.1 it appears therefore that an appropriate RAF approach must include a comprehensive hypothetical risk assessment focused on the identifiable hazards to support the trade-restricting measure. Risk assessments based on speculative risks or the social interpretation of the precautionary principle would not be deemed legitimate assessments according to these principles. In other words, the WTO rulings essentially rejected the social rationality approach to the RAF, and hence leave the European Union with the task of trying to introduce additional cultural/social provisions into the SPS rules that would better reflect domestic circumstances. The scientific risk assessment information was decisive despite the overwhelming socio-economic factors calling for a ban. This dispute illustrates a severe controversy within the multilateral SPS Agreement where the two pillars of the international trading system – the European Union and

North America, with their equivalent levels of scientific expertise and economic development – differ in their interpretations of a “legitimate justification”. Until some kind of rapprochement can be achieved on this crucial issue of appropriate domestic safety regulations, support for multi-lateral SPS rule-making will be reduced in favour of support for regional SPS rule-making that accounts for the risk analysis approach.

Ambiguity number two: Precautionary approach

Another source of ambiguity in the multilateral rules on SPS measures, related closely to the first, is associated with the acceptable interpretation and use of the precautionary approach in the SPS Agreement. According to article 5:7, WTO members may adopt temporary precautionary bans to prevent the introduction of risks when sufficient scientific evidence is absent. The problem here does not lie with this provision; indeed, it is a necessary provision that empowers all WTO members to act to protect human, animal and plant safety and health in the event of a perceived crisis. The problem lies, however, with *removing* the provision once it is triggered. The SPS Agreement is silent on the steps that need to be taken by a member country which has lost international market access because trading partners have invoked this provision. For example, when a single case of BSE (bovine spongiform encephalitis) was discovered in Canada it immediately lost access to 34 markets that – quite legitimately – established temporary precautionary bans. Canada took measures which it believed had identified, isolated and eradicated the risk that any BSE-infected animals would enter the food supply, and animal health experts from the OIE vetted these and confirmed that the Canadian measures had been effective. Yet many important markets remained closed or only partially open for a considerable period of time.¹⁵ The ambiguity here arises because of an absence of any agreed procedures or even a harmonized blueprint for opening markets after temporary precautionary bans have been invoked. In turn, this has led to calls for additional administrative disciplines on the SPS measures in order to streamline the market access process. Greater clarification is needed in the SPS Agreement on how long is “temporary” and on the quantity and type of scientific evidence that is sufficient to revoke a temporary measure.

Ambiguity number three: Regulatory boundary

Another source of ambiguity arises from the fact that the SPS Agreement sets a regulatory floor but not a ceiling. According to the agreement, members are committed to both the international harmonization of SPS measures (subject to the three international scientific organizations) and

the mutual recognition of measures employed by other members. With respect to mutual recognition, members are committed, in principle, to granting equivalence to the SPS measures adopted by exporting countries “if the exporting Member objectively demonstrates to the importing Member that its measures achieve the importing Member’s appropriate level of sanitary or phytosanitary protection” (SPS Agreement, art. 4:1). To facilitate the process, the importing member must be allowed to conduct a conformance assessment including inspection, testing, monitoring and evaluation of the measures in place in the exporting member. The problem here is that the agreement is silent on the limits that exist for countries to use rules for inspection and monitoring that are substantially above those of other WTO members. Indeed, this issue is related to the discussion above, because many of the markets that continued to ban Canadian beef products – such as Japan – had domestic traceability and slaughtering regulations much more stringent than those of Canada. Therefore, while there is a minimum level of SPS measures that must be met, should a maximum level of stringency be set for such standards/rules?

Ambiguity number four: Like products

Another source of ambiguity is associated with the operationalization of the like-products concept within the SPS Agreement. While the principle of non-discrimination limits the focus of trade rules to “like products”, it is obvious that some SPS-related risks may, in fact, be associated not with the end-use characteristics of a product but rather with the PPMs employed. Indeed, this is at the heart of the WTO trade disputes over both beef hormones and genetically modified crops (Isaac and Kerr, 2003, 2004). In both cases the European Union delayed or denied market access to products from North America on the grounds of PPM technologies that Canada and the United States argue had neither safety nor quality impacts on the end-use characteristics of the final product. The agreement is relatively silent with respect to the legitimacy of PPM-based SPS market access barriers and greater clarification is required. In this case, additional SPS disciplines may be desired to achieve either greater administrative clarity or a clarity with regard to the role of PPMs in more culture-related consumer purchasing decisions.

Ambiguity number five: Socio-economic considerations

Another source of ambiguity, which the beef hormones case also illustrated, is associated with the role of socio-economic considerations in risk assessment. The SPS Agreement permits members to establish SPS

measures based on scientific risk as well as broader assessments of risk including relevant economic factors, such as “the potential damage in terms of loss of production or sales in the event of the entry, establishment or spread of the disease or pest; the costs of control or eradication in the territory of the importing Member; and the relative cost-effectiveness of alternative approaches to limiting risks” (SPS Agreement, art. 5:3). Trade agreements traditionally avoid such socio-economic assessments because of their inherent subjective character. Indeed, it has been argued that the WTO attempts to depoliticize trade and make it a function of comparative advantage by insulating trade agreements from socio-economic assessments (WTO, 1995). However, in the SPS Agreement it is recognized that imported risks to human, animal and plant safety and health are likely to have perhaps quite significant socio-economic impacts. The inclusion of article 5:3 introduces significant ambiguity concerning how socio-economic assessments should be worked into legitimate justifications based on sufficient scientific evidence. None of the international scientific organizations on which the WTO has relied provides much assistance, because they do not really consider socio-economic factors. So it is unclear as to how and when such factors should be legitimately included, despite the fact that many members are actively exploring ways to do just this.

Summary

This section has tracked the creation and evolution of SPS measures and their rule-making. Initially rooted at the regional level, SPS rule-making became a multilateral function of international scientific organizations, resulting in the creation of the SPS Agreement under the WTO. But experience with the SPS Agreement reveals that while it is powerful in terms of the rights it establishes, it is ambiguous in terms of how legitimately to exercise those rights. Different approaches to the role of science in food standards produce different market access rules, leading to trade irritants and, sometimes, trade disputes.

Due to this ambiguity, the promise of multilateral food safety standards under the WTO has not been achieved and a new regionalism appears to have taken hold in this policy area. In other words, the ambiguity in WTO rules has been a crucial *driver* in the shift from the multilateral level to the regional level of rule-making as members use the regional level to clarify the rules or set precedents in rule-making that promote international rules which meet domestic SPS interests. This has occurred in two ways. The first has been to include SPS measures into regional trade agreements – such as in chapter 7 of NAFTA – which typically adopt the multilateral rule-making functions of the WTO’s SPS Agreement. Here,

SPS measures are still based upon a policed national treatment or regulatory competition model of international integration – which does not create supranational rule-making structures. The second involves regional rule-making functions through regional food standards authorities (RFSAs), such as the European Food Safety Authority (EFSA) and the Australia-New Zealand Food Standards Agency (ANZFS), which entails close regulatory coordination with supranational rule-making agencies determining regional SPS measures.¹⁶ In the next section, the *drivers* for the regional shift are categorized and their *impacts* are assessed.

SPS measures and RTAs

The power and ambiguity of the multilateral SPS Agreement have been a source of dissatisfaction for many WTO members, who have called for additional disciplines to be included in the SPS Agreement that more accurately reflect domestic rules and rule-making realities. From the discussion above, it is possible to categorize the *drivers* for an increasing regionalization of food standards according to one of two objectives. The first – procedural drivers – are associated largely with members who are satisfied with the science-based foundation of the SPS Agreement but dissatisfied with procedural issues such as conformance assessment, which if not done in a timely manner creates market access problems. The second – substantive drivers – are associated largely with members who are dissatisfied with the science-based foundation of the SPS Agreement and are seeking to broaden the legitimate justifications for discrimination beyond just a science basis. Whatever is driving the change, however, greater emphasis has been placed on incorporating additional SPS measures – or SPS-plus measures – at the regional level to correct the perceived shortcomings of the multilateral agreement.

The *impact* of this regional focus upon multilateral SPS rule-making is, however, dramatically different depending upon the driver. Procedural drivers allow for a regional rectification of procedural impediments that then easily flows back up to create a procedurally streamlined multilateral science-based SPS Agreement, because it does not challenge any of the fundamental principles of the multilateral agreement. Inversely, substantive drivers can create a regulatory regionalism where regional members are grouped according to their perspective on the role of science in domestic food safety regulations, which may be in conflict with the multilateral agreement.

Table 3.2 provides a catalogue of RFSAs and RTAs. With respect to the analysis in the previous section, these regional arrangements are

Table 3.2 RTAs (bilateral and plurilateral) and SPS measures

	SPS measures	SPS-plus	Rule-making (RAF-type)	Notes/other
<i>Regional food safety authorities (RFSAs)</i>				
NAFTA	Yes (ch. 7)	No	Scientific rationality	Free trade agreement (FTA)
FTAA (<i>proposed</i>)	Yes	Yes – administrative	Scientific rationality	Regulatory competition FTA
EU	Yes	Yes – cultural	Social rationality	Regulatory competition Customs/monetary union
• EFSA				Regulatory coordination
CER	Yes	Yes – administrative	Scientific rationality	Preferential arrangement
• ANZFA				Regulatory coordination
<i>Regional trade agreements (RTAs)</i>				
EC-Iceland (1972)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Norway (1973)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Algeria (1976)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Syria (1977)	Yes	Yes (EFSA approach)	Social rationality	Customs union
EC-Andorra (1991)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Romania (1994)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Bulgaria (1994)	Yes	Yes (EFSA approach)	Social rationality	Customs union
EC-Turkey (1995)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Faroe Islands (1997)	Yes	Yes (EFSA approach)	Social rationality	Customs union
EC-Palestinian Authority (1997)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Tunisia (1999)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-South Africa (2000)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Morocco (2000)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Israel (2001)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Mexico (2000)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-FYROM (2001)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Croatia (2002)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Jordan (2002)	Yes	Yes (EFSA approach)	Social rationality	FTA

EC-Chile (2004)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Lebanon (2003)	Yes	Yes (EFSA approach)	Social rationality	FTA
EC-Egypt (2004)	Yes	Yes (EFSA approach)	Social rationality	FTA
Canada-Israel (1997)	Yes	No	Scientific rationality	FTA
Canada-Chile (1997)	Yes	No	Scientific rationality	FTA
Canada-Costa Rica (2003)	Yes	No	Scientific rationality	FTA
US-Israel (1985)	Yes	No	Scientific rationality	FTA
US-Jordan (2002)	Yes	No	Scientific rationality	FTA
US-Singapore (2003)	Yes	No	Scientific rationality	FTA
US-Chile (2003)	Yes	No	Scientific rationality	FTA

assessed according to whether they include mention of SPS measures, whether the measures are SPS-plus with respect to procedural or substantive drivers and whether scientific rationality or social rationality dominates. Table 3.2 shows two dominant regional blocs with respect to SPS rules and rule-making – North America (Canada and the United States) and the European Union. The former could be said to be procedurally SPS-plus and based on regulatory competition (i.e. national treatment), while the latter could be said to be substantively SPS-plus and based on regulatory coordination. Somewhere in between is the regional arrangement between Australia and New Zealand, which is characterized as being procedurally SPS-plus provisions but using regulatory coordination. Below is an assessment of the procedural and substantive SPS-plus regional drivers and their subsequent *impacts* upon the multilateral system.

Procedural SPS-plus

The negotiations for the proposed Free Trade Area of the Americas (FTAA) provide an excellent example of procedural SPS-plus measures. Many Central and South American agricultural exporters, led by Brazil, hold the view that the WTO's SPS Agreement does not deal with the pressing market access problems they have as a result of the administration of SPS measures in developed importing countries. According to the SPS Agreement (art. 4:1), importers are allowed to determine the equivalency of the exporting countries' SPS measures – via conformance assessments – before permitting market access. To do this, an importing country most often inspects and accredits the exporting country's food safety systems (both private and public). The procedural problem is that officials from the importing countries do not inspect and accredit very quickly, due to both real resource constraints and a disingenuous lack of interest in increased competition for domestic producers. As a result, it takes many developing countries considerable time and effort to obtain a developed country's accreditation. Either way, developing countries view this as a procedural barrier to trade. This is not only a North-South issue, but has also been at the heart of criticisms of Japanese market access rules by developed agricultural exporters such as Australia and Canada.

Because the SPS Agreement is silent on the procedural obligations and time-frames that developed countries must follow in accrediting foreign products and producers, calls have been made for SPS-plus measures that provide additional disciplines on the procedural rights and obligations of designated bodies in potential foreign markets, especially among developed countries. For example, in the FTAA context Brazil has de-

mandated that an FTAA SPS agreement be negotiated which specifies accreditation procedures and time-frames and affords easier accreditation to countries that have achieved a pest-free or disease-free status from the recognized international scientific organizations.

Unnevehr and Roberts (2003) list proposals by both developing and developed countries for food safety and quality regulation in agricultural negotiations. The proposals by developing countries – consistent with the argument above – deal entirely with proposals that can be defined as procedural SPS-plus.

The regional procedural SPS-plus measures appear to be consistent with eventual multilateralization because the additional disciplines can be seen as complementary to the existing SPS rules and, once operational at the regional level, can be applied multilaterally. The longer-term objective of this approach is to facilitate convergence of the multilateral WTO SPS Agreement with the regional SPS-plus approach by showcasing how the additional disciplines lead to greater international trade certainty and predictability.

Substantive SPS-plus: Drivers and impacts

In contrast to the procedural SPS-plus regional measures, the substantive SPS-plus measures reject the science-based and rules-based nature of the SPS Agreement in favour of more contextualized regional agreements in which safety goes beyond scientific rationality to include social rationality, as discussed in the previous section. Indeed, a frequent comment from some of the experts consulted is that the SPS Agreement was an experiment that has clearly illustrated the limits of multilateral rule-making in the trade rules/domestic regulation interface. That is, SPS measures are too intertwined with domestic political economy factors to be governed solely by top-down rule-making according to a science-based framework that allegedly discounts socio-economic and cultural factors.

As mentioned previously, two transatlantic trade examples are highly illustrative of this. First, the EU regulations prohibiting the use of growth-promoting hormones in beef production were a market access barrier preventing Canadian and US beef exports to the European Union (under Canadian and US regulations the use of growth-promoting hormones was approved as safe). Canada and the United States both challenged the EU regulations as a violation of SPS Agreement obligations, and the WTO agreed. However, the European Union has effectively ignored the ruling and the market access barriers remain in order to achieve socially rational regulatory outcomes. That is, when domestic regulations and international trade rules overlap, it is at the cost of the multilateral trading system. Second, in August 2003, at the request of

Canada and the United States, a WTO dispute settlement panel was established to rule on the SPS market access barriers that have prevented Canadian and US exports of genetically modified crops from entering the European Union (Isaac and Kerr, 2004; Anderson and Jackson, 2003; Bernauer and Meins, 2001). In both cases, the European Union has argued that the science-based and rules-based approach advocated under the SPS Agreement does not have enough scope for precautionary market access rules focused on domestic multifunctionality concerns and the consumers' right to know. The European Union has been very active in advocating SPS-plus measures applying within the union that define safety in broader terms than just science and support a socially rational interpretation of the precautionary principle.

Another recent example of culturally based market access barriers affected Canadian and US beef producers. Canada, which discovered a single case of BSE in May 2003, and the United States, which discovered a single case of BSE in December 2003, both faced immediate precautionary SPS market access bans on their beef exports, which according to the SPS Agreement (art. 5:7) were supposed to persist until the two countries had taken all reasonable steps to identify, isolate and eradicate the risks to consumers in importing countries. The ambiguity here arises because of an absence of a harmonized blueprint for the opening of markets after temporary precautionary bans have been invoked. Greater clarification on how long is "temporary" and on the quantity and type of scientific evidence that is sufficient is required in the SPS Agreement, and indeed Canada and the United States have begun the process of incorporating such disciplines into the guidelines of the OIE. But other countries, such as those in South-East Asia, have been calling for greater discretion in setting their SPS measures according to domestic political economy characteristics, with the result that APEC has produced a draft guideline to specifying substantive SPS-plus measures.

Proposals from developed countries with a socially rational interpretation of the RAF, identified in the Unnevehr and Roberts (2003) study, deal almost entirely with proposals that can be defined as substantive SPS-plus proposals. For example, the EU proposals include clarification of the precautionary principle; improved protection of animal welfare; and labelling rules that enshrine the consumers' right to know. Substantive Japanese proposals include specific rules on GMOs and consumers'-right-to-know labelling. South Korean proposals include improved rules beyond food safety and incorporating environmental protection rules, along with improved rules based on the consumers' right to know. Substantive Swiss proposals include improved rules on consumers' interests, such as broadened scope for the precautionary principle and greater measures to promote animal welfare. Each of these countries may be de-

defined as employing the socially rational approach to the RAF. As a result, the proposals all indicate dissatisfaction with the narrow scientific focus of the WTO SPS Agreement. On the other hand, substantive proposals from the United States – which holds a scientifically rational interpretation of the RAF – confirms the classic trade objective of ensuring transparent, predictable and timely rule-making.

The substantive SPS-plus measures appear to be consistent with the entrenched regionalization illustrated in figure 3.1. The additional measures may be viewed as conflictive to the SPS Agreement because they seek to alter its science-based and rules-based nature in favour of broader non-science concerns and a framework based on the precautionary principle. In this case, the RTAs represent a clustering of like-minded countries into a regional bloc that diverts trade not just temporarily but in a permanent fashion, as illustrated in figure 3.1. This diversion becomes entrenched due to particular institutional, legal and regulatory path dependencies. Such RTAs facilitate a structural divergence from the market access rules specified by the multilateral trading system.

Conclusions and implications

This analysis of SPS measures confirms the underlying assumptions of this study. First, the distinction between market access and rule-making is largely artificial and to gain a thorough understanding of the situation they must be dealt with simultaneously. SPS measures are inextricably linked to domestic political economy factors, such as a domestic history with food safety. These factors determine the norms (including the role of science in society), which in turn determine the SPS rule-making. Market access is then determined according to the congruency of products with this domestic structure of norms and rules. Transatlantic trade disputes over both hormone-treated beef and genetically modified organisms illustrate this. This case study of SPS measures also reveals that regional rule-making models differ, with a socially rational model in Europe and a scientifically rational model in North America that is consistent with the WTO's approach.

Second, while rule-making may be dominated by a particular level, there has always been a complex interplay between the levels. An agreed framework for SPS measures first emerged in Europe, and was then multilateralized but remained in the control of a community of experts, in the shape of the relevant scientific organizations, until these organizations were linked into the WTO, thus codifying the scientifically rational rule-making approach. Dissatisfaction with the link has produced two types of regional responses: those calling for procedural improvements and those

calling for substantive improvements. Looking ahead, it is not clear which level of rule-making will dominate. Indeed, this case study illustrates that the regional level of rule-making does not always defer to the multilateral level.

Third, it is the nature of the interaction between the levels of rule-making that is most informative. In the case of SPS measures, one could argue that the WTO's SPS Agreement has been an experiment which has exposed the differences in regulatory models that currently exist among member states. The nature of the interaction is determined by strategic behaviour on the part of actors (i.e. governments and the European Union), who have one of two broad approaches to change for the WTO SPS Agreement: procedural or substantive approaches. The former approach leads to demands for procedural SPS-plus measures clarifying the administrative rights and obligations of countries at the regional level before the multilateralization of a science-based and rules-based SPS system can be fully established by the WTO. The longer-term effect of such efforts is likely to be a convergence between regional and multilateral SPS rules in a way that maximizes the certainty and predictability of international trade. The latter approach leads to demands for substantive SPS-plus measures broadening the determination of safety beyond just a science-based notion in a way that is domestically contextualized and, perhaps more importantly, gives an approach built on the precautionary principle. The longer-term effect of such efforts is to protect regional rule-making norms from multilateral rule-making; hence an entrenched regionalism and not a convergence may be the outcome. Like-minded countries cluster together to support a particular regulatory norm and may actively engage in the promotion of that norm to third parties in order to build a broader coalition for the rule-making approach. This could well be the process by which US-centred or EU-centred RTAs are used to promote their respective approaches to SPS rule-making. Interestingly, retaliation does not seem to impact on the resolve of these regional blocs, as the failure of US and Canadian trade sanctions to remove the EU ban on hormone-treated beef illustrates. In fact, retaliation may stiffen the resolve of countries to resist multilateralization (Isaac and Kerr, 2004).

According to the framework laid out in the introductory chapter, the nature of the interaction between multilateral and regional rule-making can be categorized as strategic use of linkage to create a regional bloc that then exports domestic norms. This would suggest that the interaction has an illiberal and perhaps malign impact upon the multilateralization of SPS measures.

A final assumption of this study is that the multilateral system must continue to play a major role in areas of complex deep integration even

as other levels of rule-making evolve. Given the analysis above, this role is a difficult one. The WTO's SPS Committee, along with the three scientific organizations that support the agreement, should give careful consideration to the disaffections which have resulted in an increased regionalization of SPS measures. It can be expected that when WTO members are dissatisfied with particular multilateral rules, they will seek quicker remedy through regional associations rather than through multilateral negotiations. As a consequence, multilateral rule-making will have to focus more centrally on interregional negotiations to achieve multilateral disciplines rather than solely negotiations among individual WTO members. Such interregional negotiations will not be easy because the regionalism is driven by fundamental differences in norms associated with the interpretation and implementation of the RAF. Governments have few degrees of freedom to compromise food safety and health regulations in order to liberalize trade. Similarly, regulatory competition – which necessarily creates regulatory winners and losers – would not be welcome. Therefore, the multilateral system is left with the task of carrying out the experiment of deeper integration involving the convergence of norms; a time-consuming endeavour.

In the meantime, commercial interests seeking market access must position their food products to meet the specific market access rules that have emerged in various relevant markets. That is, the GATT notion of “approved once, approved everywhere” cannot be assumed to hold. Instead, products that are easily approved and accepted in one jurisdiction may face significant regulatory approval delays and/or consumer acceptance issues in another jurisdiction.

Notes

1. This means that it is not possible to differentiate between products according to how they have been produced.
2. For example, the “like-products” concept implies that a cotton shirt produced in an organic agricultural system is like a cotton shirt produced in an intensive agricultural system; market access rules are not permitted to distinguish between the two types of cotton shirts.
3. For instance, article XI specifically permitted regulations setting out national “standards or regulations for the classification, grading or marketing of commodities in international trade”. Article XX(b) permitted the adoption or enforcement of measures necessary to protect human, animal or plant life or health.
4. These interests ranged from food-exporting countries and multinational food processing and distributing companies which shared a common concern about market access barriers facing food trade to consumer organizations which wanted to ensure that as food products were increasingly traded some minimum standards of safety prevailed (Isaac, 2002).

5. Unsafe imports can jeopardize human safety and health either directly by making imported foodstuffs unsafe or indirectly by infecting domestic food inputs, including livestock and agricultural plants that are part of the domestic food chain. There is a crucial distinction to note. The SPS Agreement targets measures taken to protect the domestic food supply, not measures taken to target overall domestic biodiversity. In this sense, the SPS Agreement relates to food safety measures only, not environmental protection measures, although in practice this distinction is blurred.
6. The SPS Agreement's annex A reads: "no member should be prevented from adopting or enforcing measures necessary to protect human, animal or plant life or health arising from: the entry, establishment or spread of pests, diseases, disease-carrying organisms or disease-causing organisms; additives, contaminants, toxins or disease-causing organisms in food, beverages or feedstuffs; and diseases carried by animals, plants or products thereof". Agreement on the Application of Sanitary and Phyto-Sanitary Measures, Uruguay Round of Multilateral Trade Negotiations Legal Texts (the SPS Agreement), Preamble, pp. 69–84.
7. The meaning of a "legitimate justification" will be discussed below.
8. The agreement states: "In cases where the relevant scientific evidence is insufficient, a Member may provisionally adopt sanitary or phytosanitary measures on the basis of available pertinent information, including that from sanitary or phytosanitary measures applied by other Members. In such circumstances, Members shall seek to obtain additional information necessary for a more objective assessment of risk and review the sanitary or phytosanitary measure accordingly within a reasonable amount of time." (SPS Agreement, art. 5:7.)
9. The agreement states that "in the assessment of risks, Members shall take into account available scientific evidence; relevant processes and production methods; relevant inspection, sampling and testing methods; prevalence of specific diseases or pests; existence of pest- or disease-free areas; relevant ecological and environmental conditions and quarantine and other treatment" (SPS Agreement, art. 5:2).
10. The agreement states that "when a Member has reason to believe that a specific sanitary or phytosanitary measure introduced or maintained by another Member is constraining, or has the potential to constrain, its exports and the measure is not based on the relevant international standards, guidelines or recommendations, or such standards, guidelines or recommendations do not exist, an explanation of the reasons for such sanitary or phytosanitary measure may be requested and shall be provided by the Member maintaining the measure" (SPS Agreement, art. 5:8).
11. For a comprehensive assessment of the RAF and the many debates associated with its appropriate use see Isaac (2002).
12. Regulations based on the RAF can be found in many countries, such as Canada, the United States, the European Union (as well as its member states), Australia and Japan. The RAF is also supported by international organizations such as the Organization for Economic Cooperation and Development (OECD), the WTO and several UN agencies, including the World Health Organization (WHO), the Food and Agriculture Organization (FAO) and the CAC.
13. The normative and theoretical roots of scientific rationality – from a regulatory perspective – may be found in neo-classical economics. For a discussion on the role of technology in society according to neo-classical economics see Grossman and Helpman (1991). For a general discussion on the "scientific rationality" of neo-classical economics see Blackhouse (1994).
14. The normative and theoretical roots of social rationality – again, from a regulatory perspective – may be found in risk society theories; for a discussion see Beck (1992) and Giddens (1994). For a general discussion of "constructivism" see Wendt (1999).

15. In September 2003 the USDA announced the Canadian producers could export boneless meat from animals younger than 30 months to the United States; however, trade in live cattle and boned meat cuts was not reinstated.
16. For a comparative assessment of the regulatory competition and regulatory coordination approaches to international economic integration see Isaac (2002) and Woolcock (1996, 1998).

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Preferential rules of origin: Models and levels of rule-making

Luis Jorge Garay and Philippe De Lombaerde

Introduction

It has been argued that the proliferation of overlapping or partially overlapping preferential/regional trade agreements (RTAs) since the 1990s has created a veritable “spaghetti bowl” of divergent, opaque and restrictive rules of origin (RoO) (Schiff and Winters, 2003; OECD, 2003). Recent preferential RoO are also more complex than in the past, which has resulted in higher transaction costs (OECD, 2003) and low utilization of preferences (European Commission, 2003) that should be promoting trade expansion (World Bank, 2005: 27, 57). Preferential RoO are seen as neo-protectionist instruments serving the protectionist interests of specific sectors in the regional hegemonic economic powers (Krishna, 2004; Vermulst, 1992; LaNasa, 1996; Schiff and Winters, 2003; Moïsé, 2003b). The costs of divergent preferential RoO are also seen as particularly at odds with the widespread practice of using inputs made in different countries in the multistage production processes of large and medium-sized enterprises (Pawlak, 1995; World Bank, 2005: 46).¹ For these reasons, the harmonization of RoO is seen as one of the most important challenges facing the WTO’s work on trade facilitation (Moïsé, 2003a, 2003b), although even harmonized rules would still result in costs for trade given the increased internationalization of production.

This chapter first analyses the role of the two dominant rule-makers (the European Union and the United States) and identifies the characteristics and elements of convergence and/or divergence of the two domi-

nant regulatory models concerning RoO. The subsequent sections elucidate the influence of these two models on third countries and regions, concentrating on RoO provisions in recent RTAs. Finally, the chapter discusses the interaction between the regional and multilateral levels of rule-making, at which only slow progress has been registered with respect to the harmonization of non-preferential rules.

Typology of rules of origin

Whilst all based on the substantial transformation principle, RTAs use different approaches to confer preferential origin to imported goods and usually combine different criteria even at the product level. Under the aegis of the World Customs Organization, the Technical Committee on Rules of Origin has produced a helpful typology of the various criteria used (table B.4.1). The essential rules apply to product categories, which are defined on different levels of aggregation of the Harmonized System. In addition, a number of general (regime-wide) criteria are considered.

For goods that are wholly obtained or produced (from locally available raw materials or locally produced components) in the exporting country, the determination of the origin is straightforward. More difficult is the determination of the origin of goods with a production process covering two or more countries. In that case, origin is conferred on the basis of a minimum amount of working or processing in the exporting country (substantial transformation).

The problem comes in determining what constitutes substantial transformation. There are three basic criteria used for this: a change in tariff classification (CT), a minimum content of national or regional value added ((R)VC) and technical requirements (TRs) (see table 4.1). A change in tariff classification means a change in the tariff heading (CTH) as a result of the manufacturing process compared to the foreign input and materials used in their production. For example, a CTH at the level of the first four digits of the Harmonized System of Tariff Nomenclature² (HS) constitutes the basis for the system of preferential RoO in cases like the European Community and ALADI. Besides the “positive” CT criterion, a “negative” criterion can be formulated in which a CT does not confer origin. This negative criterion is usually formulated as an exception to a positive CT rule (ECT) and is usually more restrictive. Indeed, some of these negative CTs can in practice be considered as functional alternatives to the exclusion of sensitive goods from preferential trade liberalization.

The CT can also be used sequentially, as in the case of textiles in NAFTA. In this case the inputs used to produce a final good should also

Table 4.1 Typology of RoO (Kyoto Convention)

Coverage	Primary criterion	Secondary criterion	Tertiary criterion
Product-specific	Wholly obtained/ produced Substantial transformation	Change in tariff classification (CT) Exception attached to particular CT (ECT) Value content (VC) Technical requirement (TR)	Chapter (HS 2) (CTC) Heading (HS 4) (CTH) Subheading (HS 6) (CTS) Item (HS 8–10) (CTI) Domestic/regional value content (RVC) (min. %) Import content (MC) (max. %) Value of parts (max. %)
Regime-wide	<i>De minimis</i> rule (max. %) Roll-up/absorption principle Cumulation	Bilateral Diagonal Full	

Source: *Consolidated Text*, Technical Committee on Rules of Origin, Brussels: World Customs Organization.

fulfil a CT criterion. This obviously raises the level of restrictiveness of the rules and the potential for trade diversion. As Moisé (2003b) noted, sequential CTs closely resemble a TR.

Among the principal problems encountered with a CT is the absence of sufficient tariff elements to determine specific CTs that guarantee an equivalent “substantial transformation” in the production of each and every item in the tariff universe. This is basically due to the fact that the HS was not designed to provide the sole criteria conferring RoO of merchandise.

The value added of value content (VC) criterion sets out the maximum percentage of foreign content (inputs and raw materials) from third coun-

tries outside the RTA permissible for the manufactured product to be considered as originating in the RTA. Alternatively, the VC may set out the minimum percentage of RVC required for a good to be granted its originating character. The application of this criterion is also not without its problems. Being based on value added it tends to penalize the use of more efficient cost-reduction techniques. It is highly sensitive to changes in determining factors of the cost of production between countries, such as, for example, relative exchange rates, wages and labour costs. It is costly to administer because it necessitates strict and thus expensive accounting, operational and financial procedures, both at the national customs level and at the level of the producers themselves. It reproduces inequalities in the distribution of benefits between countries, not only by favouring countries with more vertically integrated and generally more complex production facilities, but also by penalizing those countries with low wages and salaries. Finally, there is the problem associated with the reliable classification of intermediate materials and inputs used in production, and with the precise accounting of their respective values in the regional content value of the final product, to avoid inappropriately considering all of the input as originating or non-originating. This phenomenon is known as “roll-up” or “roll-down”.

The technical requirement (TR) criterion refers to the requirement to carry out certain technical operations or use certain inputs or raw materials in production as a condition for conferring regional origin. Apart from the difficulties maintaining access to an updated inventory of production techniques at any given time, this criterion grants extensive discretion to national implementing agencies because there is no objective classification of TRs that could guarantee the equivalence of product transformation for different products. As a result the TR criterion tends to have the highest compliance cost compared to the VC and CT (World Bank, 2005: 70).

RoO regimes also include some additional (regime-wide) clauses to facilitate administration and verification of origin. *De minimis* clauses specify that products shall not lose their status as originating products if the value of non-originating materials constitutes less than a given percentage of their transaction value. Roll-up clauses (or the absorption principle) allow an intermediate product that has acquired origin by satisfying processing requirements to be considered as fully original in the calculation of the value added in its subsequent transformation into another product even when the intermediate product incorporates some imported materials from third countries. RoO regimes also include duty drawback provisions that prohibit the refunding of tariffs on non-originating inputs included in a processed good which is then exported to another member country's market. As noted above, there may also

be lists of processes or operations that are considered insufficient to confer origin (such as packaging), and provisions on certification procedures for RoO.

Finally, there is the important question of cumulation that allows a producer located in the customs territory of a signatory to an RTA to use non-originating materials from another signatory without this affecting origin. For example, consider a set of countries (A, B, C ...) that have signed an FTA. A bilateral cumulation clause permits use of inputs originating in country A in production of a good in country B and the export of that good back to A with origin calculated as if all these inputs originated in B. Diagonal cumulation permits the use of inputs originating in other signatories to the RTA (A, C, D ...) in the production of a good in country B with origin calculated as if all these inputs originated in the exporting country B. Full cumulation also permits processed inputs imported from A, C, E ... that are non-originating in these countries to be considered as originating in B (for exportation to A).

The pan-European model

The first building block of the global regulatory architecture for RoO is the so-called pan-European model. This model emerged in the 1990s as an effort to harmonize the RoO embedded in different RTAs negotiated by the European Union since the 1970s,³ such as the origin protocols with EFTA from 1972 to 1973, the EEA agreement and the Europe Agreements with the associated Central and East European countries (CEECs) from the beginning of the 1990s.⁴ The impetus for the pan-European model came from the aim, expressed at the Copenhagen European Council (21–22 June 1993), of improving trade opportunities for CEECs. This decision of EU heads of state and government was followed by European Commission proposals in 1994 for a harmonization of EU preferential RoO to reduce the underutilization of trade preferences and maximize the gains from trade within the wider European region. The Commission proposed a three-step harmonization programme: a harmonization of RoO among the Visegrád countries (with Bulgaria and Romania to be added later); implementation of diagonal cumulation⁵ between the European Union, EFTA and the CEECs; and full cumulation.⁶ These proposals were adopted at the Essen European Council in December 1994, but application of the third stage was conditional upon an evaluation of its expected consequences for EU industries. In 1997 harmonized protocols replaced the existing RoO covering an area comprising the European Union, the EEA, Switzerland and the associated CEECs.

For each heading of the HS, the protocols define what should be con-

sidered as sufficient working or processing for non-originating materials to qualify as originating goods. Although the previous protocols explicitly privileged the CTH criterion at the four-digit level (although with many exceptions), the new harmonized protocols do not provide a general rule. The criterion is established for each tariff heading. In many cases (about 25 per cent of HS tariff headings) two criteria are proposed, of which at least one should be fulfilled (i.e. alternation or the ability to choose different criteria). The first criterion can be CT (e.g. when processing results in a CT; CTH for more than 60 per cent of HS tariff items), import content (MC) or a technical criterion, such as a requirement that a specific process is carried out in order to impart origin.⁷ If there is a second criterion, it is MC. The pan-European RoO include a so-called “soft rule of origin” provision that allows the use of inputs at the same heading when the RoO require a CT at a heading level or a chapter level (CTC), reducing the degree of stringency of the requirement.

In the EU regime there are also provisions on *de minimis* operations: a (conditional) *de minimis* rule of 10 per cent (e.g. non-originating materials up to 10 per cent of the ex-works price do not alter the origin of the good), but with some exceptions like textiles and apparel products. There are also roll-up rules, and restrictive provisions on outward processing and bilateral and diagonal cumulation.⁸ Full cumulation was initially limited to the EEA. Duty drawback is precluded for at least two years after signing the FTA. The EU’s method of certification of origin provides two alternative procedures: a two-step procedure in which RoO are certified by the government’s agency once a certificate has been issued by the exporter or a competent agency, or an invoice declaration provided by exporters which have been approved as frequent exporters by the customs authorities.

The Euro-Med Trade Ministerial Meeting of July 2003 endorsed the “pan-Euro-Mediterranean protocol on rules of origin”, by which the system of diagonal cumulation will be extended to all Mediterranean partner countries: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Syria, Tunisia and the West Bank and Gaza Strip (and the Faroe Islands).⁹ This southward expansion of the pan-European regime, which would include a generalization of diagonal cumulation to all participating countries, requires FTAs with identical RoO to be in place between the European Union and its Mediterranean partners before diagonal cumulation can function. It also requires these partners to conclude agreements among themselves, as well as the harmonization of all administrative procedures and the withdrawal of drawback provisions (Gasiorek, Augier and Lai-Tong, 2003: 10–11). This extension of the pan-European zone was initiated with the negotiations of FTAs with Morocco, Tunisia and Algeria, all containing full cumulation provisions.¹⁰

Factors shaping EU RoO

Before the efforts to harmonize EU RoO, different divergent rules implied an important cost for the companies involved in international trade with the European Union. This was especially the case for RoO in the Europe Agreements, which were regarded as being too restrictive (Driessen and Graafsma, 1999: 20–21). The CEECs were mostly small countries and therefore depended heavily on imported inputs, so that the rules were often difficult to meet and the possibilities for cumulation were limited (to within the Visegrád or Baltic groups of countries). The direct costs of administering the origin certification in the EC-EFTA FTA were found to be considerable. According to Koskinen (1983) these costs amounted to 1.4–5.7 per cent of (the value of) exports; according to Herin (1986) they were 3–5 per cent of FOB export value.

The move towards harmonization clearly has a positive effect in terms of transparency and the possibilities to cumulate. Indeed, one of the outstanding features of the EU model is its high level of standardization and harmonization across the multiple FTAs signed since 1997, and the remarkable similarity and continuity since the first protocol published in 1973.

On the other hand, as Estevadeordal and Suominen (2004) have shown, the degree of restrictiveness of the EU RoO appears to be quite closely correlated with the pace of tariff reduction: the faster the tariff liberalization schedule, *ceteris paribus*, the less restrictive the RoO. In other words, the more restrictive rules are applied for products that previously benefited from higher levels of tariffs. Furthermore, the European Union tends to eliminate tariffs faster for tariff lines in which the EU's partner country is less competitive and/or its distance and transport costs for shipping to the European Union are higher. This is the case for Chile, which obtained the fastest phase-out of tariffs among the latest extra-European FTAs (South Africa, Mexico and Chile).

Driessen and Graafsma (1999: 37–39) evaluate the EU RoO system generally as complex, although they recognize that significant progress has been made in terms of internal logic and sourcing opportunities compared to the pre-existing protocols. According to them, considerable trade deflection was likely in different production sectors given the RoO criteria and the drawback prohibitions in trade with the CEECs.

There have been a number of studies of the economic effects of extending the pan-European model to the EU's Mediterranean partners. According to Hoeller, Girouard and Colechia (1998), the relatively high “local” content requirements in the Euro-Med agreements (often 60 per cent) restrict the (in principle duty-free) access to the European market for manufacturers.

Restrictive RoO have been linked to the underutilization of EU preferences, which has worked contrary to the development aims of some of the EU's preference schemes (World Bank, 2005: 52). According to the European Union only about 50–55 per cent of EU imports from countries with which the European Union has a preference agreement actually benefit from the preference (European Commission, 2003). Candau, Fontagne and Jean (2004) found that, in general, underutilization of EU preferences did not constitute an important degree of protection encountered by non-EU exporters. They did find, however, that the utilization is generally correlated with the tariff margins, suggesting that compliance costs are significant. They also found exceptionally low utilization rates for textiles and clothing under the EU's General System of Preferences (GSP) and Everything But Arms (EBA) schemes, and identify the restrictive RoO as main causes for this. Brenton and Ikezuki (2004) also confirmed that the low preference utilization rates by the EU's commercial partners in textiles can be linked to the restrictiveness of the RoO.

Using gravity models, Gasiorek, Augier and lai-Tong (2003) estimated that the absence of diagonal cumulation reduces bilateral trade volumes by 40–45 per cent.¹¹ A CGE analysis showed that RoO cumulation in the European Union can be expected to lead to positive effects on intra-regional trade, output levels (+2–3 per cent) and welfare (+0.5 per cent). Estevadeordal and Suominen (2004) also demonstrated that cumulation has a significant impact on intraregional trade.

In a 2003 green paper, the European Commission launched a major review of EU preferential RoO in the light of the tariffs likely to emerge from the Doha Round of multilateral trade negotiations, the role of preferential RoO in RTAs and the policy of market access and supporting sustainable development. The review was also to extend to “management procedures and supervisory and safeguard mechanisms to ensure that preferential arrangements are used properly and shield the business community and the financial interests at stake from abuses of the system” (European Commission, 2003: 4). The review involved a survey of interested parties, mainly businesses (approximately 70 per cent of respondents) and authorities (the European Union, third countries and regions; approximately 30 per cent of respondents), which showed a widespread support for the view that present RoO do not fit current economic reality for the following reasons. First, the RoO do not correspond to the global production processes and technologies, but reflect past defensive policy aims. Second, the EU preferential RoO were seen to be still too complex, restrictive, opaque and in need of rationalization and simplification. There was, however, a recognition that there needed to be an assurance that the products for which preferential treatment is claimed do actually satisfy the origin rules (European Commission, 2004: 4).

At this point it is still too early to foresee a major change in the existing regime. It is likely that further initiatives will be needed to make the rules more transparent and improve their administrative and technical aspects. It is not clear, however, whether declared aims like “supporting development” and “taking into consideration actual market, trade, industry and agriculture conditions” will always be compatible. The consultation process sheds some light on the political economy of European RoO, in that the distribution of respondents, showing a preponderance of industry views, probably reflects relatively well the political weights of the different interest groups influencing the European decision-making process on RoO. It is not surprising then that, according to the majority of the respondents, European preferential rules reflect the objectives of European industrial policy (rather than trade or development policies) (European Commission, 2004).¹²

The NAFTA model and origin regimes in the Americas

The regional model for RoO is the NAFTA model. In order to understand the importance and particularities of this model it is worth contrasting it with pre-existing and competing models on the American continent.

Regional integration agreements in the Americas include the Latin American Integration Association (ALADI), the Central American Common Market (CACM), the Andean Community (CAN), the Common Market of the South (MERCOSUR), the Caribbean Community (CARICOM) and NAFTA, as well as other “new-generation” FTAs signed in recent years. ALADI has served as a model for MERCOSUR, CAN and CARICOM. NAFTA has been used as a model for Mexico’s agreements with Bolivia, Costa Rica and Colombia and Venezuela (the so-called Group of Three or G3), Chile’s agreements with Canada and Mexico and US FTAs with Chile and Central America. The CACM stands at an intermediate point between the two. NAFTA-type FTAs (new-generation FTAs), such as the G3 agreement by Colombia, Mexico and Venezuela and Mexico’s bilateral treaties, tend to be more comprehensive than the ALADI type in that they cover issues such as services, investment and public procurement.

The new-generation FTAs also contain more specific and detailed origin regimes. Traditional integration schemes in Latin America have relied on rules that are less selective and more uniform than those found in NAFTA-type agreements, which employ a multiplicity of families of rules at the tariff-item level. What follows compares the principal features of the three regimes that have been used as reference frameworks for other agreements, namely ALADI, NAFTA and the CACM (Garay and Cornejo, 1999).

The principal differences among these regimes can be assessed by considering a number of core elements of the rules (table 4.2). With regard to *diversity* of criteria the CT is applied uniformly in the ALADI regime at the HS four-digit level, regardless of the type of merchandise. In contrast, under NAFTA and the new-generation regimes the required CTC varies between goods: a change in chapter, heading, subheading or even tariff item may be required. As far as the *multiplicity* of criteria is concerned, RoO regimes in MERCOSUR, the CACM, CAN and ALADI are basically defined in terms of the CTC or, alternatively, a given level of regional content; in some exceptional cases a combination of criteria is used for specific lists of goods. In contrast, NAFTA and the new-generation regimes are based on a multiplicity of criteria, which prevents any one criterion from being singled out as the guiding principle for determining origin. In part, this multiplicity reflects the high degree of detail and selectivity contained in new-generation FTAs.

Some schemes also use *alternation* or the choice of more than one rule to classify a good. In ALADI, MERCOSUR, the CACM and CAN alternation is uniform, with the additional feature that each rule is based exclusively on a single qualification criterion: for example, the first criterion is based on a CTH and the alternate one on a specific regional content value. In contrast, NAFTA and new-generation regimes frequently offer a variety of alternate rules for determining a good's origin, without each rule necessarily being based on a single qualification criterion. In practice, however, the levels of stringency within alternative rules that constitute a family differ as a result of the different requirements of the criteria used to determine origin.

ALADI, MERCOSUR and CAN require the use of the FOB or CIF transaction value of the merchandise to be used as a method of calculating its regional or national content. These values are well known, and they require neither the exporter nor the customs authorities to keep special records or employ additional controls. On the other hand, NAFTA and new-generation regimes tend to use the two alternate methods of net cost and transaction value. Estimating the value of regional content using the net cost method requires detailed records of – and information on – merchandise promotion and sales costs. The CACM regime stands midway between these two groups, in that it uses two methods to determine regional content: transaction value, defined in accordance with the WTO's Customs Valuation Code, and normal price, calculated from the FOB price of the exported goods and the CIF price of third-country components.

The new-generation agreements contain novel concepts aimed at, among other goals, increasing the flexibility of the tariff classification change criterion by introducing *de minimis* clauses, facilitating the regional integration of production processes by allowing the cumulation of

Table 4.2 Origin regimes in the Americas

Regime of origin	Criterion 1	Criterion 2	Other criteria 3	Specificity	Member countries treatment	Other clauses	Method of calculation	Administration
1. ALADI	CTH (4-digit level), <i>or</i>	RVC no less than 50% of FOB value	–	Uniform for the tariff universe, based on a single qualification criterion	No differential treatment	–	Based on an FOB or a CIF value of transaction	No rigorous administrative procedures
a. CAN	As ALADI, <i>or</i>	As ALADI	Specific requirements in exceptional cases	As ALADI, except for some exceptional cases	Preferential treatment for less developed countries (Bolivia and Ecuador)	–	As ALADI	Imposes detailed sanctions applicable to certification agencies
b. MERCOSUR	As ALADI, <i>or</i>	RVC no less than 60%	Specific requirements for a list of goods (like chemicals, iron, steel, data-processing and communication)	As ALADI, except for a list of goods	Preferential treatment to some products with origin in Paraguay	–	As ALADI	

2. NAFTA	CT in a more versatile fashion than the other regimes, from CTI up to CTC (8-, 6-, 4- or 2-digit level)	RVC 50% or 60%, <i>and/or</i>	TR in terms of specific process of production or inputs	Diverse, <i>not</i> uniform between goods, based on a multiplicity of criteria and a variety of alternative rules	No differential treatment	<i>De minimis</i> , accumulation and roll-up	Net cost or transaction value	Specifies verification, control and sanction procedures in detail and precision Introduces self-certification by exporting companies
3. CACM	As NAFTA, <i>or</i>	RVC for some specific goods, <i>or</i>	TR for exceptional goods	Diverse, not uniform, based basically on a change of tariff classification	No differential treatment for less developed countries	<i>De minimis</i>	Midway between ALADI and NAFTA: transaction value according to WTO's Custom Valuation Code, and normal price	Stipulates some rules and procedures to reinforce verification and control

regional components in calculating regional content values and streamlining the origin certification process by enabling exporting companies to issue their own certificates.

The new-generation agreements also specify enforcement provisions such as verification, control and sanction procedures with greater detail and precision. These are aspects that an origin regime must address, and were not dealt with adequately in some “first-generation” agreements. Although some of these stipulations or innovations can increase the cost of administrating the RoO for both public and private sectors, they do guarantee adequate rigour in the application of the regime.

Comparing origin regimes in the Americas

The recent proliferation of FTAs shows a tendency towards the adoption of an RoO regime that stand between the classic “first-generation” and the “new-generation” approaches. These developments in regional, preferential RoO in recent years may turn out to be decisive in the integrationist dynamics of the American hemisphere. It is possible to conceive of the various countries or groups as constituting RoO “poles” within the region. A “pole” is understood to be the set of FTAs that emulates the origin regime negotiated under a specified FTA in such a way that their contents are very similar in their regulatory aspect as well as in the specification of the RoO at the level of tariff subheading. In order to determine whether a pole exists it is necessary to assess the degree to which different RoO are similar. This is done by a “representativeness” for each pole and then for the poles themselves.

A rule of origin is representative when identical rules exist in regimes and/or when its resultant components show a high frequency of correspondence. RoO are therefore more “representative” the more the components of the rules correspond. The degree to which rules correspond is measured by classifying RoO in five categories according to the degree of similarity/dissimilarity: identical, highly similar, fairly similar, similar and scarcely similar.

This approach shows significant similarities among the new-generation regimes of origin. In the case of NAFTA, G3 and Mexico-Costa Rica FTAs there are significant similarities at both the aggregate and sectoral levels (e.g. two digits ISIC), with the exceptions of the chemical, petroleum and plastic manufacturing sectors (Garay and Estevadeordal, 1996). In addition, it should be noted that the degrees of stringency of the G3 and NAFTA RoO – taking the tariff subheading as the basic unit of analysis – are significantly correlated,¹³ both at the level of the economy and at the sectoral level (two digits of the ISIC classification, rev. 2). On the other hand the degree of average stringency of the RoO regime, at least a priori, of the G3 is lower than that of NAFTA (Garay and

Quintero, 1997). One gets the same results comparing the characteristics of the RoO in the FTAs recently signed by the United States with various Latin American countries, such as Chile, and some Central American countries, namely a high degree of correspondence of their RoO with NAFTA, but lower levels of stringency compared to NAFTA.

As a result, it can be argued that the NAFTA new-generation regime of RoO has tended to be replicated in other FTAs subsequently signed by the United States and Mexico during the last decade. At the same time there is a clear tendency to simplify the new-generation RoO by reducing the number of instances of alternative rules, stressing the CT as a predominant qualification criterion and reducing the degree of stringency, at least *ex ante*, in relation to the NAFTA original regime of origin.

Garay and Cornejo (2001a, 2001b) point to the same conclusion, by showing that the degree of “representativeness” of the MERCOSUR and Mexico poles is broadly similar, with only 3 per cent of the subheadings not assigned to a representative RoO of the corresponding pole regime, and 80 per cent of the subheadings are either identical (60 per cent for the Mexican pole and 72 per cent for MERCOSUR) or show a high degree of similarity with the pole regime. Following these authors, it is possible to argue that there are four main origin regimes currently in effect in the Americas – NAFTA, the CACM, MERCOSUR-pole FTAs and Mexico-pole FTAs.¹⁴

The US policy debate on RoO

There has been awareness of the possible trade-restricting effects of RoO in the United States for some time. In 1987 the US International Trade Commission (USITC) identified some of the principal problems with the criteria for determining origin, and recommended four basic principles to guide RoO: uniformity, simplicity, predictability and expeditious administration (USITC, 1987). The USITC report, however, also recommended a focus on the use of TR for conferring origin, which has the major drawback of requiring a detailed, up-to-date inventory of all available processes for the universe of manufactured goods.

From the beginning of the 1990s there were signs that RoO were beginning to be used as instruments of protection (Nogués and Quintanilla, 1992: 305), with NAFTA RoO being used to protect the clothing, automobile and colour television sectors (Schiff and Winters, 2003: 79). The costs of administering the origin certificates in NAFTA have been estimated at around 1.8 per cent of the value of exports and the trade-distortion effect of the RoO as equivalent to an average tariff of around 4.3 per cent (World Bank, 2005: 70; Ansom et al., 2004; Carrere and de

Melo, 2004). The NAFTA regime shows the highest levels of *ex ante* trade restrictiveness in the world. As in the European Union there is a correlation between the degree of a priori stringency of RoO and the tariff level applied to third parties (Garay and Quintero, 1997; Garay, 2002). For example, for nearly 80 per cent of the tariff universe the NAFTA RoO would seek to preserve, at least partially, the level of US protection against foreign competition by imposing more stringent RoO requirements on imports from Mexico for products on which the US tariff applied to third parties is higher. In addition there is an inverse relationship between the degree of stringency of the NAFTA RoO and the margin of preference that the United States concedes to Mexico, but specifically for those items for which the Mexican tariff level is higher than the US tariff level to third countries.

These findings of the protectionist use of the NAFTA origin regime support the view that rule-making in this field was subject to regulatory capture by various vested interest groups. On the basis of the NAFTA experience, Simpson (1997) has recommended that RoO for the Free Trade Area of the Americas (FTAA) should dispense with RCV because of its “Byzantine complexity”, use a simple CTH criterion that avoids changes beyond the six-digit level and create partial customs unions to reduce the use of RoO in the sectors covered while moving progressively towards a true CU.

Given US leadership in FTAs and the way the NAFTA model is being emulated in other agreements, the latter (albeit a less complex and stringent version) is likely to find a growing predominance across the American hemisphere. The conclusion of an FTAA and/or a US-MERCOSUR agreement is likely to strengthen this trend further. Meanwhile, the MERCOSUR countries, Chile and the Andean countries will probably continue with a rather different model.

Finally, a footnote on Africa. Some recent empirical work suggests these conclusions on the impact of US RoO in FTAs within the Western hemisphere also apply to Africa. With respect to the Africa Growth and Opportunities Act (AGOA), signed in 2000, Mattoo, Roy and Subramanian (2002) and Walmsley and Rivera (2004) found that the medium-term effects of US trade preferences would be much more significant without restrictive RoO. Clothing is a particularly problematic sector.

Comparing the pan-Euro and American regimes: A summary

In order to compare the EU approach and the new-generation and first-generation FTAs in the Americas, the new EU RoO regimes (FTAs with South Africa, Mexico and Chile), NAFTA, the Mexico pole and the

MERCOSUR pole can be selected as “representative”.¹⁵ In the case of the change of tariff criterion, the first component of the RoO, the EU regime is highly concentrated on the CTH at the four-digit level HS, which accounts for 60 per cent of the tariff universe compared to 45 per cent for NAFTA but 100 per cent for the first-generation regimes. A big difference can be found in the importance of the CTC, which accounts for only 14 per cent of cases in the EU regime compared to 42 per cent in the NAFTA/new-generation regimes but none in the first-generation regimes. But a distinctive feature of the EU regime is that it dispenses with the CT criterion for almost 25 per cent of the tariff subheadings of the HS; for more than 85 per cent of these cases it imposes a wholly obtained criterion or sets a ceiling of 40–50 per cent for non-originating materials.

The second element in the EU regime is the value-added or value-content criterion (VC), which applies for almost 25 per cent of the EU tariff universe. This contrasts with just 8 per cent in the NAFTA/new-generation regimes, but 34 per cent in the first-generation regimes in the Americas. In the European Union the VC criterion is basically applied to those cases subject to no CT or to a CTH under the EU rules. But in the cases of the NAFTA/new-generation rules VC is applied as an additional component to the CTH.

In the EU FTAs considered, nearly 21 per cent of the tariff universe is subject to a TR criterion, compared to 15 per cent in the NAFTA/new-generation regimes and 43 per cent in the first-generation regimes in the Americas. This criterion is used as an additional component to the CT at the chapter and heading levels under the EU and NAFTA/new-generation regimes but is applied at the CTH level under the first-generation regimes.

Estevadeordal and Suominen (2004) compare the EU and NAFTA-based RoO and find a

rich diversity of combinations of different RoO criteria across sectors particularly in the EU- and NAFTA-based RoO regimes [with] MERCOSUR [rules being] more uniform ... Even though NAFTA RoO diverge at the sectoral level from the EU model, the differences are seldom marked, but derive from the particular combination of RoO. Particularly notable are the prevalence of the exception to CTH and VC criteria in combinations with the CTH criteria. Both NAFTA and the EU RoO regimes rely heavily on TR in the textile sector, which can have important implications to production patterns ... However, NAFTA and EU models do diverge in ... that NAFTA uses the regional value content as the main VC RoO, whereas the EU mainly employs the import content criterion.

In terms of restrictiveness, the *ex ante* degree of restrictiveness of the NAFTA RoO regime is higher than that of the European Union (10 per

cent higher on average), except in 4 out of 20 sectors: live animals, vegetable products, electrical equipment and optics. The first-generation RoO regime shows the lowest *ex ante* degree of restrictiveness, both on average and at the sector level. Variability in restrictiveness suggests the use of RoO for protectionist purposes for specific sectors. In the European Union the degree of restrictiveness tends to be uniform in sections 13–21 of the HS, but under the NAFTA-type rules it varies significantly and tends to be relatively higher, except in the case of foodstuffs, in which the EU level of restrictiveness varies.

All systems of RoO also include roll-up clauses¹⁶ and allow cumulation (bilateral but not diagonal accumulation, except in the cases of the EU FTAs with South Africa and Poland). The *de minimis* rule, which allows a set percentage of non-originating content to be ignored, is 10–15 per cent in the EU FTAs and 7 per cent in NAFTA. Drawback is precluded after two years in the EU FTA with Mexico and after five years for Mexico under NAFTA. There are also important differences in the method of certification, with the NAFTA-type new-generation rules allowing self-certification and the pan-Euro and first-generation rules requiring certification by a public entity or a private entity approved as a certifying agency by the government.

Table 4.3 summarizes the degrees of restrictiveness of the different RoO families (clusters), using the methodology developed at the Inter-American Development Bank (IDB).

The Indian Ocean RoO regimes

The RoO regimes of the preferential trade areas in the rest of the world include ASEAN, ANZCERTA, SAFTA, ECOWAS, COMESA, the SADC and the Namibia-Zimbabwe FTA. These regimes are characterized by relatively simple rules, applied across the board. Usually a VC criterion is used, sometimes the CTH criterion. The MC varies from 30 per cent to 70 per cent; the VC rule from 25 per cent to 35 per cent (Estevadeordal and Suominen, 2003; table 4.3).

The SADC case is sometimes used to illustrate that these regimes might feel the influence of the development of the more complex (and restrictive) regimes of the European Union and the United States/NAFTA. SADC rules initially consisted of a CTH, RVC of minimum 35 per cent or an MC of maximum 60 per cent of total inputs.¹⁷ However, they were revised and now include more restrictive content requirements and TRs have also been added (Flatters, 2002). According to Schiff and Winters (2003: 8), the revision shows the influence of the rules embedded in the EU-South Africa agreement and the EU-ACP trade preferences.

Table 4.3 Restrictiveness and facilitation index numbers for different RoO regimes

	Restrictiveness index (RI)	Standard deviation (RI)	Facilitation index (FI)
<i>Pan-Euro cluster</i>			
Pan-Euro	4.81	1.37	2
EEA	4.81	1.37	3
<i>NAFTA cluster</i>			
NAFTA	5.15	1.16	3
US-Chile	4.37	1.61	3
Canada-Chile	4.61	1.43	3
G3	4.94	1.46	2
Mexico-Costa Rica	4.77	1.31	3
<i>MERCOSUR cluster</i>			
MERCOSUR	2.00	0.00	1
MERCOSUR-Chile	2.98	1.85	1
MERCOSUR-Bolivia	3.02	1.84	1
<i>CACM</i>			
CACM	2.00	0.00	3
<i>LAIA cluster</i>			
LAIA	4.00	0.00	1
CAN	2.00	0.00	1
CARICOM	2.00	0.00	1
<i>Indian Ocean regimes</i>			
AFTA	4.00	0.00	1
ANZCERTA	4.00	0.00	2
SADC	4.68	1.40	2
COMESA	2.00	0.00	1
ECOWAS	3.00	0.00	1
<i>Extra-regional EU-centred agreements</i>			
EU-Mexico	4.82	1.36	2
EU-South Africa	4.81	1.37	4
EFTA-Israel	4.81	1.37	2
<i>Extra-regional US/NAFTA-centred agreements</i>			
US-Israel	3.00	0.00	2
Canada-Israel	4.00	0.00	4
Mexico-Israel	4.00	0.00	3
Chile-Korea	4.69	1.08	3

Source: Estevadeordal and Suominen (2003: 35).

Methodological note: The restrictiveness index (RI) shows the *ex ante* restrictiveness of an RoO regime. The numbers in the table are unweighted averages of RIs calculated at the HS six-digit level. Ordinal values are attached to different RoO: 1 (CTI), 2 (CTS), 3 (CTS + VC), 4 (CTH), 5 (CTH + VC), 6 (CTC), and 7 (CTC + TR). This implies that: $1 \leq RI \leq 7$. See also Estevadeordal (2000) and Garay and Cornejo (2001a) for an alternative algorithm. The facilitation index (FI) evaluates the *ex ante* effect of the regime-wide rules. The minimum value of FI is zero (*de minimis* ≤ 5 per cent) and no other regime-wide rules apply. The values 1 to 4 reflect the application of 1, 2, 3 or 4 of the following additional rules: diagonal cumulation, full cumulation, drawback and self-certification (in any order). The value of 5 is reached with a *de minimis* ≥ 5 per cent and all other rules apply. Thus: $0 \leq FI \leq 5$.

Table 4.4 Frequency of various product-specific criteria

PTAs	Criterion				
	CT	Value content			TR
		MC	RVC	VP	
Customs unions (sample size = 6)	6	2 (40–60%)	2 (35–60%)	–	–
FTAs and other PTAs (sample size = 87)	83	68 (30–60%)	7 (25–65%)	67	74

Source: Estevadeordal and Suominen (2003: 5).

Note: CT = change of tariff classification; MC = import content; RVC = regional value content; VP = value of parts; TR = technical requirement.

Table 4.5 Frequency of general RoO provisions

PTAs	<i>De minimis</i>	Type of cumulation			
		Bilateral	Diagonal	Full	Roll-up
Customs unions (sample size = 6)	3	6	0	0	2
FTAs and other PTAs (sample size = 87)	85	87	58	8	81

Source: Estevadeordal and Suominen (2003: 6).

Mapping preferential RoO worldwide

The discussion above now enables us to take a global view and map the preferential RoO and criteria used worldwide. This global picture will then allow us to evaluate how far we are from a (more) homogeneous multilateral regulatory framework. From a cross-section of 93 RTAs (FTAs and CUs), CT appears to be the most widely used criterion (table 4.4), used in 89 cases (Estevadeordal and Suominen, 2003: 5). MC, value of parts and TRs are also very often used in FTAs. The table also shows that most of the RTAs use a combination of different RoO, which obviously does not contribute to transparency and consistency. Table 4.5 shows that *de minimis* rules, bilateral cumulation and roll-up clauses are also generally present in RTAs, with diagonal cumulation almost exclusive to the EU-based RTAs.

The dominance of a particular criterion or combination of criteria characterizing subsets of RTAs allows the identification of families (clusters) of agreements around a few poles or models. A purely empirical screening of the rules used in different RTAs reveals in effect the exis-

tence of two important clusters: one around the European Union (the pan-Euro model) and one around the United States/NAFTA (table 4.6). The CACM pole is relatively close to the latter. The RoO regimes in the rest of the world (mostly Asia and Africa), the Indian Ocean model, are usually more transparent and simpler. Here the VC criterion is applied across the board, sometimes complemented by a CTH criterion.

The dynamics of the global regulatory framework: The extra-regional expansion of the NAFTA and EU models

The EU and NAFTA models therefore appear to be the dynamic factors in origin rule-making. As noted above, the US/NAFTA model has expanded southwards on the American continent due to its application in US FTAs and the use of NAFTA-type rules in “new-generation” agreements between other countries. If the FTAA were to succeed the NAFTA model might become pre-eminent in trade between the American countries. US FTAs with countries in other continents like Australia and Singapore are also beginning to spread the NAFTA model. But contrary to the European Union, the United States has shown more flexibility regarding RoO, especially in the framework of extra-regional agreements. The US-Jordan and US-Israel FTAs, for example, rely basically on the VC rule (Moisé, 2003b). The agreement with Israel therefore shows levels of restrictiveness significantly below the NAFTA level and resembles more the Indian Ocean model in terms of restrictiveness. The US-Singapore and Chile-Korea FTAs show more complexity (table 4.3).

At the same time the EU origin regime is finding application in FTAs concluded between the European Union and countries such as Mexico, Chile and possibly MERCOSUR, as well as countries elsewhere that negotiate FTAs with the European Union (De Lombaerde, 2003). The European Union also exported its model indirectly via the EFTA-Mexico and EFTA-Singapore agreements (although the latter uses the slightly less restrictive VC criterion; table 4.3).

Further expansion of these two dominant models can be expected with the negotiation and conclusion of new agreements by the European Union (economic partnership agreements with the African, Caribbean and Pacific states, EU-MERCOSUR, Gulf Cooperation Council) and the United States (SACU and bilaterals with Thailand, Colombia, Peru, Ecuador, Panama, etc.). The level of restrictiveness of the RoO contained in these agreements has already been signalled as one of the important determinants of the development effectiveness of these agreements (World Bank, 2005: 32).

As a consequence, in order to harmonize the regimes of origin on a

Table 4.6 RoO regimes

Regimes	Selectivity	CTC	CTH	CTS	CTI	ECT	VC	TR	Application
Pan-Euro	SS		■				■ (MC 30–50%, ex-works)	■	Europe agreements, Euro-Med agreements, EU-Croatia SAA, EU-FYROM SAA, EU-South Africa FTA, EU-Mexico FTA, EU-Chile FTA, ACP, EU GSP, EFTA-Mexico, EFTA-Singapore CAN, CARICOM
LAIA	AB		■				■ (MC 50%)		
MERCOSUR	INT		■				■ (MC 40%; RVC 60%)	■	MERCOSUR-Bolivia, MERCOSUR-Chile
CACM	SS	■	■	■	■	■	□	□	
NAFTA	SS	■	■	■	■	■	■ (RVC 50–60%; 60 FOB, 50 cost prod.)	■	Mexico-Costa Rica, Mexico-Chile, Mexico-Bolivia, Mexico-Nicaragua, Mexico-Northern Triangle, Chile-Canada, G3, US-Singapore, (US-Chile), (FTAA)
Indian Ocean	AB		□				■ (MC 30–70%; RVC 25–35%)		ASEAN, ANZCERTA, SAFTA, SPARTECA, ECOWAS, COMESA, Namibia-Zimbabwe FTA

Source: Based on Esteveadeordal and Suominen (2003).

Note: SS = sectoral selectivity; AB = across the board; INT = intermediate; ■ = characteristic criterion; □ = less characteristic criterion.

multilateral basis it may be necessary to follow a two-track strategy: first to seek a convergence of the NAFTA-type (“new-generation”) and EU models, whilst secondly pursuing the aim of harmonized rules regarding common criteria, methodology and administrative procedures for preferential and non-preferential RoO.

Preferential rules and the multilateral trade system

There are different ways in which RoO in RTAs interact with the multilateral level and other levels of rule-making. The proliferation of new preferential rules contained in the various FTAs signed since the 1990s has not made trade rules more opaque and probably caused some trade diversion. RoO in “new-generation” agreements tend to vary among FTAs depending on the underlying “sensitivity” to intraregional competition and on member countries’ strategic goals. The proliferation of FTAs and GSP regimes has generated a problem of multiple RoO which entail costs of origin administration for both governments and companies and give rise to inefficiencies in resource allocation and specialization patterns. Any important initiative to make preferential rules more transparent or, taking it a step further, to come to a harmonized system of preferential rules will obviously have to be launched at the multilateral level. And the harmonization process of non-preferential rules will logically be the obligatory point of departure. While this process might contribute to the harmonization of preferential RoO, it is also the case that preferential rules in recent RTAs complicate the negotiations on non-preferential rules’ harmonization.

Although one might think that RoO will become of less importance given the general trend towards lower tariffs and the elimination of quotas, it should be recognized that RoO derive their importance not exclusively from their capacity to determine the applicability of these traditional trade barriers, but that they are also relevant for other issues on the current and future broader trade agenda, such as trademarks and origin marking (TRIPs), TRIMs, SPS, public procurement, exclusive economic zones, anti-dumping, etc.

Harmonization of non-preferential rules

GATT left it to each importing country to define the RoO to be used in the application of most-favoured nation (MFN) treatment and other non-preferential commercial policy instruments. This led to a multiplicity of rules and a variety of distortions to trade. In November 1982 ministers

of the GATT contracting parties agreed to a review of the rules the parties applied. But at the end of the Uruguay Round in 1994 all that had been agreed was a general framework of principles for RoO and the initiation of a work programme to harmonize non-preferential RoO.¹⁸ There was a statement of general principles for preferential RoO: these should be objective, predictable, coherent, based on positive standards and not (ab)used as instruments of trade policy/protection. But preferential rules were not included in the work programme. The agreement also expressed a preference for the CT criterion to determine substantial transformation, so the work on harmonization proceeded with efforts to define the CT criterion on a product-by-product basis. If, and only if, the CT criterion could not be used for technical reasons was the harmonized rule to be based on either a percentage VC or a TR (manufacturing or processing operations).

The work programme on non-preferential rules has been undertaken by a committee on RoO and a technical committee on RoO, under the auspices of the Customs Cooperation Council (CCC), but little progress has been made and deadlines missed, due in no small part to a failure to agree on how to treat sensitive sectors such as agriculture, textiles and clothing (Schiff and Winters, 2003: 31). A new work programme agreed in July 1998 focused on problematic areas, such as the implications of harmonized RoO on other WTO agreements, discussion on product-specific rules, outstanding issues on product-specific rules, definitions, etc. The work programme has also been criticized on the grounds that a lack of human and technical capacity means that developing countries are not fully represented, with the result that their interests are not fully taken into account in the rule-making process (Lal Das, 2003).

Regulation and harmonization of preferential rules

What might be done to address the failure to make progress towards harmonization of preferential (and non-preferential) RoO? Wonnacott (1996) proposed the elimination of the RoO below a certain tariff level – a kind of expanded *de minimis* rule. Serra et al. (1997) recommended that preferential RoO should in general not be more restrictive than those that existed before the FTA was concluded. Schiff and Winters (2003) argued that the former proposal is too mild and the latter impractical. Instead they support a single set of internationally agreed RoO or, failing this, a rule requiring preferential RoO to be identical to non-preferential rules to reduce the use of RoO for protectionist purposes. Estevadeordal and Suominen (2004) also called for harmonized RoO based on non-

preferential rules. Bi-regional business sector initiatives like the Transatlantic Business Dialogue (TABD) have addressed issues related to RoO (see for example UNICE, 2000: 51–61), and these may play a functional and more prominent role in future harmonization initiatives.

The WTO agenda on preferential RoO has been set by its secretariat (WTO, 2002b), prepared upon request of the Negotiating Group on Rules. This includes whether preferential RoO should/could be interpreted as “other regulations of commerce” under art. XXIV(5) of GATT 1994; whether diagonal cumulation contravenes WTO rules when certain third countries are favoured (which is linked to the question of RoO in networks of overlapping RTAs); and the feasibility of preferential rules’ harmonization in the long run (WTO, 2002b: 13, 21, 27–28; WTO, 2002a).

There appears thus to be a clear case for efforts to establish basic principles for preferential RoO. Although this will be a complex task, a number of basic principles for the harmonization process can be applied. For example, there should be agreement that the principle aim of RoO should be to facilitate trade liberalization; the number of criteria applied in determining the origin of a product should be minimized and preference given to a CT for reasons of simplicity and transparency; where a choice exists between criteria this should be kept to a minimum, and the degree of transformation required by each criterion should be equivalent; verification procedures should be transparent and as simple as possible; and there should be a multilateral agreement within the WTO on a common methodology for non-preferential and preferential RoO (Garay and Estevadeordal, 1996). In particular, preferential RoO should use non-preferential (WTO/World Customs Organization) rules as a reference point. RoO should not be used when the differences between FTA members’ third-country tariffs are minimal or when their tariff levels are low. Efforts should be made to harmonize external tariffs on a sector basis in areas where the nature of production processes and the internationalization of production make administering RoO particularly complex.

Conclusions

The proliferation of RTAs has led to a proliferation of preferential RoO. These rules have become more complex and less transparent over time, resulting in higher transaction costs. Moreover, they are apparently increasingly used for protectionist purposes, especially by industrialized countries in sectors like textiles and clothing, automotive products and agriculture (when these are included in the RTAs). The prevailing RoO

have resulted in the underutilization of trade preferences by exporting developing countries, and they imply important governance costs for these countries.

The EU and NAFTA rules, which are the most restrictive rules in the world and which typically show high degrees of variation between product categories, represent the dominant models. These dominant models are still increasing their influence in the rest of the world. As a result, RoO in North-South RTAs are usually more restrictive than those in South-South agreements. The relatively recent proliferation of inter-regional agreements forms an important transmission channel for the diffusion of these models.

There is clearly a need for multilateral regulation of preferential RoO. The *de facto* proximity (similarity) of the EU, US and NAFTA (or more precisely the “new-generation”) models provides an opportunity for harmonization. *De jure* harmonization of preferential RoO will not be achieved in the short run, however. Progress will depend on how the harmonization process of non-preferential rules evolves, how the origin is applied in other areas of multilateral rule-making such as trademarks, origin marking, anti-dumping, SPS etc. and the strength of protectionist pressures in specific sectors. Progress might be facilitated by further detailed analyses of the costs of the existing amalgam of preferential RoO.

Acknowledgements

The authors wish to thank Steve Woolcock and participants at an LSE/ UNU-CRIS workshop in Brussels (December 2004) and the CSGR/ UNU-CRIS/CIGI conference in Warwick (October 2005) for comments on a previous draft, as well as US and EU officials for providing useful information. The authors are solely responsible for the text.

Notes

1. The import content of manufactured exports varies between >45 per cent (on average) in East Asia and the Pacific and around 25 per cent in South Asia (World Bank, 2005: 47).
2. The HS was developed by the Customs Cooperation Council (CCC) and implemented by the International Convention on the Harmonized Commodity and Description Coding System on 1 January 1988. It is important to note that the HS was not developed to be used in the determination of origin, but for statistical and commodity classification purposes.
3. The European Union is the only regional bloc that also adopted a common set of non-preferential RoO.

4. The Europe Agreements refers to a set of bilateral agreements with the CEECs with the objective of preparing them for eventual accession.
5. Diagonal cumulation is the system that facilitates trade by enabling the inclusion of products from outside an RTA that have obtained originating status in assemblies or products from RTA partners without these assembled products losing their originating status.
6. Full cumulation is when products from RTA partners are taken to be originating regardless of their composition. In other words, they can contain products originating outside the RTA and there is no attempt to measure the RTA or third-party content.
7. No change specifies for almost 20 per cent of the tariff universe (table 4.1).
8. Outward processing is when goods produced in one country/customs territory A are processed abroad and then returned for sale in A. In such cases duty (i.e. the tariff) has to be paid only on the value added abroad. Without such a system, duty would have to be paid on the goods as produced in A as well as on the value added abroad.
9. Cyprus and Malta were also included in the protocol. The inclusion of the Mediterranean partners in the pan-European system was decided in principle at the Euro-Med Trade Ministerial of March 2002 in Toledo. These advances are part of the economic and financial partnership dimension of the Barcelona process, initiated by the establishment of the Euro-Med partnership at the conference in Barcelona in November 1995. The declaration supported the creation of an FTA by 2010 to be established through the completion of the Euro-Med association agreements (EMAs).
10. Bilateral agreements have been signed with Israel (in 1995), Tunisia (1995), Morocco (1996), the Palestinian Authority (1997), Jordan (1997), Egypt (2001), Algeria (2001) and Lebanon (2002).
11. The analysis was carried out with aggregate flows. It is likely that more disaggregated flows would reveal more variation.
12. On UNICE's position on RoO and customs policy in general, see UNICE (2000).
13. With positive Pearson correlation coefficients (greater than 0.3) with a level of confidence of 0.01 per cent.
14. For these poles 44 per cent of the subtariff headings compared (or 4,538 subheadings from the tariff universe at the six-digit HS level) were found to be representative for the RoO regimes against which they were compared. The degree of "representativeness" of the distinctive rules of the four origin regimes may be specified as follows: a representative rule, which is identical in the four regimes, is applied to 4 per cent of the subheadings of the tariff universe; a highly similar rule between regimes corresponds to another 6 per cent; a fairly similar rule applies to another 20 per cent; and a similar or barely similar rule is applied to another 14 per cent. Moreover, a certain trend would seem to exist showing a relatively higher level of "similarity" between the regimes of origin in the case of goods with less technological complexity. The main RoO representative of the four regimes are CTC (without exception or VC or TR requisites), applicable to 44 per cent of the subheadings with a representative rule – that is, 877 subheadings; CTH (without any other requisite), applicable to 32 per cent of the subheadings with a representative rule; and CTC with exception to raw materials included in certain subheadings and with TRs, applicable to 11 per cent of the subheadings with a representative rule. For the remaining subheadings of the universe it is not possible to assign a representative RoO for the regimes considered because there is at least one origin rating criterion for which a representative value does not exist. The absence of representativeness does not necessarily imply a discrepancy in all the components of the rule; on the contrary, in the majority of cases the discrepancy is present in only one or two of its criteria. For the 2,530 subheadings without a representative rule the cause for the dissimilarity occurs in 71 per cent of the cases related to the CT criterion and, to

a much lesser extent, the ECT. Besides, in only 327 of such subheadings is the discrepancy generated around two or more criteria. The MCCA origin regimes and the one representative of the MERCOSUR pole tend to be the most dissimilar among the origin regimes considered. In particular, both regimes differ specially in the employment of the CT criterion (MERCOSUR pole 59 per cent and MCCA 55 per cent) and, to a lesser extent, in the ECT (MERCOSUR 26 per cent and MCCA 27 per cent). The remaining differences in the criteria of origin rating are of scarce relative importance. The NAFTA regime differs substantially from other regimes only in 23 per cent and 10 per cent of the subheadings without a representative rule in terms of the CT and ECT criteria, respectively. The Mexico pole regime stands out for having the fewer dissimilarities as it differs significantly from other regimes in only 5 per cent, 10 per cent and 6 per cent of the subheadings without a representative rule in terms of the CT, ECT and VC criteria, respectively (Garay and Cornejo, 2001a).

15. For a detailed comparison of control and certification measures in both models, see Keizer (2004).
16. Roll-up occurs when imported parts are substantially transformed in a preference-receiving country into an intermediate part whose whole value then counts towards fulfilling the value-added requirement for the final good.
17. These rules were similar to the COMESA RoO.
18. The harmonized set of RoO will be established by the Ministerial Conference as an annex to the ARO, and will thus technically and formally be part of the legal text of GATT 1994.

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The interaction between levels of rule-making in public procurement

Stephen Woolcock

Introduction

Public procurement was excluded from GATT 1948 because of a concern that compliance costs would be excessive and exclusions would undermine the effectiveness of an agreement,¹ and a desire to retain procurement as an instrument of industrial policy. In the absence of any international rules, national rules evolved along divergent paths consolidating national procurement preferences. Since the establishment of GATT there have been repeated efforts to contain this divergence and develop rules governing public procurement (PP). This case study illustrates how these efforts have occurred on different levels. The leading proponents of wider international rules, initially the United States and subsequently the European Union, have used plurilateral and more recently bilateral/regional agreements to promote the wider application of rules when a range of developing and some developed countries blocked the multilateral route. On balance, however, the case of PP shows how synergy between different levels of rule-making has resulted in development of more extensive rules.

The importance of PP

PP makes up 7–8 per cent of GDP in developed (OECD) economies, where it was estimated that central government procurement alone ac-

counted for US\$1.795 trillion each year (OECD, 2002a). In non-OECD countries procurement is estimated to average about 5 per cent of GDP or a total of \$287 billion in total contestable markets, with the 40 major developing economies accounting for most of this. Sixty of the 106 developing countries included in the OECD figures had PP of less than \$1 billion per annum (OECD, 2002a). In terms of the trade effects of procurement one might argue that the lion's share is accounted for by the OECD countries plus some 10 developing or transitional countries. A plurilateral regime that covered these would therefore encompass most PP. Although on a smaller scale, PP is equally if not more important for smaller countries and developing countries. Evidence from World Bank and other surveys suggests that developing countries find maintaining sustained reform of procurement practices in order to establish more competition, make better use of limited public funds and restrict the scope for corruption is difficult without external discipline (Evenett, 2003).

Definitions of PP

This chapter uses the term “public procurement” rather than the term “government procurement” that is used in much of the discussion. PP is a wider concept, in that it includes not just purchasing by government but also that by public enterprises, such as in the form of utilities (e.g. energy, transport, postal services, telecommunications and water). As will be shown, the determination of the coverage of framework rules on purchasing is an important element in any agreement. Table 5.1 provides a breakdown of the main elements of rules on PP in line with the analytical framework set out in chapter 1.

PP is also diverse in terms of the types of things purchased. These range from standard items, such as school equipment or delivery vehicles for postal services, to major pieces of capital equipment, such as generating sets for power stations or the power stations themselves. PP can include supplies (i.e. goods and equipment), works (construction projects) or services (such as architectural services or insurance). It can include all levels of government, including central government agencies and departments, state and regional government and local government. In recent years agreements at both the regional and plurilateral² levels have included public agencies or public enterprises and, in some cases, private companies which operate under rights granted by public agencies or governments. Broadly speaking central government accounts for about one-third of all PP, lower levels of government about one-third and public enterprises such as utilities the remainder.

Table 5.1 The elements of rules in public procurement

Coverage

Rules may cover procurement of supplies (goods) only or also works contracts (construction) and services. Rules covering central government will mean that 60–80 per cent of “public purchasing” remains outside the rules, with 30–40 per cent at sub-central-government level and the rest in public enterprises such as utilities. Some rules cover private companies that benefit from “special or exclusive rights” granted by government, because it is thought that such rights can be used to influence procurement.

Coverage is also determined by thresholds below which contracts are exempt from the rules. The aim of such thresholds is to ensure that the most valuable contracts are open to competition whilst avoiding significant compliance costs on the larger number of smaller contracts.

Principles

As noted above, PP was excluded from GATT national treatment and MFN provisions, so one important issue in any negotiation is the extension of these principles to PP or any regulation or procedure associated with PP. A national treatment and MFN obligation would, for example, prohibit *de jure* discrimination between different national suppliers.

Transparency

Central to the aim of facilitating increased competition in PP is the provision of information. This can encompass the statutory rules on procurement, including those on contract award procedures set out below, and information on specific tenders. Without this information non-local suppliers would not be able to bid for contracts. In practice, transparency represents a major contribution to “liberalizing” public contracts.

Contract award procedures

Standard (harmonized) contract award procedures can considerably enhance transparency, but these also need to accommodate the diverse nature of contracts. Rules on procurement do this by providing for open, restricted or selective and single or negotiated tenders. Open tendering is used when procurement concerns standard commodities or products where price is the only or the predominant factor. Restricted or selective tendering is used when the purchasing entity wishes to be sure that the potential suppliers are qualified (both technically and financially) to complete the contract successfully. In restricted procedures the purchaser keeps a list of certified or approved suppliers, who are then invited to bid for tenders. This means that open and transparent procedures and criteria have to be devised to determine which suppliers are qualified to produce the goods or service. When special expertise or knowledge is needed, single/negotiated tendering may be used, in which a specific supplier is selected and negotiations on a contract conducted.^a For all forms of tendering there are also important details concerning, for example, how calls for tender are made and what information is provided, and what time limits are set for bidding and for awarding contracts. For example, short time limits may put foreign bidders at a disadvantage, while long time limits may be detrimental to the service provided by the procuring entity.

Table 5.1 (cont.)

Technical specifications

By requiring suppliers to comply with specific technical specifications or standards, a procuring entity can prefer certain suppliers over others. Rules on procurement may therefore require the use of international, regional, national or other standards, or require the use of performance standards over design (or prescriptive) standards. Performance standards set out how the equipment or system should perform, not the details of its components or dimensions.

Regulatory safeguards

As with other rules there may be scope for exclusions from national treatment and other obligations under PP rules, such as on grounds of human health or national security. Apart from such formal exemptions, discretion in contract award procedures, discretion not to award a contract or discretion in the use of enforcement provisions, such as waiving contract suspension rules, can all be seen as constituting forms of regulatory safeguards.

Reciprocity

Typically WTO negotiations include market access and rule-making elements. But, as noted above, rules on procurement straddle this divide. Market access negotiations in the field of procurement have tended to take the form of an exchange of schedules determining the coverage of an agreement – hence the country schedules annexed to the 1994 GPA agreement and the requirement that all new signatories to the GPA negotiate schedules and thus reciprocity with the existing signatories. In this sense negotiating partners have sought to achieve reciprocal market access. Here the focus is on the benefits accruing from access to other countries' procurement markets. There are, indeed, two elements to the WTO GPA "liberalization": a framework agreement setting out the rules and obligations on signatories, and "market access" in the sense of the negotiation of country-by-country commitments on sector coverage. It will be argued here, however, that on the basis of evidence from existing rule systems, greater transparency and better procedures in awarding contracts will lead to increased competition but not to a great deal more import-market penetration. This means that most of the benefit of introducing rules governing PP is likely to accrue to the economies introducing transparent rules.

Compliance provisions and remedies

Experience shows that without effective compliance rules on PP will have little effect. Given the thousands of contracts awarded every day it is very difficult to have an effective form of central compliance monitoring. Rules have therefore provided for bid-challenge procedures, which provide bidders who believe they have not been fairly treated with an opportunity to seek a review – by an independent body – of a contract award decision. Penalties in the case of non-compliance may involve project cancellation or financial penalties (sometimes limited to the costs of bids, and sometimes exemplary damages). Rules requiring information on contracts awarded and reasons why bids failed can also be seen as facilitating compliance.

^aNote there is a difference between negotiated procedures for contract award and post-award negotiations.

Liberalization and de facto and de jure discrimination

It is worth clarifying what is meant by “liberalization” of PP, because this is not as straightforward as removing a tariff. Explicit preferences for local suppliers are an obvious means of providing a national or regional preference. For example, the United States maintained “buy American” preferences of 6 per cent for many years. The European Union included the option of a 5 per cent price preference for EU suppliers in its regional liberalization measures for utilities, although this has not yet been used. In India price preferences of 15 per cent are provided for small and medium-sized companies in order to promote this sector of the economy. Such explicit preferences that are based on the nationality of the supplier are inconsistent with national treatment; thus liberalization of procurement markets in this context means conformance with national treatment.³ But these *de jure* preferences pale in comparison to the *de facto* preferences in the allocation of public contracts.

Opaque or complex contract award procedures can constitute a form of local preference even when trade agreements have committed governments undertaking the procurement to national treatment and MFN.⁴ Where contract award procedures are complex or when different ministries or purchasing entities use different contract award procedures, it is likely to be much harder for suppliers or contractors not familiar with the different procedures to be successful.

Perhaps the most important source of *de facto* preference, however, is the exercise of discretion in contract award procedures. Rules generally allow a good deal of flexibility; for example, all major regimes provide for restricted or negotiated procedures as well as open tendering. Restricted tendering is when a limited number of contractors are invited to tender, and negotiated contracts are used when only specific companies can supply the goods or services. Contract award criteria such as “the most advantageous” or “economically efficient” bid also provide scope for discretion that can be used to favour local or national suppliers. It is very difficult to exclude such abuse of discretion without making the rules excessively rigid. National treatment or MFN obligations have little or no effect on such *de facto* preferences, which undermine confidence that contracts will be awarded fairly, deter competitors and allow *de facto* closed markets to remain.

The use of proprietary or design standards (as opposed to harmonized international standards or performance standards) in defining technical specifications also enables *de facto* discrimination. Finally, there can be *de facto* discrimination if the provisions of national or international rules governing procurement are not applied or not rigorously applied.

To address *de facto* discrimination and “liberalize” markets requires

rule-making that enhances transparency and reduces the scope for the abuse of discretion on the part of the procuring entities.

In PP the distinction between rule-making and market access has been further complicated because of the way rules on procurement have been negotiated over the years. As discussed below, it has been expedient to divide discussion of the rules from questions of which sectors will be subject to the rules. This enabled negotiators in effect to separate work on what might be seen as the liberal aim of economically rational, transparent procurement rules for all from the (mercantilist) sector interests that lay just below the surface of the negotiations. This resulted in a coherent set of rules, but negotiations on coverage produced an intricate, opaque and illiberal set of lists and schedules in the pursuit of reciprocity (Arrowsmith and Trybus, 2003; Reich, 1997).

The issue of what is liberalization has an immediate bearing on the ongoing discussion of PP in the WTO. With no agreement on the inclusion of PP in the Doha Development Agenda, a compromise was sought in which “transparency” in PP would be included but not “market access”. But the fact that in reality one cannot distinguish between these two created difficulties in the negotiations. From an economic point of view “there is [also] little to be gained by separating negotiations on transparency from negotiations on market access to procurement markets” (Evenett, 2003: 4; Evenett and Hoekman, 2004: 281). Developing countries have assumed that transparency is part of market access, or at least the first steps towards the liberalization of PP. This is a reasonable assumption given the history of negotiations on PP (see below), in which rules were seen by sectors seeking to open (and protect) markets as a means of facilitating market access. Paradoxically, work on the effects of discrimination in PP has found that the use of non-discriminatory rules appears to result in more competitive markets and thus enhanced welfare, but no significant increases in market access (Evenett and Hoekman, 2004). This has also been the experience in the European Union, which has the most developed and stringent rules on PP, but which has seen only modest increases in PP markets being supplied by producers in other EU member states (Woolcock, 1991).⁵

A history of interaction between multilateral and regional approaches

The ITO debate

As in all rule-making, current approaches to procurement rules have been shaped by past negotiations and precedent. In the case of PP, as

with other cases considered in this study, there is in particular a history of interaction between multilateral and regional regimes. This section covers the period from the ITO to the mid-1980s, and argues that regional initiatives have had a significant and generally favourable impact on efforts to “open” PP markets. The following sections cover the period from the mid-1980s until the mid-1990s and the post–Uruguay Round period.

Some of the central issues discussed above were already on the agenda at the time of the Havana Charter. The US draft ITO charter included specific reference to public purchasing, but the MFN and national treatment obligations that this contained were limited to central government. Opponents argued that existing buy-national measures in many countries would undermine the credibility of the rules. Britain opposed the inclusion of local government on the grounds that this would create insurmountable problems of compliance. The inclusion of services was discussed but rejected, because here rules would affect the treatment of foreign nationals, and the drafters of the ITO wished to avoid such entanglement. This opposition resulted ultimately in the explicit exclusion of PP from the MFN provisions and the removal of any specific reference to it in the national treatment provision (Blank and Marceau, 1997). As a compromise the US delegation accepted some weak wording in the provisions on state trading, to the effect that where government was the purchaser it should provide “fair and equitable treatment having full regard to the relevant circumstances”, although the drafters appear to have made the incorrect assumption that state trading was the same as PP, which it is not (Blank and Marceau, 1997). GATT took over the approach and exact drafting produced for the ITO, so that PP was excluded from GATT coverage. The sense of the negotiating history is that the issue of PP would be revisited sometime in the future.

When the Treaty of Rome was drafted in 1957 there was no specific reference to public purchasing. This was in part because of the nature of the treaty as a framework treaty. There were provisions on non-discrimination and national treatment which could have – and subsequently have – been used to challenge discriminatory practices in PP. Other provisions, such as those covering competition and public enterprise (arts 90–92), also might have been used for this purpose. But the sentiment at the time the treaty was negotiated was not ripe for inclusion of European-level discipline in this sensitive policy area (Blank and Marceau, 1997).

Work in the OECD

No work was initiated in GATT, but in the early 1960s discussions began in the OECD. Serious discussions were precipitated by a 50 per cent

increase in US preference for domestic defence contractors. European complaints led to a survey of national procurement policies and practices in 1963, the results of which were published in 1966 (OECD, 1966). This work led to the drafting of a set of guidelines on PP rules covering transparency in contract award procedures. The work in the OECD also introduced the concept of thresholds, to catch the economically most important contracts but to relieve procurement entities of an undue burden of compliance costs. At the same time as the OECD work being done, the European Commission was drafting the first EEC directives aimed at implementing the non-discrimination principles of the Treaty of Rome in the PP sector within the EEC. The EC's 1965 proposals used the model of the OECD code, but were not adopted until 1971 as the Directives on Public Suppliers and Works.

In 1969 the US government, prodded by US suppliers seeking access to the European and Japanese heavy electrical equipment markets, proposed a sector agreement on the liberalization of PP in this sector (Epstein, 1971).⁶ The idea of a sector agreement was resisted by the Europeans because it was clearly targeted at them. Most European governments used preferential procurement to promote national champions in key sectors. There was also no common position within the EEC on how to treat procurement in the utilities sector. Germany had a number of powerful privately owned utilities that rejected any inclusion in EU rules, but France and other member states with public utilities were not ready to open their utilities unless German private utilities were also covered. The issue of EC competence in trade negotiations on procurement was also not clear at this point.⁷

The US proposals for a code on PP were, in part, due to pressure from US electrical equipment and later telecommunications equipment exporters, who wanted access to the European and Japanese utility markets. Discussions in the OECD faced differences between the United States and the European Union on the level of thresholds and coverage. The United States wished to limit coverage to central government, whilst the Europeans wanted to adopt the approach taken by the EEC directives that included central, regional and local government. On contract award procedures the United States also proposed a system of open tendering used in US federal procurement, but the European Union and Japan argued for selective tendering as an option because they used this in domestic rules.

The 1979 GATT Government Purchasing Agreement

Discussions on possible OECD guidelines on PP continued until 1975, with progress towards agreed rules on procedural issues and transpar-

ency, but not on coverage and thus “market access”. In 1976 the chairman of the OECD working group submitted a draft instrument on government procurement, policies and practice to GATT. This can be seen as the distillation of 15 years of work in the OECD, enriched by the EEC experience in drafting similar EU rules. The European Union was working on its rules on PP that led ultimately to the adoption of, for example, the directive of December 1976 that set out the revised procedures for the award of public supply contracts (i.e. goods) in all member states (Bourgeois, 1982). The OECD draft was taken up by the GATT Sub-committee on Government Procurement that had been set up early in 1976 as part of the Tokyo Round negotiations (1973–1979). As the Tokyo Round had a completion deadline of the end of 1977, this was the optimum time for the OECD to provide an input. Developing participants in this subcommittee believed that PP was an area of some interest to them, and one in which there was scope for special and differential treatment.

There is little doubt that “to a very large extent the logic and wording of the OECD draft was incorporated into the draft integrated text for negotiations on government procurement of December 1977” and thus provided the model for the qualified MFN code in the Government Purchasing Agreement (GPA) of 1979 (Blank and Morceau, 1997: 41). The GPA reintroduced national treatment and MFN treatment (art. II) for signatories with regard to all laws, regulations, procedures and practice regarding procurement of products by the entities covered (GATT, 1979). It included detailed transparency rules on advertising contracts, the submission, receipt and opening of tenders and the awarding of contracts. All of these measures were more or less exactly as they had been developed in the OECD and adopted in EC directives. On tendering procedures the OECD compromise of allowing open, selective and single tendering was also carried over into the GPA. This approach had also been used in the EEC directives of the early 1970s.

The weaknesses of the GPA, such as its limited coverage, also reflected the status of the OECD discussions.⁸ Only central government purchasing of supplies (i.e. goods) above 130,000 special drawing rights (SDRs) were covered. Public works and services contracts were excluded, as were sub-central-government purchases due to the opposition of federal states, such as the United States, Canada and Australia. Utilities were excluded due to the opposition of the European Community, which had made no progress on this within the European Union⁹ and was therefore unable to make commitments on this in GATT.

A second weakness was the absence of any effective enforcement provisions. More particularly the GPA did not include a bid-challenge system that would enable aggrieved tenders to bring actions. The OECD

had made proposals for a kind of bid-challenge mechanism, but this was seen as too ambitious at the time (Blank and Marceau, 1997). The 1979 GPA required entities to provide information on the contracts awarded and reviews of the contract award decision, but there was no requirement to provide for an independent review of decisions. The only means of enforcement were standard GATT consultation and dispute settlement procedures, which given their inherent delays could clearly offer no remedy for unfair contract award decisions but could only address laws, practices or procedures that systematically discriminated against foreign suppliers. With hindsight the absence of any effective bid-challenge provision in the 1979 GPA was a major reason why it had little effect on liberalizing procurement markets.

Although the agenda of the negotiations was set in the OECD, India, Korea, Nigeria and Jamaica participated actively in the GATT negotiations on the 1979 GPA. None of these countries signed the GPA, however, because they feared the rules might threaten the use of procurement to promote industrial and development objectives (despite the special and differential treatment provisions included), and because of what they saw to be the excessive compliance costs. Developing countries were also unhappy about the bilateral negotiation of coverage that put them at a distinct disadvantage *vis-à-vis* major developed countries and added to the costs and complexity of the agreement. The GPA was therefore a plurilateral agreement signed only by the OECD countries (less Australia and New Zealand), Hong Kong, Singapore and later Israel. Developments – or rather lack of progress – in European regional initiatives had a negative impact on the multilateral negotiations because failure to agree coverage of utilities within Europe meant these were also excluded from the GPA. This and the other limitations on coverage discussed above meant that the GPA covered only about one-third of public expenditure in the signatory countries, and even then demands for reciprocity meant that although the rules were plurilateral the coverage was determined by bilateral schedules using positive lists. The economic impact of the 1979 GPA was limited.¹⁰

Interaction in the 1986–1994 period

Progress on procurement rules during the 1986–1994 period came from advances at the regional rather than the plurilateral or multilateral level.

The EU level

The EC directives of the 1970s had very little effect in opening markets. Discretion under the rules, entrenched practices, technical requirements

and splitting of contracts to bring their value below the thresholds all contributed to keeping markets closed. More importantly, with no confidence they would get a fair chance, foreign suppliers simply did not bother bidding, with the result that non-national suppliers accounted for only 4 per cent of public contracts in Germany and less than 1 per cent in Italy and Britain (European Commission, 1986a). PP represented a major gap in the Single European Market (SEM), just as it did in GATT.

The EU SEM programme therefore included a range of directives on PP. The earlier EU directives on supplies and works were revised to tackle evasion, but otherwise the new rules followed the pattern of the earlier directives (and the GATT 1979 GPA) by providing flexibility in the form of open, restricted and negotiated contract award procedures. Stronger transparency rules were introduced, and purchasers were obliged to use agreed European or international standards where these existed and performance (rather than design) standards where they did not. Like the GATT rules, the European Union used thresholds, which for supplies were set at the same level as the GATT GPA (Directive 80/767, *EEC Official Journal* 4215). The use of regional rules as models for plurilateral rules is illustrated in the fact that the European Union set a threshold of 5 million ecus for works (construction) contracts, a level subsequently used in the 1994 GPA.

Interaction between the European Union, the CUSFTA and GATT

The EU's SEM programme was being developed in parallel with negotiations on the CUSFTA (Canada-US FTA) and the work of the Uruguay Round Working Group on Government Procurement (WGGP). Indeed, negotiations on revision of the GPA in the WGGP really only began in earnest in 1988 once the CUSFTA had been adopted and the European Union had produced drafts of its planned directives on the so-called "excluded sectors" – the utilities, including power and telecommunications, along with water and transport.¹¹ The EU programmes also included stronger compliance rules that emulated the "bid-challenge" rules of the 1988 CUSFTA (European Commission, 1986b; Compliance Directive 89/665, *EEC Official Journal* L395, 1989).

The EC Compliance Directive¹² set out minimum common requirements for review and compliance provisions. Each EU member state was obliged to provide access to independent reviews of contract awards for aggrieved suppliers, establish powers to suspend contract award procedures, set aside decisions taken unlawfully, require purchasing entities to remove discriminatory specifications from calls for tender and award damages. The controversial issue of contract suspension illustrates again the interaction between the EU and GATT rules. Concern that contract

suspension would interrupt “normal” commercial practice resulted in the EC directive providing a national-interest waiver. The relevant provision reads: “when considering whether to order interim measures (including suspension) the body responsible (the local implementing body) may take into account the probable consequences of the measures for all interests likely to be harmed, as well as the public interest, and may decide not to grant such measures where the negative consequences could exceed the benefits” (art. 2(4)). This waiver subsequently found its way into the 1994 GPA (see tables 5.2 and 5.3).

The SEM rules also covered purchasing of *services* by central, regional/state and local government entities (Council Directive 92/50/EEC, relating to the coordination of procedures for the award of public service contracts), but a two-tier approach was adopted in which the initial market-opening effort was focused on the “easier” service sectors such as telecommunications and financial and professional services. There is an interaction here with the GATS negotiations, which were focused on these sectors at that time. The more sensitive sectors, such as rail transport, legal services, education and health, were left for a later date, although calls for tenders in these fields still had to comply with the transparency provisions of the EU’s directives. The structure of the EU rules for procurement of services adopted the same approach as for supplies and works and were subject to the same compliance rules, but with a higher threshold of 200,000 ecus. The EU’s SEM programme therefore went beyond the 1979 GPA on coverage, to include works (construction) and services, as well as on enforcement by following the CUSFTA to include bid-challenge rules.

The SEM also went beyond the GPA by including purchasing by *utilities*. Alternatively, it could be said that the European Union finally acted to remove the blockage it had represented to the inclusion of utilities in the GPA. The 1990 SEM rules extended coverage to telecommunications, power, gas, water and transport services (Utilities Directive 90/531/EEC). By 1990 privatization and the general shift towards more liberal policies altered the balance of interests, but it was still necessary to establish a “level playing field” by including private utilities that benefited from special or exclusive rights as well as publicly owned utilities. This arrangement cleared the way for the inclusion of utilities in the GATT GPA.

The basic structure of the Utilities Directive was similar to that of the earlier EU directives. Greater sensitivity to compliance costs on the part of private utilities, however, meant thresholds were set higher, at 400,000 ecus for the energy, water and transport sectors and 600,000 ecus for telecommunications. These thresholds set the precedent for equivalent rules in the 1994 GPA. There was also somewhat greater flexibility shown in

the use of restricted and negotiated tendering to placate lobbying from powerful (private) utilities. Services procurement by utilities was excluded from the initial SEM rules, which meant the EU position in the GPA negotiations on coverage excluded services until 1992, when a further EC directive extended coverage to services. So again the pace of liberalization within the European Union had a direct bearing on the pace of rule-making within GATT.

Regional standards-making may also have facilitated wider international liberalization. Technical specifications posed – and pose – a particular problem in utilities that provide network services, because of the need to ensure compatibility of equipment connected to the network. In the case of the EU utilities there was a large backlog of agreed international standards – in other words, firm-specific or “design” standards that could prejudice competition were still in use. To counter this, the European standards institutions were mandated to work on the technical standards needed to facilitate an opening of markets in the utilities sector.

Compliance or bid protest in the utilities sector caused some major difficulties, because private utilities opposed what they saw as onerous compliance costs and regulation. This led to the EU rules including a range of additional options, such as the use of financial penalties for non-compliance or attestation of contract award procedures (Utilities Remedies Directive 92/13/EEC). In practice this meant countries could opt for the approach they preferred, so that the benefit for suppliers of having a common approach to bid protest was lost.

Reciprocity provisions

As the EU SEM measures went beyond the GPA (1979), the issue of access for third-country suppliers soon arose. Some member states argued for reciprocity provisions to ensure that third countries offered EU suppliers equivalent access. In the case of supplies (goods and equipment) bought by central government, the 1979 GATT GPA code prohibited any reciprocity provision. In the case of works (construction), companies tendering for contracts usually had a presence in the European Community and would normally in any case use local subcontractors, so local value added was less of an issue. In the service sector there was strong opposition to reciprocity provisions in some member states. The earlier 1989 Second Banking Directive had included reciprocity provisions and precipitated the “fortress Europe” debate between the European Union and (primarily) the US government and financial services sector. The liberal EU member states therefore clearly sought to avoid a similar reaction in the services procurement field.

Table 5.2 Main elements of key regional/bilateral agreements compared to the GPA

	1994 GPA	EU-Chile	EU-Mexico	NAFTA
Coverage	<p>Cat. I Central government supplies and works negative list, services positive list Thresholds: Supplies and services 130,000 SDRs, works 5 million SDRs</p> <p>Cat. II Subnational government “Voluntary” upon first subnational level, no local government Thresholds: Supplies and services 200,000 SDRs, works 5 million SDRs</p>	<p>Coverage of central, subcentral government and utilities as per GPA for EU and equivalent for Chile (annexes XI and XII)</p> <p>Goods, services and works</p>	<p>Coverage by entities broadly equivalent to NAFTA for Mexico and GPA for EU (annex VI)</p> <p>Goods, services and works covered as per schedule (annexes VII–IX)</p>	<p>Central government First subfederal level coverage to be agreed this process was driven by negotiations in GATT</p> <p>Goods, works and services through negative listing</p> <p>Threshold slightly lower than GPA: \$50,000 for goods and services, \$6.5 million for works, \$250,000 and \$8 million respectively for public enterprises</p>

Cat. III Other entities e.g. utilities Thresholds: Supplies and services 400,000 SDRs; works 5 million SDRs		No private companies covered, even regulated utilities
Principles	National treatment and MFN for signatories	National treatment and non- discrimination (art. 10003)
Transparency	Information to be provided on national procurement laws and rules	Detailed information on tenders and decisions to facilitate private actions and reviews
	Contracts to be advertised to facilitate international competition	Provision of detailed information on tenders and decisions
	Information on why bids unsuccessful on request (art. 154)	Statistics to be provided that help ensure there is no systematic evasion of provisions (art. 31)
Contract award procedures	Option of open, restricted or single tendering	Open, restricted and single tendering
	Open and selective (i.e. restrictive); single tendering possible in exceptional cases (arts 143–146)	Detailed procedures vary slightly from GPA

Table 5.2 (cont.)

	1994 GPA	EU-Chile	EU-Mexico	NAFTA
Contract award criteria	Lowest price or most economically advantageous bid	Lowest price or most advantageous bid based on previously determined criteria	Lowest price or most advantageous bid based on previously determined criteria	Lowest price or most advantageous bid based on previously determined criteria
Technical specifications	Use of international standards encouraged; performance standards preferred to design standards	Performance rather than design or descriptive standards (art. 149)	No mention	Performance standards rather than descriptive standards
		International, national or recognized standards to be used, but exceptions possible		Encourages use of international standards, but exceptions always possible (art. 1007)
Compliance provisions	Bid challenge introduced in GATT for first time Independent review	Bid challenge (art. 155) Independent review	Bid challenge (art. 30) Independent review body with detailed provisions relating to proceedings in review hearings (as in NAFTA)	Elaborate bid-challenge provisions Independent review body

	Interim remedies, but no contract suspension	Rapid interim remedies that may include contract suspension; compensation, but may be limited to costs of bid and protest	Rapid interim measures that may include suspension of procurement process but with override in public interest; compensation, but may be limited to costs of bid and protest	Rapid interim measures including suspension and termination of contract
Local content or presence	Prohibits origin rules	None	Substantial business activities test for services possible (art. 27)	Substantial business test for services possible (art. 1113)
Institutional provisions		Vague technical cooperation commitment (art. 157)	Special Committee on Government Procurement established to promote mutual understanding of procurement procedures Bilateral dispute settlement under title VI of the agreement	Technical cooperation
Extension provisions		If a party offers better terms to a third party it must open negotiations on an extension of terms		If a party offers better terms to a third party, negotiations on extension must be opened

Table 5.3 Main elements of recent regional/bilateral agreements

	US-Chile	US-Australia	US-Morocco	US-Singapore
Coverage	<p>Central government supplies and works</p> <p>Subnational government supplies, services and works</p> <p>Thresholds: Central government \$280,000 and \$6.5 million for supplies and works; \$518,000 for sub-central government for supplies and services, \$6.5 million for works</p>	<p>Central government supplies and services</p> <p>Subcentral (regional) government supplies, services and works</p> <p>Some public enterprises</p> <p>Thresholds: Central government US\$58,000 and \$6.7 million for supplies and services and works respectively; Regional government US\$477,000 and \$6.7 million; Public enterprises US\$292,000 or \$538,000 and \$6.7 million</p>	<p>Central government supplies and services</p> <p>Subcentral government supplies, services</p> <p>Thresholds: Central government US\$175,000 for supplies and services and \$6.7 million for works; Subcentral government US\$500,000 for supplies and services and US\$ 6.7m for works</p>	<p>Central government supplies, services and works as per GPA</p> <p>Subcentral government as per GPA schedules</p> <p>Some public enterprise as per GPA schedule</p> <p>Thresholds as for US-Australia</p>
Principles	National treatment (art. 9.2)	National treatment (art. 15.2)	National treatment (art. 9.2)	National treatment and non-discrimination as in GPA

Transparency	Information to be provided on national procurement laws, regulations and judicial decisions (art. 9.4)	Information on national laws, regulations and judicial decisions (art. 15.2)	Information on laws, regulations and judicial decisions (art. 9.3)	As in GPA 1994
	Contracts to be advertised to facilitate international competition (art. 9.4–9.6)	Notice of intended contracts to facilitate international competition (art. 15.3–15.6)	Notice of intended contracts to facilitate international competition (art. 9.4–9.6)	
Contract award procedures	Open procedure with option of restricted tendering (art. 9.9)	Open, selective and limited (art. 15.7)	Open tendering but with option of restricted tendering (art. 9.9)	As in GPA 1994
	Most advantageous in terms of requirements and evaluation criteria set out in tender documentation (art. 9.10)	Lowest price or most advantageous bid based on previously determined criteria (art. 15.13)		As in GPA 1994
Technical specifications	Use of international standards encouraged; performance standards preferred to design standards (art. 9.7)	Performance standards and use of international standards (art. 15.6)	Performance standards and use of international standards when possible (art. 9.7)	As in GPA 1994

Table 5.3 (cont.)

	US-Chile	US-Australia	US-Morocco	US-Singapore
Compliance provisions	Bid challenge with independent review (art. 9.13) Interim remedies, including contract suspension	Bid challenge with independent review (art. 15.11) Interim remedies, including contract suspension	Bid challenge with independent review (art. 9.12) Interim measures, including contract suspension	As in GPA 1994
Local content or presence	Determination of origin on non-preferential basis	Origin determination as in normal trade	Origin rules as in normal trade	As in GPA 1994
Institutional provisions	Committee on Government Procurement established to promote cooperation (art. 9.18)	Review under general Joint Commission on US-Australia FTA	No special committee	No special committee, no technical assistance or S&DT
Extension provisions	If a party offers better terms to a third party it must open negotiations on an extension of terms (art. 9.19)	If a party offers better terms to a third party it must open negotiations on an extension of terms	None	None

The EU rules on utilities did, however, include reciprocity provisions (arts 29 and 36 in the Utilities Services Directive) that allowed purchasing entities to reject bids if more than 50 per cent of the value of the contract was of non-EC origin. There was also scope to apply a 3 per cent price preference for EU suppliers in utilities. Normal EC origin rules were to be applied as per EC regulation 802/68. These reciprocity provisions were to feature in a major controversy in the final phase of negotiations of the GPA (see below).

EU bilateral agreements during the 1985–1995 period

Article 65 of the EEA (European Economic Area) agreement extended the EC *acquis*, including all provisions on procurement, to the EFTA states. Annex XVI to the EEA agreement listed those acts referred to in the *acquis*. There were a number of modifications to the procurement directives of a largely technical nature, and Liechtenstein and Norway were given transition periods to implement the utilities directives until 1994 and 1995 respectively.

The reciprocity provisions are also extended to the EEA area. Thus products originating in the EEA are not included in the calculation of origin for the purposes of article 29 of the Utilities Directive. The operation of article 29(3) (reciprocity) is based on the conditions that no existing trade agreements are affected and there is consultation between the contracting parties in their negotiations with third countries. The concrete result of this last requirement was that in the closing stages of the negotiations on coverage of the 1994 WTO GPA, the EEA members, including the prospective members of the European Union, submitted schedules identical to those of the European Union.

The second major set of EU bilateral agreements that affected PP were the Europe Agreements (EAs) concluded with the Central and East European countries (CEECs) in the early 1990s. Prior to the EAs some of the CEECs had introduced elements of a coherent procurement policy. For example, Poland had a central PP office, required notification of all contracts above a (fairly low) threshold and provided for a bid challenge/review of contract award decisions. But in Poland, as in most countries, these reasonably transparent procurement rules did not reach far beyond central government and public enterprises were not covered. Article 67 of the EA with Poland offered non-reciprocal access to EU PP markets, whilst granting Poland a 10-year transition period. This meant that *de jure* preferences granted to domestic suppliers in Polish procurement (a 20 per cent price preference and a 50 per cent origin rule) were to be phased out over this period. Significant EU technical assistance was then channelled into training procurement officials in the CEECs, because this

was identified early on as a major constraint on the development of a professional, competition-based procurement regime.

The EAs therefore promoted reform in PP practices that had already begun in the CEECs, and EU technical collaboration helped speed up the process. Without the top-down pressure from the EAs it is unlikely that reform would have made significant progress (Feldmann, 2003). The EAs began a process of reform and approximation to EU norms that was confirmed with the accession process for the CEECs to the European Union. These bilateral agreements promoted plurilateral rules in the sense that all CEEC accession states were obliged to sign up to the commitments in the 1996 GPA as a condition of EU membership.

The North American approach

US bilateral agreements in the 1985–1995 period

The United States concluded three major agreements during the 1985–1995 period, with Israel, Canada and Mexico in NAFTA. In the case of Israel, a signatory to the 1979 GPA, the provisions essentially confirmed commitments under the GPA. In the case of the CUSFTA there are clear signs of synergy between the bilateral and plurilateral/multilateral negotiations on the GPA. The provisions on PP in the CUSFTA (chap. 13) built explicitly on the 1979 GPA, with the procedural rules set out in the GPA replicated in the CUSFTA (Government of Canada, 1989).

The CUSFTA did not go much beyond the 1979 GPA because of the asymmetry in the size of the US and Canadian markets. So NAFTA coverage in this regard is more extensive. With a US central government procurement market 10 times the size of Canada's, the United States was not willing to extend US schedules much beyond those of the 1979 GPA. Coverage was also limited by the opposition of subfederal governments in both countries to the inclusion of their procurement. Only by lowering the threshold for supplies and services to US\$25,000, compared to 150,000 SDRs for the GATT and EC regimes, did the CUSFTA go beyond the GPA (Hart and Sauvé, 1997).

In line with the 1979 GPA, the CUSFTA required national treatment and thus prohibited *de jure* preferences. Contract award criteria had to be based on the bid that best met the requirements detailed in the tender documentation, which must be clearly specified in advance. The contract award procedure also had to promote competition and be free of any form of preference for national goods or suppliers. Bid challenge was the one area in which the CUSFTA went considerably further than the 1979 GPA. This reflected US domestic practice and required, among

other things, that each party establish an independent review authority to consider bid challenges. The respective authorities were given powers to suspend contract award procedures and terminate the contract, except in the case of urgency or “where delay is prejudicial to the public interest”.

With regard to the issue of reciprocity, an origin test was included in the CUSFTA according to which only “eligible goods” shall be accorded national treatment in all measures concerning government procurement (art. 1305). Eligible goods were defined (art. 1309) as those manufactured in the territory of either party “if the costs of the goods originating outside the territories of the Parties and used in such materials is less than 50% of the cost of all goods used in such materials”. Unlike the European Union, therefore, the CUSFTA applied an origin test for central government purchasing of goods.

A comparison of the CUSFTA and the EU provisions shows large areas of similarity, especially with regard to the general approach and structure of the agreements. The EU’s SEM initiative, however, took coverage in the European Union well beyond anything in the CUSFTA and the GPA during the period; the 1994 GPA redressed the difference somewhat. In terms of compliance, there was also a greater emphasis in the European Union on the role of governments and the European Commission to enforce the rules, compared to the emphasis in the CUSFTA on private actions. This was reflected in the procedural and information requirements of the two approaches.

The North American Free Trade Agreement

NAFTA essentially adopted the CUSFTA rules, but went further on coverage, was more detailed and contained provisions to accommodate the less developed Mexico. Coverage of NAFTA was greater than that of the CUSFTA in large part because of developments in the plurilateral negotiations in Geneva. The active phase of negotiations of the revised GPA in the Uruguay Round occurred after 1990, in other words after the European Union had most of its domestic regime in place. By 1992 it was clear that works and services, subcentral government and public enterprises were going to be included in the revised GPA. NAFTA negotiators appear to have followed these developments and extended NAFTA coverage to match the plurilateral developments. Thus NAFTA coverage was extended beyond the CUSFTA to include the subcentral government level, services and public enterprise.

The NAFTA rules also emulated the emerging GPA rules (which were in turn shaped by the European Union) with respect to thresholds for public enterprises, which were set at the same level as the European Union (\$250,000 for goods and services and \$8 million for construction/

works). The final thresholds in the 1994 WTO GPA were set somewhat higher at 400,000 SDRs for “other entities”, including public enterprise. NAFTA, however, drew a clear line between public enterprise, which was covered, and private enterprise, which was not, even when the latter benefited from special and exclusive rights. So in this respect it reflected the less comprehensive approach that one generally finds in NAFTA.

The threshold for central government procurement of supplies was set at \$50,000, higher than the \$25,000 for the CUSFTA, in order to accommodate Mexico. The threshold for works was set at \$6.5 million in line with EU rules and the 5 million SDRs that had been proposed in the GPA negotiations in Geneva. So here again is evidence of quite close synergy between the NAFTA and GPA negotiations (Hart and Suave, 1997).

There were further transitional measures for Mexico to reflect its less developed status, such as the exclusion of Pemex (the Mexican oil major), a general “set-aside” for Mexican suppliers of around \$1 billion up to 2003 and Mexico was permitted local content requirements of 40 per cent for labour-intensive contracts and 25 per cent for capital-intensive contracts.

NAFTA provisions on tendering procedures were essentially the same as the GPA, but those on transparency slightly more detailed. As NAFTA makes it possible to choose between open, selective and limited tendering, as in the European Union, there remains potential scope for purchasing entities to use this flexibility to retain existing suppliers. Thus limited tendering with selected tenders is possible when there is a need for network operators to maintain the compatibility of equipment used in the network. This provides an important *de facto* regulatory safeguard.

NAFTA requires international standards to be used in preference to firm-specific or national standards “where appropriate”, which is similar to the GPA. In contrast to the European Union, which has made significant efforts to promote agreed international standards, NAFTA simply relies on language preferring performance over design standards.¹³ This reflects the general North American aversion to what are seen as “bureaucratically” determined international standards in preference to industry or market-driven standards.

The criteria for awarding contracts follow other agreements in providing for flexibility so that the lowest tender or that “determined to be the most advantageous” can be chosen. In determining the most advantageous tender the purchasing entity can consider a broad range of non-price issues. As in the European Community and the GPA, there is also a public-interest override (art. 1015) that qualifies price and other economic criteria. Here, then, is another element of “regulatory safeguard”, as discussed in the analytical framework (tables 5.2 and 5.3).

The CUSFTA model of “bid challenge” was also extended to NAFTA

so that each country is required to establish an independent review body with common remedies for non-compliance, such as the suspension of bids and cancellation of a contract once awarded, under national law. But NAFTA (art. 1022), in common with the CUSFTA and the European Union, contains a general public-interest override of contract cancellation. This is another form of regulatory safeguard and is envisaged for those cases in which contract suspension would result in unacceptable costs – as, for example, when a bridge is left half built.

There are no reciprocity provisions in the NAFTA rules on procurement, but there is a substantial “origin” test for third-country suppliers of *services* in article 1005, which states that “a Party may deny to an enterprise that is a supplier of *services* of another Party the benefits of [the procurement chapter] if: (a) nationals of any non-Party *own or control* that enterprise; and (b) that enterprise has *no substantial* business activities in the territory of the Party under whose laws it is constituted”. This “origin” rule applies to services only. The 1979 GPA prohibited such origin rules for supplies (goods). NAFTA, as with the CUSFTA, required a renegotiation of the agreement in the light of the outcome of the multi-lateral negotiations.

Australian-New Zealand Closer Economic Cooperation

Not all progress in procurement rules has been linked to the GPA. Australia and New Zealand opted not to sign the 1979 GPA, but still made progress towards reducing national preferences. In the mid-1980s the Australian states agreed to the National Preference Agreement (NPA), under which they agreed not to apply preferences against each other. As part of the review of the CER (Australian-New Zealand Closer Economic Cooperation) in 1991, New Zealand pressed for – and was successful in gaining – inclusion in the renamed CER Government Purchasing Agreement (CER-GPA). As neither Australia nor New Zealand had signed the 1979 GPA they still maintained preferences in procurement against third countries. New Zealand and Australia had refused to sign the GPA on the grounds that the compliance costs were too high and they pursued a competition-based procurement policy anyway (Walker, 1997; Hoekman and Mavroidis, 1997).

Negotiations during the Uruguay Round

When discussions on a revision of the GATT GPA began in the Informal Working Group on Government Procurement in 1985, the objective was

fourfold: strengthened procedures; increased entity coverage; improved enforcement; and more signatories to the agreement, including more developing and middle-income countries.¹⁴ The negotiations, which continued right through to 1993–1994, were more or less successful in the first objective, although little really changed in terms of the rules for procurement. Increased entity coverage was achieved, but at the expense of a very complex and opaque set of schedules. Improved enforcement was achieved in the bid-challenge rules, unique in GATT, that provide for private companies to challenge contract award decisions taken by governments. But the negotiations failed to get more countries to accept the GPA rules. As will be argued below, regional and bilateral agreements have been subsequently more successful in this aim.

Work on the GPA began in earnest in late 1988 after the CUSFTA procurement rules had been agreed, and at the time the European Union was concluding its new directives. Consequently the US and EU proposals for the GPA closely reflected the status of the respective regional initiatives. The CUSFTA had been agreed in 1988 and provided the basis for US and Canadian proposals for the GPA, and in particular the inclusion of bid-challenge provisions.

The EU's action plan to create a single market in public procurement was tabled in 1986. This consisted of seven directives covering revisions of the existing supplies and works directives, stronger compliance rules and the inclusion of utilities and services. It was not until 1988, however, when the EU's position on the key utilities sector was clear, that negotiations could begin in earnest in GATT. The modalities used for the negotiations were to divide entity coverage into three groups: central government (category I), regional, state and local government (category II) and other entities including public enterprises (category III). But the European Union had still not sorted out the scope of its internal regime and the member states had not signed off the EU rules for utilities, so serious negotiations on extending coverage of the GPA had to await progress in the European Union.

Agreement was reached without much difficulty on stronger wording for procurement of supplies and works. After 1989, when the European Union adopted its directive on compliance introducing bid challenges, there was little difficulty finding an agreement that incorporated this and the US proposals, which were word for word the bid-challenge rules adopted in the CUSFTA.

Negotiations on coverage began seriously in 1990. This was again facilitated by the adoption of a common position on utilities in the EU Council of Ministers (a common position is a political agreement at the level of ministers). This was followed by the formal directive (Proposal for a Directive, COM(90) 297, July 1990). The proposals included the

so-called third-country provision (reciprocity), which provided for a 3 per cent price preference for EU suppliers and a 50 per cent origin rule.¹⁵ This provision was supported by France, Italy and the European Parliament, but opposed by Germany and Britain. In order to resolve the deadlock within the European Union, it was agreed that the Commission would produce a report on progress in the GATT GPA negotiations before deciding what use if any to make of the third-country rules when the directive was implemented in January 1993 (Woolcock, Hodges and Schreiber, 1991: 38).

The rules element of the GPA was more or less settled by 1991, when the chair of the GPA negotiating group produced a draft for inclusion in the so-called draft final agreement of December 1991. But the issue of coverage remained contentious. The United States withheld any commitment on categories II and III until the European Union decided what to do about its third-country rules, which the United States saw as a means of again denying market access for US electrical and telecommunications equipment. On implementation of the EU Utilities Directive in 1993, bilateral negotiations resulted in a US-EU memorandum of understanding on the treatment of US electrical equipment exports to the European Union that effectively waived the use of the third-country provision for this sector. These bilateral negotiations illustrated how increased entity coverage of the GPA had come at the expense of a still greater emphasis on reciprocity in the schedules determining coverage. This, along with the general complexity of the rules, resulted in developing countries and some developed countries deciding not to sign the GPA. As a result, unlike other rule-making aspects of the Uruguay Round, PP remained a plurilateral agreement excluded from the single undertaking. Even some countries which signed the Tokyo Round code on procurement, such as India and Hong Kong, opted not to sign the 1994 GPA.

Coverage

The 1994 GPA therefore extended the areas covered by the agreement, but at the cost of a complex set of schedules and thresholds. Central government purchasing was extended to include works (construction) and services as well as supplies (i.e. goods), with negative listing used for works but positive listing for services! This mix of negative and positive listing reflects the fact that multilateral rules on services in GATS used positive listing. Coverage of subcentral government was new, but not comprehensive; for example, only 37 US states agreed to be covered and local government still remained outside the agreement. Public enterprises in category III were also covered for the first time, but here sensitivities resulted in different and higher thresholds.

Basic elements of the agreement

The principles of the 1994 agreement are common to the 1979 GPA and the major RTA provisions; namely national treatment and non-discrimination for covered purchasing. The 1994 GPA reflects the globalization of production by prohibiting discrimination based “on the degree of foreign affiliation or ownership” or country of production.

The GPA strengthens the transparency requirements concerning contract award procedure by, for example, requiring information on why a bid was unsuccessful. As in the 1979 GPA, open, restricted, single and negotiated tendering are all possible under the agreement provided detailed procedural obligations aimed at ensuring fair and open competition are used. Contract award criteria are the lowest cost or the “most advantageous” bid, which still provides considerable scope for discretionary interpretations of what is advantageous. Another area in which the 1994 GPA provides scope for discretion is in its provisions on technical specifications. These continue to be based on the view that international standards are encouraged, as are performance standards, but that any type of specification can be used when the international standards are not “appropriate”.

The 1994 GPA was a major advance on the 1979 agreement in its compliance rules. As noted above, these were based on the regional models introduced in North America and Europe, and open bid-challenge procedures to aggrieved companies that must provide for independent review of decisions and offer agreed remedies, including contract suspension (with the public-interest opt-out used in the European Union and NAFTA) and damages, which may be punitive or limited to the costs of bidding.

Conclusions on the interaction during the 1985–1995 period

It has been shown that the earlier period of rule-making was shaped by the OECD, where rules were developed that then found application in both the GPA and the EU regional initiatives of the 1970s. During the period of the Uruguay Round most of the impetus in rule-making came at the regional level. The advances in the EU regime facilitated wider entity coverage of the plurilateral rules. The CUSFTA and EU rule-making took the 1979 GPA as a starting point but developed rules further, in particular in the area of bid challenge. As both North American and EU regional approaches and the GPA built on the common OECD norms, all were broadly compatible. This was also helped by the fact that the GPA was to a large extent a transatlantic exercise. Compatibility of the EU

and NAFTA rules was enhanced by the synergy between the regional and plurilateral GPA (i.e. GATT) rule-making. Rules were being developed at both levels at the same time. Progress in the GPA fed back into regional rule-making, and regional rule-making was kept in conformity with the GPA rules. This synergy between regional and plurilateral rule-making produced stronger, more credible rules that promoted effective transparency, rule enforcement and more competitive procurement markets. The regional rules removed *de jure* preferences and eroded *de facto* national preferences, without replacing these with regional preferences. Although the European Union introduced a *de facto* regional preference in its third-country rules on utilities, this appears to have been used more to gain negotiating leverage to ensure extension of the GPA to subfederal entities in the United States than as a permanent preference. Tackling the *de facto* preferences and increasing transparency and competition benefited the economies concerned, but did not bring about a massive increase in import penetration (Evenett and Hoekman, 2004).

This all suggests a positive synergy between the regional and plurilateral negotiations with regard to the rules themselves (Blank and Marceau, 1997; Delsaux, 1997). On coverage the picture is mixed. The EU initiatives facilitated wider coverage, but could also be said to have represented a brake on wider agreement. Regional initiatives also did little to temper complex bilateral negotiations on the coverage of categories II and III that are likely to have trade-diversionary effects.

Regional initiatives in the post–Uruguay Round period

Initiatives at the regional level during the post–Uruguay Round period appear to have had less to do with developing the rules than with extending the number of countries signing up to the 1994 GPA or GPA-type rules. Looking first at the EU-centred RTAs, the eastern enlargement of the European Union effectively added 10 signatories to the GPA, since all accession states to the European Union had to sign the GPA (OECD, 2002b).

In terms of EU RTAs with non-accession states, the EU–Mexico agreement of 2000 (implementing the EU–Mexico cooperation agreement) was the first EU bilateral agreement with non-accession states to include substantial provisions on PP (table 5.2). With regard to coverage the EU–Mexico agreement is essentially the same of the 1994 GPA, including central and some state-level government with the same thresholds. Mexico is not a signatory to the GPA. The agreement includes the principle of national treatment, which precludes explicit use of national prefer-

ences. Transparency provisions are detailed and equivalent to those in the 1994 GPA, although the requirements to gather statistics on contracts awarded may be more extensive.

Interestingly, when it comes to detailed provisions for advertising and awarding contracts Mexico uses the NAFTA text and the European Union uses the GPA text, which illustrates how close are the EU and NAFTA rules. The EU-Mexico agreement has a bid-challenge procedure including independent reviews, rapid interim decisions and contract suspension (but not contract termination as in NAFTA). Finally, the EU-Mexico agreement establishes the Special Committee on Government Procurement to promote mutual understanding of procurement procedures. This committee also has the aim of promoting technical cooperation and expertise in purchasing procedures.

The EU-Chile FTA provisions on procurement are interesting in that Chile had been consistent in its criticism of the 1994 GPA as being unduly complicated and costly to implement. For this reason Chile, despite its liberal trade policies, refused to sign the GPA. But the EU-Chile FTA, along with the US-Chile FTA, have the effect of bringing Chile into the fold of the GPA, illustrating how bilateral agreements can result in a strengthening of the existing GPA.

Other EU FTAs with developing countries do not have extensive rules on procurement. The Euro-Med agreements, for example the EU-Morocco agreement, contain only the objective of “a reciprocal and gradual liberalisation of public procurement contracts” (art. 41) to be achieved through “necessary steps” (*EU Official Journal* L 70/2, 18 March 2000). But there is no specific timetable nor concrete provisions. Likewise the EU-Algeria agreement has as its objective the “reciprocal and gradual liberalisation of public contracts” (art. 46), but no reference to any concrete measures to achieve this aim. Even the EU-South Africa agreement (the Trade, Development and Cooperation Agreement of 1999), which is in other respects more developed than the Euro-Med agreements, only has a general provision (art. 45) calling on the parties “to cooperate to ensure that access to Parties procurement contracts is governed by a system which is fair, equitable and transparent”.

The US bilateral initiatives post-1994 have had a similar effect in promoting more signatories to the GPA. As table 5.3 shows, the US bilateral agreements have effectively extended the GPA disciplines to Chile, Australia, which had previously not signed the GPA, and even Morocco, which given its developing country status is rather surprising. The US-Morocco FTA goes far beyond anything that has been included in the Euro-Med agreements. The US-Singapore agreement has little substance on procurement because both parties are signatories to the GPA, so the bilateral agreement simply refers to existing GPA obligations. In general,

as tables 5.2 and 5.3 show, the US and to a lesser degree the EU FTAs are effectively extending membership of the GPA to FTA partners. This strategic interaction does not pose a threat to the multilateral system because the EU and US approaches are very similar. But the FTAs appear to have obliged more countries to sign up to GPA-type commitments than would otherwise have been the case.

Issues in the multilateral negotiations

A Working Group on Transparency in Government Procurement (WGTGP) was established after the Singapore WTO Ministerial. Opposition to market access in procurement (defined as the removal of preferences for national suppliers) from developing countries was the reason for talks on “transparency” (WTO, 2001). But the lack of any clear distinction between market access and transparency made the work of the WGTGP difficult.¹⁶ Many of the measures needed to “liberalize” government procurement are in fact to do with transparency or good regulatory practice.

The issues identified by the WGTGP were very similar to those covered by the GPA and RTAs (Evenett, 2003: 35–42).¹⁷ There were, in addition, questions concerning dispute settlement in the field of PP under the WTO, technical assistance and special and differential treatment for developing countries.

In terms of coverage the United States and the European Union argued that transparency rules should apply to all procurement because of the general economic efficiency gains from more open and transparent purchasing.¹⁸ The (developing country) WTO members seeking to restrict coverage argued that transparency rules should only apply to procurements “open to competition”; in other words those covered by schedules and being above set thresholds in any agreement. The dominant view in the WGTGP favoured limiting transparency rules to central government, with many countries pointing to the impracticability and costs of extending transparency rules to cover state or local government.

The WGTGP reflected a broad consensus on a continued use of flexibility in contract award procedures, such as the use of open, restrictive and negotiated contracts, but differences over the degree of detail needed to ensure transparency in the use of these procedures. The WTO members seeking an expansive approach (i.e. the European Union and the United States) argued that information was needed on a long list of things: contract details, contact points, delivery details for the bids, information on the type of contract award procedure (open, restricted or negotiated), the criteria for selection of bids, information on any existing

preferences for national producers or categories of producers, technical specifications, the timetable for completion of the contract, etc. Other WTO members found such a long list burdensome and argued for more national discretion on what to include in transparency rules. One sensitive issue was whether there should be transparency for existing *de jure* preferences. Potential suppliers should arguably know if they are facing a preference, but publication of such discrimination could also provide a focus for pressure for the removal of such distortions. Another issue was whether there should be information on why bids had not been accepted or debriefing for unsuccessful bidders. Again, the issue of compliance costs was raised by developing countries.

Implementation and enforcement were also discussed. WTO members accustomed to bid challenge and access to reviews in GPA or regional rules argued that these were essential if the rules were to work. The United States in particular argued that all WTO rules, including transparency rules, should be covered by the DSU (Dispute Settlement Understanding). Non-signatories to the GPA argued that such enforcement provisions were only relevant for rules on market access, and that maintaining the institutions necessary to offer an independent review of transparency in procurement was excessive.

Finally, the WGTGP discussed forms of special and differential treatment for developing countries, such as a development exemption from the rules¹⁹ and higher thresholds in terms of coverage for developing countries. The developed countries also offered technical assistance in drafting procurement laws and implementing the transparency rules.

Results of the work in the WGTGP

The work of the WGTGP produced some valuable material and there appears to be a consensus on the value of transparency in government procurement (Minutes of the Meeting of WGTGP, 13 June 2003). But differences remained that precluded a consensus prior to the Cancun Ministerial. The EU view was that the case for transparency had been accepted by all, reiterating that developing countries would still be able to retain (*de jure*) preferences. The European Union further argued that many countries already had forms of transparency in place, so the costs would not be insurmountable. Compliance costs could be reduced by the use of thresholds, and technical assistance would be forthcoming.

The developing countries did not accept the view that an agreement on the “modalities” for negotiation on procurement was imminent. Brazil argued that all accepted that transparency in PP was a good thing, but the case for a WTO agreement on transparency had not yet been made. India argued that it was not yet (in 2003) time to enter negotiations as it

still remained unclear what the scope of any agreement on transparency would be.

Conclusions

This case study clearly shows how the different levels of rule-making interact over time.

Rules developed in OECD discussions in the 1960s and early 1970s provided the model for regional and plurilateral agreements on procurement during the 1970s. But limited progress in the European Union held back advances in GATT. When the EU's single market programme gained a new impetus in the 1980s this also facilitated progress in the GATT negotiations. Developments in the CUSFTA helped shape the GATT rules. The concomitant rule-making at regional and multilateral levels in the period 1986–1994 and the intense EU-US negotiations helped ensure “synergistic” interaction between the levels.

In the post-1994 period RTAs and bilateral agreements appear to have been used more “strategically” to extend the effective membership of the GPA. Through bilateral agreements with the European Union and the United States, countries that declined to sign the 1994 GPA have in effect accepted provisions equivalent to the GPA rules in these bilateral agreements. This is the case for Mexico, Chile and a number of other developing countries as well as Australia, through its FTA with the United States. Most North-South RTAs typically include GPA-type rules on procurement. Multilateral negotiations were initiated on transparency in PP and there appeared to be some areas of consensus on the possible shape of such rules. But if there is no progress at the multilateral level, it seems likely that RTAs will continue to provide an alternative route to the establishment of rules in this policy area.

The chapter suggests some scope for policies that would ensure compatibility between the levels of rule-making. For example, transparency rules could be established at the multilateral level, but without detailed review and bid-challenge provisions. RTAs could then include obligations on signatories on these topics, thus effectively enforcing agreed multilateral rules.

Notes

1. The United States was the main protagonist in favour of including provisions on “government procurement” because it saw this as a means of addressing the distortions to trade that resulted from the greater role of government and the public sector in Europe and other developed economies.

2. The 1979 GATT Government Procurement Agreement (GPA) was only signed by a limited number of countries. It could therefore be described as plurilateral rather than multilateral. The same remains the case with the 1994 WTO GPA.
3. There is an interesting question as to whether price preferences that discriminate between classes of suppliers may not be inconsistent with national treatment. For example, preferences for companies that agree to create x new jobs as a result of winning a contract could be applied to all suppliers regardless of their nationality and therefore be consistent with national treatment.
4. This characteristic of PP is of course common to most non-trade barriers, and is a feature of all of the cases discussed in this chapter to some degree.
5. The process of creating the Single European Market was, however, associated with structural changes in the major sectors supplying PP markets. This resulted in the national identity of suppliers becoming blurred as a result of cross-border rationalization. Thus national PP markets are supplied by the local subsidiary of what are often pan-European or international companies. As a result there are more open markets for procurement, but these markets are not supplied by non-national suppliers.
6. The US government was pressed by the US electrical equipment sector because the US market, which was made up of more than 1,000 purchasing entities, was less centralized and more open than the European markets that were dominated by centralized procurement of nationalized utilities which saw procurement as a means of promoting their national equipment industries. In the late 1960s European suppliers with massive surplus capacity supplied 50 per cent of the US market (with most purchasing decisions made at the municipal level). Foreign penetration of the British, French, Italian and German markets was zero (Epstein, 1971: 119).
7. It was only with the adoption of the Tokyo Round Code on Government Procurement in 1979 that the issue of EC competence in procurement negotiations with third countries was sorted out (Bourgeois, 1982).
8. The original agreement negotiated during the Tokyo Round of GATT and concluded in 1979 provided for 150,000 SDRs, but this threshold was reduced in 1988.
9. See for example Directive on Public Supply Contracts, L 13/4, of 15 January 1977.
10. See for example Frignani (1986: 567), who reports on survey evidence carried out by the International Chamber of Commerce that showed the GPA had had little effect.
11. See Bulletin of the European Communities Supplement 6/88 for information on the draft directives.
12. For the texts of the various EC directives see European Commission (1994).
13. There have been some selective efforts to promote standards in sectors such as telecommunications and transport.
14. PP was not formally part of the Uruguay Round so this work took place under the auspices of the 1979 GPA, which provided for revisions. In practice the negotiations on procurement were linked to the wider multilateral negotiations.
15. Purchasing entities could deny suppliers rights under the directive if the products supplied were not of at least 50 per cent EU origin.
16. See Reports of the Working Group on Transparency in Government Procurement, especially WT/WGTGP/W/03, 3 October 2002.
17. The work in the WGTGP was also informed by the experience with the World Bank guidelines on procurement for IBRD projects (World Bank, 1995) and the UNCITRAL model law on procurement (UNCITRAL, 1992). The UNCITRAL model law on procurement of goods and construction promotes, voluntarily, an approach that is broadly in line with the GPA-type procedures in terms of its emphasis on transparency and the provision for domestic reviews, for example. But the UNCITRAL model law allows for *de jure* discrimination, for example on development grounds, and proposes much more

discretion in the hands of national purchasers (Evenett, 2003: 27–31). As such it offers a model preferred by many developing countries to that of the European Union or NAFTA.

18. For an analysis of the issues involved see Arrowsmith (1997).
19. The scope of the security exemption under the GPA has not been tested. There was some discussion of whether the European Union should challenge US contracts for re-construction in Iraq on the grounds that these excluded signatories to the GPA (such as France and Germany) which had not supported the US action in Iraq, but the European Union chose to avoid confrontation for obvious reasons.

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Assessing the interaction between levels of rule-making: Trade in telecommunications services

Heidi Ullrich

Introduction

Since the 1980s international trade in services, including telecommunications, financial services, transport and tourism, has been an essential component of the global economy. Growth of global exports of commercial services surged from \$400 billion in 1980 to approximately \$2,125 billion in 2004, with an 18 per cent annual increase between 2003 and 2004 (WTO, 2005; UNCTAD, 2003).

In particular, the telecommunications services sector has experienced a “benign revolution” due in part to rapid developments in digital technology, privatization and domestic deregulation (Cowhey and Klimenko, 2001: 62). The telecommunications services sector is not only crucial in the delivery of other services, but also facilitates trade in goods. Given this dual function, telecommunications services play an important role in economic growth in both developed and developing countries.

Telecommunications services may be divided into basic services consisting of such traditional telecoms services as voice telephone and facsimile, and value-added, or enhanced, services such as data networking, e-mail and voice-mail. Basic telecommunications services, and the infrastructure required for their supply, historically operated in a heavily regulated environment dominated by monopolies. In contrast to basic telecommunications services that are generally supplied through analogue technology, the value-added telecommunications services that emerged in the late 1970s use digital technology. Thus suppliers of value-added

telecommunications services were able to benefit from operating outside the regulated environment, although they faced high prices on the leased infrastructure required for their supply (Lang, 1996).

However, regulatory reform of the telecommunications services sector in the United States, resulting in the 1984 break-up of AT&T, technological advances and the increasingly global nature of telecommunications services suppliers spurred international reconsideration of the role of competition in this sector. To address the changing regulatory, technological and economic demands of the telecommunications services sector, beginning in the mid-1980s progress in rule-making and liberalization in trade in telecommunications services occurred at multiple levels. This included negotiations at the bilateral and regional levels within various regional trade agreements (RTAs), the plurilateral level of the Organization for Economic Cooperation and Development (OECD) and the multilateral level through the General Agreement on Trade in Services (GATS) that was negotiated within the General Agreement on Tariffs and Trade (GATT) Uruguay Round between 1986 and 1994. The GATS framework agreement in 1994 was also later followed by plurilateral negotiations within the WTO on basic telecommunications services. Additional rule-making and liberalization of the telecommunications services sector remain key objectives within negotiations under GATS within the Doha Round and an increasing number of RTAs.

Assessing the interaction between multiple levels of rule-making

Analogous to the growth and transformation of the services sector, recent RTAs have shown extensive change in terms of numbers, membership, geographical reach and scope compared to earlier bilateral and regional trade agreements as the multilateral trading system has become increasingly complex. Such developments bring a new dynamism to the debate on the role RTAs play in the global trading system. Rather than seeing such arrangements as either stepping-stones or stumbling blocks for the multilateral system, attention is increasingly shifting on to the interaction between the bilateral, regional, plurilateral and multilateral levels.

This chapter argues that the process of rule-making and liberalization in services, specifically telecommunications services, may be characterized as being iterative in nature, consisting of synergistic activity at multiple levels. This iterative nature is due to rapid technological, economic and regulatory developments outpacing multilateral negotiating rounds

under both GATT and the World Trade Organization (WTO). The increasing development of rule-making and liberalization of trade in telecommunications services at the bilateral, regional, plurilateral and multilateral levels necessitates an assessment of the interaction occurring between these multiple levels.

Through an analysis of the interaction of selected bilateral, regional and multilateral agreements, this chapter assesses the iteration that has occurred within trade in services with a focus on the telecommunications services sector. The assessment consists of four elements. First, there is an examination of the provisions relating to rule-making in telecommunications services within various bilateral, regional, plurilateral and multilateral agreements. Agreements have been chosen to reflect a broad geographical range and a balance of developed and developing country activity, to incorporate diverse approaches and priorities of RTAs and to determine the extent to which regulatory regionalism may be said to exist. Second, there is an evaluation of the systemic impact of RTAs on the evolution of international rules in telecommunications. To what extent is the interaction between RTAs and GATS characterized by iteration?¹ The example of the 1996 WTO Telecommunications Reference Paper is used to examine the degree to which more recent RTAs have been significantly GATS-plus. Third, there is an investigation of governance issues, such as whether RTAs offer greater institution-building, accountability and transparency than multilateral agreements. Finally, there are conclusions on the value of assessing the interaction between multiple levels of rule-making in the services and telecommunications sectors.

Early agreements on trade in services

The need to ensure interoperability and create common standards in services has long necessitated various international agreements in individual sectors. In telecommunications, numerous bilateral and regional agreements were negotiated within the International Telegraph Union during the latter half of the nineteenth century to ensure interoperability of telegraph networks. Its successor, the International Telecommunications Union (ITU), is primarily a technical organization that sets and supervises common technical standards and regulations in international telecommunications. But trade-related agreements in telecommunications were not part of the ITU's *modus operandi*, so negotiations on liberalization and rule-making in telecommunications services were incorporated into the broader debate on trade in services.

The plurilateral level

Initial plurilateral efforts to address the trade in specific service sectors occurred in the early 1960s within the OECD, with voluntary codes on liberalization of capital movements and current invisible operations. These codes incorporated such features as a negative list of reservations as well as holding periodic meetings aimed at progressive reduction of existing barriers to trade, barriers that were to be the subject of later services trade negotiations.²

In 1973 the OECD published the influential *Report by the High Level Group on Trade and Related Problems* (OECD, 1973) that was drawn up as part of the preparation for the GATT Tokyo Round negotiated between 1973 and 1979. This report, known as the Rey Report after the group's leader, the former European Commission President Jean Rey, recommended that developed countries should work together within the OECD to develop ways to ensure the liberalization and non-discrimination of the services sector, while allowing for future inclusion of developing countries (Feketekuty, 1988: 298–299).

Services were only marginally covered in three Tokyo Round codes, but individual US government officials, business leaders and business coalitions (such as the US Coalition of Services Industries, the US Council for International Business and the British Liberalisation of Trade in Services (LOTIS) group) worked to get services on the trade agenda.³ By the early 1980s the US-led efforts had gained sufficient support from other developed countries for the Trade Directorate of the OECD to carry out a wide-ranging conceptual study of a possible multilateral framework for trade in services.

During the first half of the 1980s the plurilateral OECD level established definitions, identified existing barriers to trade in services, analysed barriers in specific sectors, including telecommunications, and developed a conceptual framework for trade in services. At the same time, the ongoing technological revolution in network-based data transmission significantly influenced the debate by creating new modes of services delivery and identifying domestic telecommunications regulations as potential non-tariff barriers to trade (Drake and Nicolaidis, 1992: 48).

By the mid-1980s there was growing consensus, particularly within the United States and European Union,⁴ on the need for the liberalization of, and rule-making in, trade in services. While the United States and the European Union worked to gain support among the other contracting parties (CPs) of GATT to negotiate a multilateral framework in trade in services, the iterative nature of rule-making and liberalization was

evident in the progress they made within bilateral and regional trade agreements.

Bilateral and regional trade agreements pre-GATS

The first tangible efforts toward the development of rules for the liberalization of tradable services were made within RTAs. The US-Israel Free Trade Agreement, entering into force in August 1985, included a non-binding declaration on trade in services that called on the parties to eliminate existing barriers to trade in services. Included in the declaration is an early definition of trade in services, described as “when a service is exported from the supplier nation and is imported into the other nation”, accompanied by a list of several service sectors, including communications (art. 1).

The declaration established basic principles covering trade in services that served as precedents for later RTAs and GATS, including market access, national treatment for cross-border trade in services and commercial presence. Commercial presence was, however, still at the discretion of domestic regulatory agencies. The US-Israel FTA included provisions for transparency, due process and consultation, and allowed, among other things, for the continued existence of public monopolies in some services as long as these operate within the provisions of the declaration when doing business in the other country. Finally, as in the Ministerial Decision on Negotiations on Basic Telecommunications attached to GATS and some later RTAs, the parties agreed a time-frame for further negotiations, with the aim of strengthening the declaration through developing binding obligations in specific sectors.

In 1986 Israel and the United States negotiated a series of sectoral annotations in telecommunications, tourism and insurance that detailed how the general provisions were to be interpreted with respect to each sector, such as market access. Notably, the annotation on telecommunications distinguished between major and smaller suppliers of telecommunications services and sought clarification on the definition of basic versus value-added telecommunications services (Feketekuty, 1988: 182–183). These distinctions, and their eventual clarification, provided a model for later agreements and thus contributed to the eventual convergence of conceptual, regulatory and political developments. For example, prior to the GATS Telecommunications Reference Paper, RTAs such as the Canadian-US Free Trade Agreement (CUSFTA) and the North American Free Trade Agreement (NAFTA) were limited to covering value-added telecommunications services.

At the same time as the bilateral US-Israel FTA, progress on telecommunications services liberalization was being made at the regional level of the European Community. The 1985 Cockfield White Paper,⁵ which contributed significantly to the launching of the EC Single European Market programme in 1987, urged that “swift action” towards a common market be taken in both traditional and new services, such as the development of common standards for telecommunications networks (European Commission, 1985: 27).

The Commission’s 1987 green paper on telecommunications (European Commission, 1987) outlined an approach that included a process of gradual liberalization of the telecommunications services and networks by 1 January 1998, including telecommunications equipment and networks and development of common standards. Notably, concepts such as the need for competitive safeguards, interconnection, independent regulators, transparency and allocation of scarce resources addressed in the EC green paper on telecommunications were later incorporated into the WTO’s Telecommunications Reference Paper. (See annex 6.1 for examples of the iterative nature of the EC’s telecommunications services regulatory framework and the WTO’s Telecommunication Services Reference Paper.)

The bilateral CUSFTA, which took effect on 1 January 1989, is widely seen as having contributed useful conceptual elements to GATS as well as serving as a model for the liberalization of trade in services within future RTAs. Hailed as the most extensive agreement between two countries (External Affairs, Canada, 1987), the CUSFTA was the first RTA to include binding commitments in trade in services, including a pledge to eliminate barriers to such trade (art. 102.a). Four chapters of the CUSFTA cover issues related to trade in services, with chapter 14 covering services and chapters 15, 16 and 17 covering temporary entry for business persons, investment and financial services respectively. The services provisions within chapter 14 establish rights and obligations such as national treatment, the establishment of commercial presence for such purposes as distributing, marketing, delivering or facilitating a covered service⁶ and measures covering licensing and certification, including the encouragement of mutual recognition among the parties.

Annex 1408 sets out the service sectors covered by the agreement, including telecommunications network-based enhanced services but not basic telecommunications services, as well as agriculture and forestry, mining, construction, insurance and real estate, commercial services and tourism. The agreement contains individual schedules for both Canada and the United States in which the services to be liberalized are listed. Although these schedules take a positive list approach similar to GATS, direct reference is not yet made to the various modes of trade in services.

Within annex 1404 are three sector annexes covering architecture, tourism and computer services and telecommunications network-based enhanced services. Notably, while the framework of provisions within the chapter on services aims to establish standstill, the sector annexes establish the objective of a roll-back of barriers facing trade in services (Schott and Smith, 1988: 141). The annex on computer services and telecommunications network-based enhanced services sets out rights and obligations covering rights of access to basic telecommunications for enhanced telecommunications services and the resale and sharing of basic telecommunications transport services (art. 3.1:a–b), as well as establishing the parameters for defining commercial presence and investment (arts 3.2 and 3.3). Provisions stating the need for public monopolies to refrain from anti-competitive behaviour and structural separation were included that not only reflected earlier RTAs but would serve as a model for future work at the multilateral level.

In terms of process, the CUSFTA was seen as a means of bring pressure on GATT negotiators to make progress towards a multilateral agreement on trade in services. One of the stated objectives of the CUSFTA was for it to “lay the foundation for further bilateral and multilateral co-operation to expand and enhance the benefits of this Agreement” (art. 102.3).⁷ That the CUSFTA was successful in this respect was made clear by its suspension in December 1992 upon the signing of NAFTA. These bilateral and regional agreements contributed important definitional and conceptual elements to the agreement on trade in services that was simultaneously being planned and negotiated within GATT.

The General Agreement on Trade in Services

Progress toward establishing GATT as the legitimate forum in which to negotiate a possible multilateral agreement on trade in services was made at the 1982 GATT ministerial meeting.⁸ This progress took the form of an agreement between developed and developing countries to prepare national studies of trade in services as a means of deepening the parties’ understanding of the issues (Feketekuty, 1988: 319). Following work by a GATT preparatory committee, in September 1986 trade ministers agreed to launch the Uruguay Round, consisting of parallel negotiations in trade in goods and services.

After eight tortuous years of negotiations, GATS was signed in Marrakesh in April 1994 and went into effect on 1 January 1995 concomitant with the creation of the WTO. GATS embodies an approach to trade in services widely used in trade agreements that includes general and specific obligations for WTO members as well as provisions for future liber-

Table 6.1 Modes of service provision

Mode	Modes of trade in services as defined in GATS	
	Type of service	Description
1	Cross-border supply	The service is supplied from the territory of one member to that of another member (excluding telecommunications, the post)
2	Consumption abroad	Involves the supply of the service in the territory of one member to the consumer of another member (excluding tourism, ship repair)
3	Commercial presence	The supply of a service through the commercial presence of a foreign supplier such as a corporation, branch office or joint venture
4	Presence of natural persons	Involves admitting a national of one member into the territory of another member on a temporary basis for the purpose of providing a service (excluding a foreign employee of a service supplier of one member having a commercial presence in the territory of another or foreign nationals of one member operating as an independent service supplier in the territory of another member)

alization.⁹ Table 6.1 outlines the four modes of trade in services (GATS art. I) that have found wide application, specifically for agreements using a positive list approach.¹⁰

GATS consists of general obligations on most-favoured nation (MFN) treatment (art. II) and transparency measures (art. III),¹¹ but provisions on market access (art. XVI) and national treatment (art. XVII) apply to the specific commitments made by WTO members in their national schedules. Through the use of a hybrid approach,¹² during the Uruguay Round negotiations members identified the specific sectors and modes of supply subject to any of six disciplines on quantitative restrictions as well as those to which the principle of national treatment for “like services or service suppliers” will apply.¹³

Of key importance for any investigation of the interaction between RTAs and the multilateral level of rule-making in services is GATS article V on progressive liberalization. Article V.1(a) requires economic integration agreements to provide “substantial sector coverage”, while

article V.1(b) states that economic integration agreements must provide “for the absence or elimination of substantially all discrimination ... between or among parties”.

In the telecommunications sector, 48¹⁴ scheduled commitments were listed, the majority of which applied to value-added services, while 22 governments incorporated limited commitments on basic telecommunications.¹⁵ Table 6.2 outlines the main provisions within GATS.

Attached to GATS as agreed in April 1994 were eight annexes, including annexes on telecommunications and negotiation on basic telecommunications, as well as eight decisions setting out details on definitions, institutional issues and future sector negotiations, including basic telecommunications.¹⁶ The annex on telecommunications ensured access to and use of infrastructure for use by value-added telecommunications service suppliers. The decision on negotiations in basic telecommunications reflects the recognition by governments, in both developed and developing countries, that greater liberalization and rule-making in telecommunications services and telecommunications transport networks could be made through additional voluntary negotiations.

The primary achievement of GATS as agreed at the end of the Uruguay Round was that it established general obligations and rules under which trade in services would be governed. Although there was a commitment to progressive liberalization of trade in services at the multilateral level, in general the process of rule-making and liberalization under GATS has been partial, with more progress in some sectors than others;¹⁷ limited in terms of transparency, particularly as compared to agreements applying a negative list approach; and gradual. However, it should be noted that in comparison to GATT, which evolved over approximately 50 years, the “GATS framework agreement is very young and has a long way to go”.¹⁸ It is evident that negotiators recognized there was an unfinished agenda in committing to future negotiations on rules, such as emergency safeguards, government procurement, domestic regulation and subsidies, as well as further sectoral and multilateral liberalization negotiations.

Post-Uruguay Round liberalization in basic telecommunications services: The Agreement on Basic Telecommunications and the WTO Reference Paper

As mandated by the Ministerial Decision on Negotiations in Basic Telecommunications, in mid-May 1994 the Negotiating Group on Basic Telecommunications, with 33 participating members, began a series of 15 meetings to clarify which services in the sensitive sector of basic telecom-

Table 6.2 Provisions within GATS

Provision	Article(s)	Description
Coverage	I	Universal, with the exception of most air transport services and services supplied in the exercise of government authority Members apply a hybrid approach to market access, national treatment and additional commitments, in any of the four modes of delivery, for foreign service suppliers
General obligations and specific commitments	II	MFN – with exceptions*
	III	Transparency through notification of all relevant measures of general application
	III(4)	Establishment of enquiry points
	XVII	NT – specific obligations
Substantive provisions	XVI	Market access – specific obligations
		Additional commitments – specific obligations
		Progressive liberalization
	V:1(a)	Requires economic integration agreements to provide “substantial sectoral coverage”
	V:1(b)	Agreements must provide “for the absence or elimination of substantially all discrimination . . . between or among parties”
Other provisions	XIX	Builds in the progressive liberalization of trade in services through periodic negotiations, to begin no later than 1 January 2000, through “bilateral, plurilateral or multilateral negotiations directed towards increasing the general level of specific commitments undertaken by Members”
	VII	Recognition may be achieved through harmonization or otherwise, such as mutual recognition
	VIII	Monopoly service suppliers not to act inconsistent to MFN obligations or abuse their position

Table 6.2 (cont.)

Provision	Article(s)	Description
Cooperation	XXIV	Council for Trade in Services established to facilitate cooperation
	XXV	Subsidiary bodies as needed Technical cooperation for member governments and service providers
	Annex on Telecommunications art. 6	Members to support cooperation among developing countries at international, regional and subregional levels and assist in technology transfer to LDCs
	VI	Domestic regulation – measures administered in impartial manner and disciplines not more burdensome than necessary
Exemptions (collective preferences, safeguards)	XII	Restrictions to safeguard balance of payments
	Telecoms Reference Paper	Governments must take appropriate measures to prevent suppliers of telecommunications services from using anti-competitive practices
Institutionalization	XXII	Consultation and dispute settlement
	XXIII	Dispute settlement and enforcement provisions
Implementation	XXII	State-to-state consultation
	XXV	Technical cooperation

* However, members are able to exempt specific measures and border regions from the principle of equality of treatment (arts II:2–3 and V:1).

munications should be included in the negotiations and to develop further commitments. The number of governments involved increased as the negotiations progressed: by the end of April 1996 53 members were participating, with an additional 24 observing. Despite 34 offers from 48 members (the European Commission makes offers on behalf of the governments of the European Union), no consensus on an overall agreement could be agreed.¹⁹ However, the commitments made were attached to a protocol open to revision in February 1997. Negotiations, with an expanded number of participating governments, continued under the newly formed Group on Basic Communications. On 15 February the Agreement on Basic Telecommunications (ABT) was adopted. The ABT incorporated a broad definition of basic communications that included network-based and resale provisions for services for data transmission,

public voice, internet and satellite, mobile/cellular and paging among others (WTO, 1996). Contained within the ABT were the schedules of specific commitments and a list of exceptions from 69 countries, representing over 91 per cent of the telecommunications markets of WTO members submitting offers (see annex 6.2 for a summary of commitments and exemptions). Following an extended ratification period, the ABT was incorporated into GATS by its Fourth Protocol and entered into force on 5 February 1998.

The ABT is significant for several reasons. Firstly, there is greater scope and depth of liberalization than in GATS, including pro-competitive regulatory disciplines and national treatment commitments covering investment in basic telecommunications. Secondly, the rules ensured greater transparency in basic telecommunications through increased information-sharing requirements, and better enforcement through WTO dispute settlement procedures. Finally, at the national level the incorporation of basic telecommunications into the trade policy arena increased the role of departments of trade, finance and industry in regulatory policy and thus challenged the established telecoms regulators. This broadening of the policy environment has led to a consolidation among groups in favour of liberalization, consisting of political, bureaucratic and industry actors who “have stakes in promoting liberalisation to the benefit of the economy as a whole rather than in protecting the prerogatives of traditional national carriers” (Noam and Drake, 1997).

During the course of the negotiations, a reference paper was used as a means to develop a set of pro-competitive principles on national regulatory regimes.²⁰ The definitions and principles of the WTO Reference Paper, to which the vast majority of governments (57 out of the 69) agreed by the end of the negotiations, are outlined in table 6.3.

The reference paper has been described as the “bible” for telecommunications services,²¹ and credited with bringing about a “change in the international telecommunications regime” (Cowhey and Klimenko, 2001: 7). According to Cowhey and Klimenko, this new regime affected the terms of accession for countries negotiating membership of the WTO, led governments and market actors to favour states that adhered to the principles set out in the reference paper²² and facilitated the growth of new global communications carriers as the rules covered developed and developing country markets.

Due in part to the successful adoption of the ABT and the WTO Reference Paper and in part to the continuing pace of technological advancement and market forces, the post-Uruguay Round period has seen further rule-making and liberalization of the telecommunications services sector in various RTAs.

Table 6.3 WTO Reference Paper: Definitions and principles

Definition/principles	Description
Definition	The reference paper applies rules to “major suppliers” of telecommunications services which have “control over essential facilities” or use their position to “materially affect the terms of participation”
Competitive safeguards	Governments must take appropriate measures to prevent suppliers of telecommunications services from using anti-competitive practices such as cross-subsidization, applying information obtained from competitors in an uncompetitive manner or denying competitors access to relevant technical information
Interconnection	Governments must ensure that major suppliers provide interconnection of their networks to other service suppliers at “any technically feasible point in the network”; major suppliers will offer interconnection that is non-discriminatory, timely and at a rate and quality “no less favourable” than that provided for its own subsidiaries or affiliates
Universal service	Governments may set universal service obligations, as long as they are administered in a transparent, non-discriminatory, competitively neutral manner and are not more burdensome than necessary in reaching their policy objectives
Transparency	Under circumstances where licences are required, the licensing criteria, time-frame and terms and conditions are to be made publicly available; upon the request of the applicant, the reasons for denial of a licence will be made known
Independent regulators	The regulatory body must be separate and not accountable to any supplier of basic telecommunications services, and its procedures must be impartial
Allocation and use of scarce resources	Government procedures for the allocation and use of scarce resources, such as frequencies and numbers, must be objective, timely, transparent and non-discriminatory

Bilateral and regional agreements post-GATS

Empirical evidence suggests that the interaction between the multiple levels of rule-making in telecommunications services has been largely

iterative, with each level applying broadly similar approaches and objectives. The WTO Reference Paper has been used as just that in the RTAs that followed its adoption, with its pro-competitive principles being largely transferred, and in some cases enhanced, in subsequent bilateral and regional agreements. The more recent US bilateral (i.e. US-Australia, US-Singapore) and regional agreements (CAFTA-DR) have built on the reference paper by incorporating provisions on unbundling of network elements and co-locations. In addition, some of the more recent RTAs covered in this analysis are GATS-plus in their coverage in that they apply a negative list approach that delves deeper into domestic regulatory regimes.²³

In general, however, the RTAs have not liberalized deeper and faster than in the multilateral regime, including in basic telecommunications. An OECD study prepared by Sauvé concluded that “in some instances ... (e.g. non-discriminatory quantitative restrictions, domestic regulation), GATS disciplines go further than those found in a number of RTAs” (Sauvé, 2003: 24) and “in the key infrastructural areas of basic telecommunications and financial services, the GATS has in fact achieved a higher level of bound liberalization than that on offer in most RTAs” (Sauvé, 2003: 26). This is in sharp contrast to some other case studies covered in this volume, such as such as intellectual property rights, where RTAs have been for the most part TRIPS-plus (see chap. 7).

The RTAs investigated for this study can be divided into four groups: pre-reference paper US-driven (i.e. NAFTA); Latin American RTAs (i.e. MERCOSUR and the Andean Community); EU-driven RTAs (i.e. Euro-Med agreements and the EU-Chile Association Agreement); and post-reference paper US-driven FTAs (i.e. CAFTA-DR and US-Singapore). The following section explores the context, approach and scope of selected RTAs with respect to trade in telecommunications services. Where appropriate, differences between the US-centred and EU-centred approaches are highlighted. An initial attempt is made at evaluating the interaction between RTAs and the development of multilateral rules in telecommunications services.

Pre-reference paper US-driven

NAFTA

Even before it entered into force NAFTA had a significant influence,²⁴ in that it brought pressure to bear on negotiators in Geneva to conclude GATS. After its entry into force in January 1994 it provided a model for

the liberalization of tradable services. Evidence of the wider influence of NAFTA can particularly be seen in the Western hemisphere: in 2003 more than 85 per cent of the trade in services between the countries in the Western hemisphere was subject to commitments within agreements modelled on NAFTA (Prieto, 2003).

There are several key innovations that set NAFTA apart from GATS and place it in the realm of GATS-plus agreements. The incorporation of provisions covering investment related to trade in services was an innovation of NAFTA, and NAFTA uses a negative list approach. It can thus be seen as GATS-plus in mode 3. Since NAFTA entered into force, such investment provisions have been a feature of other NAFTA-type agreements (see chap. 8 on investment). NAFTA applies a negative list, or top-down, approach rather than the hybrid approach as used in GATS. Trade in all service sectors between the parties, with a few exceptions, is fully liberalized unless specifically listed in their reservation lists.²⁵ The negative list approach results in NAFTA being more transparent in its rule-making and more liberal than GATS.

In addition to provisions granting national treatment and MFN in a similar manner to GATS, chapter 12 (cross-border services) of NAFTA grants the right of non-establishment to services providers subject to reservations (art. 1205). Under this rule, service providers of another party are not required to establish a local presence, such as a branch or office, in order to be able to supply services. Unlike GATS, NAFTA does not establish disciplines for emergency safeguards or subsidies.

NAFTA is slightly GATS-plus in the area of transparency, in that in addition to requirements for the establishment of a contact point (art. 1801) it also states that parties shall inform the other parties of any “proposed or actual measure that the Party considers might materially affect the operation of the Agreement”, while GATS limits this to existing measures (art. III:3). However, the members of NAFTA have experienced difficulties in achieving full compliance with the transparency requirements of the negative list approach, specifically at the subfederal and provincial levels (Prieto, 2003: 220).

US non-state actors had significant influence on the shaping of NAFTA, as they do for all US trade agreements given the institutional consultation procedures established by the 1974 US Trade Act. During the NAFTA negotiations, the Services Policy Advisory Group and the Industry Sector Advisory Committee provided input and support. In the final stages of the ratification process, labour and environmental groups succeeded in forcing the Clinton administration to add two side-agreements to the main text addressing issues of concern to these groups. The procedural elements allowing interested parties, whether state or non-state, to

have input into the negotiations are reflected in US models of bilateral and regional agreements.

Telecommunications services under NAFTA

NAFTA included a separate chapter on telecommunications that focused on value-added services such as the interoperability of networks, but like the CUSFTA did not address basic telecommunications services.²⁶ NAFTA incorporates the language on value-added telecommunications used in the 1994 GATS Annex on Telecommunications. Parties agree to offer access to public telecommunications transport networks under reasonable and non-discriminatory conditions (art. 1302), to ensure that any procedure related to the provision of value-added services is transparent, non-discriminatory and processed promptly (art. 1303), to limit the “standards-related measures relating to the attachment of terminal or other equipment to the public telecommunications transport networks” (art. 1304) and to work to prevent anti-competitive conduct of monopolies through such measures as structural separation (art. 1305). To promote the interoperability of networks, the governments of Canada, Mexico and the United States pledged to exchange technical information (art. 1309:1). Finally, the parties agreed to assess the feasibility of progressive liberalization in all telecommunication services (art. 1309:2).

The provisions for the liberalization of telecommunications services under NAFTA illustrate that liberalization requires the right conditions for progress to be made. When NAFTA was negotiated the conditions were not right for liberalization of basic telecommunications services. Nor were the negotiating climate and technical conditions right when GATS was concluded in late 1993. It was only with the ABT and the WTO Reference Paper in 1997 that further progress could be made. As Sauvé argues, during these negotiations the “required constellation of forces – in political, regulatory and technological terms” was in place, thus allowing greater commitments to be made (Sauvé, 2003: 37).

Latin American RTAs

MERCOSUR

The Southern Cone Common Market (MERCOSUR) consists of Argentina, Brazil, Paraguay and Uruguay. The founding document of MERCOSUR, the Treaty of Asuncion, entered into force on 29 November

1991 with a commitment to establish a common market, including the free movement of goods, services and factors of production, by 31 December 1994 (art. I).²⁷ Although the initial deadline for the establishment of a common market was not met, MERCOSUR enjoyed rapid growth through the 1990s. Despite a downturn in this growth at the turn of the millennium, by 2003 MERCOSUR was the fourth largest trade bloc in the world with a population of approximately 230 million and a GDP of over US\$1 trillion (FIEO, 2004).

The Protocol of Ouro Preto, adopted in December 1994, set out the institutional structure of MERCOSUR, broadly similar to that of the European Union.²⁸ Regarding dispute settlement, the annex to the protocol grants both member states as well as individuals, natural or legal, the right to bring a complaint to the Trade Commission (art. I).

As a means towards the elimination of barriers to trade in services, the Protocol of Montevideo on Services was adopted in December 1997 but has yet to enter into force. MFN provisions call for the “immediate and unconditional”²⁹ removal of any discrimination between any service or service provider in the members, including any agreement with third countries that denotes a significant enhancement of the rules established in GATS (art. II:2–3). There are also NAFTA-type agreements that allow certain exemptions to MFN (Prieto, 2003). In contrast to GATS and NAFTA that incorporate the objective of progressive liberalization in trade in services, the MERCOSUR Protocol on Trade in Services is far more ambitious, albeit only on paper to date, in that its objective is the promotion of free trade in services between the member states (art. I). Once the protocol is in force, member states will engage in successive rounds of negotiations on an annual basis with the objective of progressive liberalization of barriers to trade in services covering a greater number of sectors and subsectors (art. XIX). This transition period is to last no longer than 10 years from the entry into force of the protocol. The protocol applies to activities involved in the provision of services, including commercial presence, and covers all services sectors with the exception of services supplied in the exercise of government authority (art. II).

Under MERCOSUR national treatment and market access provisions are ultimately to be considered general obligations, rather than specific obligations as in GATS. However, the Protocol on Trade in Services specifies that member states will use a positive list approach as in GATS during the transition to free trade in services.

Transparency provisions as set out by the MERCOSUR Protocol on Trade in Services are similar to those within GATS (art. VIII). However, Prieto (2003: 237) argues that the protocol is more expansive than GATS here, since it requires member states to provide comprehensive lists of

measures in not only sectors that are included in a member's list of specific commitments but also in sectors that are not.

Andean Community

The Andean Community, comprising Bolivia, Colombia, Ecuador, Peru and Venezuela, was established in 1969 by the Cartagena Agreement. Decision 439 (General Framework of Principles and Rules and for Liberalising the Trade in Services in the Andean Community) of the Andean Community, adopted in December 1998, established a deadline of no later than 2005 for the free trade in services. This objective is to be achieved through a process of progressive liberalization. Interestingly, in the preamble of the decision, members note that GATS, "particularly article V, and the other multilateral and plurilateral negotiations underway have created a favourable climate for liberalising the trade in services within the subregion".³⁰ With a view to consistency with GATS, the decision later states that "the idea, definition and interpretive elements contained in the GATS shall be applied ... whenever pertinent" (art. 26).³¹

In terms of scope and coverage, and in compliance with GATS article V, decision 439 covers all four modes of trade in services and all service sectors. The principles of market access, national treatment and MFN are granted.³² The Andean Community incorporates a significant level of transparency. Similar commitments to those in GATS are established for the publication of all measures of general obligation (art. 9), although there is no requirement for the establishment of enquiry points. However, during the process of liberalization towards free trade in services, members commit to the adoption of an "inventory of the measures maintained by each Member" that are contrary to the principles of MFN and national treatment by no later than 31 December 1999 (art. 14).³³ On 31 October 2001 article 510, Adoption of the Inventory of Measures Restricting the Trade in Services, was signed, with the aim of gradually phasing out the listed barriers to trade by 2005.

The Andean Community applies a negative list approach to liberalization. During the liberalization process members will engage in annual negotiations, coordinated by the General Secretariat, with a view to the gradual and progressive elimination of barriers identified in the inventory list (art. 15).³⁴ Decision 439 also incorporates a standstill provision that is not explicitly present in other regional RTAs (art. 10).

In a final provision, decision 439 stipulates that the General Secretariat will call upon experts from the member states to assist it in the implementation of the decision (art. 25). With respect to telecommunica-

tions services, the Andean Committee of Telecommunications Authorities (CAATEL) is to meet within two months following the decision's entry into force, with the objective of developing principles, commitments and rules for the liberalization of telecommunications.

Telecommunications services within the Andean Community

The liberalization provisions within the telecommunications sector of the Andean Community are significant in terms of scope and coverage. In decision 462 (Provisions Regulating the Integration and Liberalisation of the Trade in Telecommunications Services in the Andean Community) that was adopted in May 1999, the members agree to the deregulation of all telecommunications services except for television broadcasting and sound radio (art. 3). This deregulation is to take place in two stages: by 1 January 2000 elimination of all "restrictive measures concerning telecommunications services other than basic local, national and international long-distance, and mobile land telephony"; and by 1 January 2002 this liberalization is to include basic telecommunications services of local, national and international long-distance and mobile land telephony (art. 7). In March 2001 the CAATEL approved a six-year strategic plan for 2001–2006 that will shape government telecommunications policy, including the long-term objective of entering into agreements with other RTAs that will be "conducive to the development of international telecommunications markets".³⁵

Decision 462 also contains provisions covering the access to and use of public telecommunications transmission networks and services; rules for the authorization of certificates, including the aim of harmonization of requirements and procedures; measures regarding the standardization of terminal equipment; the protection of free competition; principles regarding interconnection; and transparency. The decision also addresses the important issue of universal services in setting out that member states have the right to "define the type of Universal Service obligation they wish to maintain" (art. 35). Critical in terms of consumer rights, the decision provides the final user with "a free choice of the service supplier and acknowledgement of the rates charged" (art. 36).

The Andean Community has recently sought closer economic and trade ties with other RTAs. In May 2004 the Andean Community and European Union agreed to begin work on a joint assessment exercise with the objective of beginning trade negotiations toward an RTA between their regions. In December 2004 the Andean Community and MERCOSUR signed the Cuzco Declaration committing to the creation of a South American Union similar in scope and degree of eventual integration to the European Union.

EU-driven RTAs

The Euro-Mediterranean agreements

To date the European Union has concluded bilateral association agreements with 10 Mediterranean countries: Tunisia (1995), Israel (1995), Turkey (1995), Morocco (1996), Jordan (1997), the Palestinian Authority (1997), Algeria (2002), Lebanon (2002) and Syria (2004). The overall objective of these individual agreements is to form a single Euro-Mediterranean Free Trade Area by 2010.

The Euro-Mediterranean (MED) agreements are generally characterized by their limited scope in terms of both liberalization (title III) and cooperation in trade in services. However, while the MED agreements are considered somewhat weak in terms of short-term liberalization in trade in services, their strength is in the potential for longer-term liberalization.³⁶ Progress was made towards realizing this potential at the July 2004 Euromed Conference of Ministers of Trade, where the framework protocol for the liberalization of trade in services was approved. This protocol set the stage for the negotiation of agreements on trade in services and investment between the European Union and the Mediterranean region.

The earlier/original bilateral EU agreements with Algeria and Jordan contain national treatment clauses, albeit with exceptions, thus establishing deeper liberalization than the other MED agreements. The agreements with partners that are WTO members (Israel, Jordan, Morocco and Tunisia) reaffirm their commitments under GATS and pledge for the Association Council to assess the aim of progressive liberalization of trade in services within a time period ranging between three and five years.

Both the European Union and Jordan list reservations in the application of the national treatment principle, among others in investment and mining. For Jordan, annex V explicitly places reservations on EU ownership of public shareholding companies, construction, trade, trade services and mining companies, and sets a minimum amount for non-Jordanian investment in any project. Annex VI on EU reservations include telecommunications as well as agriculture, mining, fishing, transport, news agency services and audiovisual services, all of which will be excluded from national treatment or have reservations regarding it.

In terms of cooperation, the EU-Algeria Association Agreement, not yet in force, encourages technical assistance in the form of “exchange of information and provision of any technical assistance required on regulations and standardisation, conformity testing and certification of infor-

mation and communication technologies; the dissemination of advanced information and telecommunication technologies” (art. 60). Similarly, the EU-Israel Association Agreement that entered into force in 2000 mandates that the parties shall promote cooperation in the development of telecommunications, including “harmonization of standards” (art. 52). The EU-Lebanon Association Agreement includes provisions for cooperation between the parties regarding “interconnection and interoperability between Community telematic networks and services” and for the establishment of “a dialogue on regulatory cooperation on international services” (art. 53). The EU agreements with Morocco and Tunisia are similar in encouraging cooperation in the standardization of telecommunications and dissemination of information on the interconnection of networks.

EU-Chile Association Agreement

The EU-Chile Association Agreement was signed in November 2002. The majority of the trade chapter has been provisionally in effect since 1 February 2003, and covers political dialogue and cooperation in various sectors in addition to establishing commitments for the reduction of barriers to trade in goods and services. However, given that the services sector is under mixed competence within the European Union, before the agreement can be fully implemented not only must the European Parliament give its assent but the national parliaments must also ratify it. Although the European Parliament has given its assent, not all member states have ratified the agreement.

As with the other RTAs the European Union has entered into, the EU-Chile Association Agreement conforms to the principles as set out in GATS, including its application of definitions, market access and national treatment. The schedules of each party’s specific market access commitments are set out in annex VI. The association agreement resembles several of the other EU RTAs in its commitment to progressive liberalization in services to take place within three years after entry into force of the agreement (i.e. by 1 February 2006). The European Commission and the Chilean government are to review the implementation of the services provisions every three years and make recommendations to the Association Council meeting at ministerial level (art. 100). Two years after entry into force of the agreement, the European Union and Chile commit to seek additional liberalization in the movement of natural persons (mode 4), an area which developed countries have generally been hesitant to liberalize further, as well as consider broadening the current definition of natural persons as set out in article 96(g) (art. 101). The ar-

ticles on domestic regulation and mutual recognition are subject to review every three years by the Association Committee (arts 102.2 and 103.6). In line with GATS article III on transparency, the parties agree to assign a contact point in their respective territory to direct enquiries involving service suppliers (art. 105).

Telecommunications within the EU-Chile Association Agreement

In the telecommunications services sector, the association agreement goes considerably beyond earlier EU RTAs and reflects the GATS Telecommunications Reference Paper nearly word for word, thus being an example of reference-paper-driven regionalism.

Telecommunications regulatory agencies are to be both independent from any supplier of basic telecommunications services and non-discriminatory (art. 110). There is to be public availability of the terms and conditions of licence requirements as well as the expected date of a decision (art. 111.1). Alternatively, if a request for a licence is rejected, the reasons will be provided to the applicant if requested (art. 111.2). There are competitive safeguards to prevent anti-competitive practices among large telecommunications service suppliers, including anti-competitive cross-subsidization, and “appropriate measures shall be maintained” (art. 112.2). Public suppliers of telecommunications transport networks or services shall offer interconnection to other suppliers that are not discriminatory in terms of rates, conditions and quality (art. 113.2). Interconnection procedures and agreements shall be available to the public (art. 113.4). Procedures for the allocation of scarce resources are to be objective, timely, transparent and non-discriminatory (art. 114). Under the association agreement, each party is granted the right to specify its universal service obligations as long as the provisions are “transparent, objective and non-discriminatory” as well as “neutral with respect to competition and . . . no more burdensome than necessary” (art. 115.2).

In the EU’s schedule of services restrictions, market access and national treatment for domestic and international telecommunications services for mode 4 (Presence of Natural Persons) are unbound with a few exceptions (annex VII, part A). Chile specifies that for basic telecommunications services, private services which have as an objective the satisfaction of “specific telecommunications needs of particular companies, entities or persons by prior agreement, the supply of these services does not give access to traffic from or to the users of the public telecommunications networks” (annex VII, part B). In sum, the EU-Chile agreement appears to be more GATS-consistent than GATS-plus in telecommunications.

Post-reference paper US-driven

US-Singapore Free Trade Agreement

The US-Singapore FTA was signed in May 2003 and went into effect on 1 January 2004. For the United States this was the first such agreement with an Asian country. In a similar manner to the recent US bilateral and regional trade agreements, such as the Central American-Dominican Republic FTA (discussed below) and the US-Australia Agreement, chapter 9 of the US-Singapore FTA on telecommunications incorporates significant progress in terms of detailed language as compared to earlier telecommunications services agreements. For Singapore this agreement incorporated greater telecommunications services rule-making, including the application of the WTO Reference Paper, than previous agreements, such as the agreement between Japan and the Republic of Singapore for a New-Age Economic Partnership (JSEPA) that entered into force in November 2002.

Article 9.1 of the US-Singapore agreement sets out the scope and coverage, which excludes cable or broadcast distribution of radio or television programming. However, a party may compel an organization involved in cable or broadcast distribution to make its facilities available as a public telecommunications transport network (art. 9.1:3:a).

Standard interconnection provisions are included, although there is a privacy element that calls on parties to ensure that suppliers of public telecommunications services “take reasonable steps to protect the confidentiality of proprietary information of, or relating to, suppliers and end-users of public telecommunications” (art. 9.3:2).

Article 9.4 sets out rules on the conduct of major suppliers in far greater detail than earlier bilateral, regional and multilateral agreements. Rules govern treatment by major suppliers; competitive safeguards; unbundling of network elements; co-location; resale; poles, ducts and conduits; number portability; interconnection, including resolution of telecommunications disputes; and provisioning and pricing of leased circuits services. However, the article does not apply to commercial mobile services and rural telephone companies in the United States.

Several provisions closely reflect the WTO Reference Paper, such as the requirements for independent regulation, universal services, the transparency of licensing procedures and the allocation and use of scarce resources.

The US-Singapore agreement is noteworthy for incorporating provisions covering enforcement and resolution of domestic telecommunications disputes not addressed within GATS or the Telecommunications Reference Paper. Article 9.10 mandates that telecommunications regula-

tory bodies must enforce specific domestic measures, and grants them the authority to use sanctions such as financial penalties, injunctive relief or revocation of licences. Regarding the resolution of domestic telecommunications disputes, parties shall have recourse to telecommunications regulatory bodies, reconsideration and judicial review (art. 9.11).

Provisions on transparency are similar to both other RTAs and GATS in setting out requirements for the publication and notification of relevant legislation. Additionally, interested parties need to be given adequate advance public notice in which to comment on any proposed legislation (art. 9.12.2).

Two interesting articles address the need for freedom in the choice of telecommunications technologies and a minimal regulatory environment for public telecommunications services. Article 9.13 states that the parties shall aim not to prevent public telecommunications service suppliers “from having the flexibility to choose the technologies that they use to supply their services, including commercial mobile services, subject to the ability of each Party to take measures to ensure that end-users of different networks are able to communicate with each other”. Article 9.14 allows for parties to refrain from applying regulation to public telecommunications services given “the importance of relying on market forces to achieve wide choice and efficient supply of telecommunications services”.

In their respective market access restrictions schedules, the United States does not appear to list any restrictions while Singapore reserves the right to take measures that accord “treatment to persons of the other Party equivalent to any measure adopted or maintained by the other Party limiting ownership by persons of Singapore of enterprises engaged in the provision of public mobile and wireless communications” in the United States.

CAFTA-DR

The Central American-Dominican Republic-United States FTA (CAFTA-DR) was officially signed on 2 August 2005 between Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, the United States and the Dominican Republic, but has yet to enter into force. In terms of structure and content, chapter 13 on telecommunications of the CAFTA-DR is remarkably similar to the US-Singapore FTA chapter. Thus, these RTAs may be seen as iterative platforms. However, there are some differences.

Provisions for the allocation and use of scarce resources are similar to the reference paper and the US-Singapore FTA, but add that the parties retain the right to establish and apply their “spectrum and frequency

management policies, which may limit the number of suppliers of public telecommunications services, provided that it does so in a manner that is consistent with this Agreement. Each Party also retains the right to allocate frequency bands taking into account present and future needs” (art. 13:10:3).

Notably, annex 13 sets out specific commitments of Costa Rica on telecommunications services in order to ensure that the process of liberalization in telecommunications services is “to the benefit of the user and shall be based on the principles of graduality, selectivity, and regulation, and in strict conformity with the social objectives of universality and solidarity in the supply”. Article II sets out that a new legal framework will be brought into force by 31 December 2004 in order to bring about the modernization of the Instituto Costarricense de Electricidad. The annex also establishes a schedule for the selective and gradual opening of markets in such areas as private network services, internet services and mobile wireless services between 2006 and 2007 (art. III.2). The WTO Reference Paper is also closely followed.

Conclusion

This analysis has provided an examination of the provisions relating to rule-making in telecommunications services within selected bilateral, regional and multilateral agreements in order to attempt an initial evaluation of the systemic impacts RTAs have had on the evolution of rule-making and governance issues in telecommunications at the multilateral level. This section offers tentative conclusions on the key research questions addressed in the study on the interaction between the multiple levels of rule-making.

Systemic question – Evolution of international rules

For trade in services, the general consensus seems to be that RTAs are complementary to the multilateral approach. Among some government trade officials and trade experts there seems to be a general consensus that “RTAs can be a helping hand for multilateral trade negotiations”.³⁷

In the case of trade in telecommunications services, evidence indicates that the relationship between the multiple levels of rule-making is characterized by iterative interaction, with concepts and provisions taken from one level and applied at another. This study has highlighted this relationship using the case of the WTO Reference Paper, where the developments at the multilateral level have been applied, and in some cases exceeded, at the bilateral and regional levels. Table 6.4 outlines where

Table 6.4 WTO-plus nature of FTAs in telecommunications services

Agreement	Degree to which RTAs reflect the WTO Reference Paper						
	Definitions	Competitive safeguards	Interconnection	Universal service	Transparency	Independent regulator	Scarce resources
NAFTA	NA	NA	NA	NA	NA	NA	NA
MERCOSUR	-	-	-	-	+	-	-
Andean Community	-	-	-	✓	-	-	-
Euro-Med	-	-	-	-	-	-	-
EU-Chile	✓	✓	✓	✓	✓	✓	✓
US-Singapore	✓	+	+	✓	✓	✓	✓
CAFTA-DR	✓	+	+	✓	✓	✓	✓

✓ agreements have met the principles established in the WTO Reference Paper

+ agreements have surpassed the principles established in the WTO Reference Paper

- agreements have not met the principles established in the WTO Reference Paper

NA agreements are not applicable to the principles established in the WTO Reference Paper

the agreements have met, surpassed, not met or are not applicable to the principles established in the WTO Reference Paper.

Domestic policy formulation and implementation

The United States is following an approach of competitive liberalization in which all levels are to be used to advance its trade objectives. It shows continued activity in negotiating bilateral and regional trade agreements at the same time as promoting progress in the current Doha Development Agenda (DDA) negotiations. In contrast, the European Union has focused its rule-making efforts on the multilateral level and stated its intention not to enter into any new RTAs until the DDA is completed.

Institutional factors also play a critical role in terms of ratification and implementation. In the United States, gaining Trade Promotion Authority in 2002 has had an energizing effect on the pace of negotiations of US RTAs. In contrast, the EU's procedures of mixed-competency agreements have delayed the ratification and implementation of some RTAs, such as the EU-Chile agreement.

For developing countries, negotiations with both developed countries and other developing countries may be stretching their capacity, specifically in terms of requirements of negative list transparency. However, rule-making in trade in services within developing countries may bring the benefit of promoting transparency and good governance and encouraging foreign direct investment in key services sectors.

Prescription

The influence of the GATS Reference Paper is clearly observable in agreements established after the ABT came into force. In more recent RTAs there is evidence of further progress in the detail of the rules as established in the reference paper. However, the continued synergistic interaction of the multiple levels of rule-making in telecommunications will depend to a large extent on whether future RTAs are comprehensive and complementary in terms of scope, coverage and liberalization; the degree of interaction between governments and telecommunications services providers; and the pace of technological innovation.

Acknowledgements

The author is grateful to Pierre Sauvé for raising and clarifying a number of points. Anonymous referees of the chapter also made helpful comments.

Annex 6.1: The iterative nature of the EC's telecommunications services regulatory framework and the WTO Reference Paper

Principles within the WTO Reference Paper	Recommendations, rules and principles within the EC telecommunications green paper	Progressive EC regulatory developments
Definitions		2002 Framework Directive on a Common Regulatory Framework for Electronic Communications Networks and Services (2002/21/EC)
Competitive safeguards	“to safeguard the role of the Telecommunications Administrations, operators of national public or private networks, in the supply of infrastructure to carry information and to this end to assure them of the resources to make them financially viable”	2002 Directive on competition in the markets for electronic networks and services (2002/77/EC) 1994 Satellite Directive expanded liberalization of telecommunications to the satellite communications sector (94/46/EC) 1990 Commission Directive on competition in the markets for telecommunications services (90/388/EEC; repealed by 2002/77/EC)
Interconnection	“complete freedom of access from any connection point”	2002 Access Directive on access to, and interconnection of, electronic communications networks and associated facilities (2002/19/EC) 2002 Authorisation Directive on the authorization of electronic communications networks and services (2002/20/EC) 1997 Directive on interconnection in telecommunications with regard to ensuring universal service and interoperability through application of the principles of open network provision (97/33/EC)

Annex 6.1 (cont.)

Principles within the WTO Reference Paper	Recommendations, rules and principles within the EC telecommunications green paper	Progressive EC regulatory developments
Universal service		<p>1990 Framework Directive incorporated the concept of interconnection within its open network provision</p> <p>1988 Directive on competition in the markets in telecommunications terminal equipment (88/301/EEC)</p> <p>2002 Universal Service Directive on universal service and users' rights relating to electronic communications networks and services (2002/22/EC)</p> <p>1997 Directive on interconnection in telecommunications with regard to ensuring universal service and interoperability through application of the principles of open network provision (97/33/EC)</p>
Transparency	“close consultations with all those involved to ensure a smooth transition and optimum utilisation of network and service developments to create new jobs”	2002 Framework Directive on a Common Regulatory Framework for Electronic Communications Networks and Services (2002/21/EC); article 6
Independent regulators	“complete separation of the regulatory and operational functions”	<p>2002 Framework Directive on a Common Regulatory Framework for Electronic Communications Networks and Services (art. 3)</p> <p>1990 Framework Directive</p> <p>1988 Council Resolution (88/C 257/01)</p>

Annex 6.1 (cont.)

Principles within the WTO Reference Paper	Recommendations, rules and principles within the EC telecommunications green paper	Progressive EC regulatory developments
Allocation and use of scarce resources		1997 Directive on a common framework for general authorizations and individual licences in the field of telecommunications services (97/13/EC) 1992 Directive on the application of open network provision to leased lines (92/44/EEC)

Annex 6.2: Highlights of commitments and exemptions in basic telecommunications

Subsector by subsector commitments in the Agreement on Basic Telecommunications

- Voice telephone service: 49 schedules (covering 63 governments) commit to competitive supply (defined here as permitting two or more suppliers). This compares favourably with April 1996 results when 44 governments included voice services. These commitments permit competition in the supply of public voice services, either immediate or phased in, in at least one market segment, except for one, which commits to voice only over closed user groups in all market segments.
- Public voice services: 44 schedules (58 governments) committed on local service, 41 (55 governments) offered domestic long distance, and 45 (59 governments) offered international service. Resale of public voice telephone is included in the commitments in 30 schedules (44 governments) or more than 70 per cent of the 62 governments permitting or planning to introduce a degree of competition in public voice service.
- Other services: data transmission – 51 schedules (65 governments) include commitments of data transmission services; cellular/mobile telephone – 48 (62 governments) grant access for cellular/mobile telephone markets; leased circuit services – 42 (56 governments) commit to competition in leased circuit services (the supply of transmission capacity); other types of mobile services – 48 (62 governments) include

commitments on other types of mobile services (such as PCS, mobile data or paging).

- Satellite-related communications: 39 schedules (53 governments) committed on some or all types of mobile satellite services or transport capacity and 38 (52 governments) commit on fixed satellite services or transport capacity.
- Value-added telecommunications services: 10 governments scheduled some commitments on value-added telecommunications services (e.g. e-mail, online data processing or database retrieval).

Source: WTO, www.wto.org/english/tratop_e/serv_e/telecom_e/telecom_highlights_commit_exempt_e.htm.

Notes

1. Any assessment of the iterative interaction between the multiple levels in trade in services is necessarily somewhat limited since, at the time of writing, only one round of GATS negotiations had been completed.
2. Noted by Sir Nicholas Bayne, who served as the British representative to the OECD in the mid-1980s, in an interview on 8 October 2004 in London.
3. For an excellent first-hand account of the work of this trade in services epistemic community by the leader of this group, see the appendix in Feketekuty, 1988. For an interesting discussion of this group's work within the OECD and GATT Uruguay Round see Drake and Nicolaidis, 1992.
4. The European Community was at first sceptical about the need for such a framework. However, following the publication of OECD national case studies showing that the European Community, including France, which had been opposed to multilateral trade in services negotiations, had a comparative advantage in trade in services, scepticism turned into strong support. Noted by Sir Nicholas Bayne in an interview on 8 October 2004 in London.
5. Although commonly referred to as the Cockfield White Paper, the official title is *Completing the Internal Market: White Paper from the Commission to the European Council*, COM(85)310 final, Brussels, 14 June 1985.
6. Article 1401.2(c) of the CUSFTA makes a clear exception of commercial presence for investment.
7. In the event that the Uruguay Round negotiations failed in the attempt to establish an agreement on trade in services, there was support for the idea of expanding the membership of the RTA to countries within a "market liberalization club". See Schott, 1988.
8. Members of the G10 were at this time opposed to allowing the inclusion of trade in services within any new multilateral trade round. This opposition changed in 1986.
9. Approximately 150 various types of services activity are addressed in the GATS schedules. See the WTO's services sectoral classification document MTN.GNS/W/120, available at www.wto.org/english/tratop_e/serv_e/mtn_gns_w_120_e.doc.
10. However, the notable exceptions are RTAs that apply a negative list approach. Not only do such RTAs not define trade in services on the basis of the mode of supply as applied within GATS, but commitments are also not based on modes of supply.
11. Within GATS exceptions to MFN treatment are possible through article II – Exemptions. Other RTAs, except for the MERCOSUR Protocol and the Andean Community's decision 439, also allow similar derogations to MFN. See Sauvé, 2003, pp. 26, 38.

12. GATS may be said to apply a hybrid approach to liberalization (i.e. incorporating elements of both positive and negative approaches), since members must also list any non-conforming measures they wish to preserve. See Sauvé, 2003, p. 27.
13. This is due to the character of trade in services, which does not offer the importing country additional controls such as quantitative restrictions and import duties as in the case of trade in goods. Therefore, GATS allows members to identify which sectors will or will not be subject to domestic preference (WTO, 1999: 8).
14. Since the European Community represents its member states at GATT/WTO, this figure calculates them as one.
15. Given that there was not a mandate to liberalize basic telecommunications within the Uruguay Round services negotiations, even this limited number of commitments was somewhat surprising.
16. Of particular relevance for this study, the annex on telecommunications obligates members to ensure that access to public telecommunications transport networks and services are provided on “reasonable and non-discriminatory terms and conditions” (art. 5:a). However, provided that these criteria are met, members may impose several conditions, such as limits on the resale or shared use of public telecommunications services and interconnection and interoperability requirements (art. 5:f).
17. This successive liberalization has included additional successful sectoral negotiations in telecommunications, lesser success in financial services and the movement of service suppliers and abortive negotiations on maritime services, as well as the current GATS negotiations under the Doha Development Agenda.
18. As pointed out by Christopher Roberts, senior trade adviser with Covington and Burling, during an interview on 12 October 2004 in London.
19. The United States was unhappy with the lack of significant concessions by key members. Additionally, some US services firms were concerned about certain elements of the proposed agreement (Noam and Drake, 1997: 6).
20. This reference paper was largely prepared by the United States.
21. As described by Pascal Kerneis, managing director of the European Services Forum, on 27 October 2004 in Brussels.
22. A counsellor in the WTO Trade in Services Division argues that the real value of the reference paper was that it showed which governments wanted to liberalize their telecommunications services and which did not. Interview on 3 November 2004 in Geneva.
23. Interview with a counsellor in the WTO Trade in Services Division on 3 November 2004 in Geneva.
24. In addition to influence, NAFTA has great impact on the world economy. NAFTA documents prepared for the occasion of the agreement’s tenth anniversary declared that it was the “world’s largest free trade area, with about one-third of the world’s total GDP (\$11.4 trillion), significantly larger than that of the European Union” even following the accession of the 10 new member states (NAFTA Secretariat, 2003: 1).
25. With respect to the reservations lists, NAFTA grants parties the right to modify their specific reservations within a specific time-frame as long as they do not increase the degree of protectionism. Under NAFTA, parties will receive credit for any such autonomous liberalization in any future negotiations. NAFTA was the first RTA to incorporate this innovative “ratchet mechanism”, which is a feature of several other NAFTA-type agreements.
26. The language in NAFTA and later agreements also reflects the dynamic technological environment of the telecommunications services sector. Distinctions between basic telecommunications and value-added networks made in earlier agreements such as NAFTA are not made in more recent agreements.

27. Annex 1 of the Treaty of Asuncion grants Paraguay and Uruguay an extended deadline of 31 December 1995 for their schedules of elimination (art. 1).
28. MERCOSUR institutions include a Council representing the member states, an executive Common Market Group and a Trade Commission responsible for trade policy between member states and with third countries. Democratic accountability is addressed through the establishment of a Parliamentary Commission and Economic-Social Consultative Forum. Additionally 10 sectoral working groups are established, none specifically covering trade in services.
29. This MFN requirement is unlike GATS article II:2 that allows derogations to MFN.
30. See decision 439 of the Andean Community.
31. *Ibid.*
32. However, balance of payment safeguards are established (art. 20).
33. Prieto (2003: 238) argues that the information contained within this inventory is critical to the process of liberalization and to "efforts aimed at harmonising the existing regulations" of each member while being "an instrument of extraordinary commercial value for the conduct of services trade" between the countries of the Andean Community.
34. Accelerated liberalization between two or more members may occur (art. 16), but Bolivia and Ecuador are granted preferential treatment in respect to deadlines and temporary exception (art. 22).
35. See www.comunidadandina.org/ingles/services/teleco.htm.
36. The Euro-Med agreements have been reviewed by a series of Euromed ministerial trade conferences in Brussels (2001), Toledo (2002), Palermo (2003) and Istanbul (2004).
37. Interview with senior Commission official in DG Trade on 26 October 2004 in Brussels.

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The international regulation of IPRs in a TRIPs and TRIPs-plus world

Meir Perez Pugatch

Uno avulso non deficit alter
When one is torn away, another succeeds
Virgil: *Aeneid*

Introduction

Any discussion of trade-related intellectual property agreements is far from being natural and straightforward. Unlike other trade agreements, the international regulation of intellectual property (IP) rights ultimately deals with a very unique commodity – knowledge. It is therefore subject to a set of constraints and interests that differ substantially from the “conventional” challenges of international trade agreements. Suffice it to say that while trade liberalization agreements aim (at least in theory) to reduce the level and volume of protectionism, international IP agreements aim to increase it.

There is substantial evidence suggesting that, since the year 2000, regional and bilateral trade agreements between developed and developing countries have gone beyond the WTO agreement on trade-related aspects of intellectual property rights (TRIPs). There is also evidence that these so-called TRIPs-plus provisions are based on the IP standards of developed countries, primarily the United States and the European Union. Thus far, however, less attention has been devoted to theoretical and empirical analysis of the interaction between the international, regional

and bilateral levels of rule-making in IPRs. That is the purpose of this chapter.

The chapter first provides an overview of the economics of IPRs in general and their manifestation in international trade agreements in particular. Attention here is given to the basic dilemma of knowledge creation and knowledge allocation under a regime of IPRs; balance of trade issues; and the possible linkage between international IP commitments, technology transfer and foreign direct investment. The chapter then identifies some typical key elements of IPR rules in trade agreements. This provides the analytical framework for assessing rules at the different levels.

Finally, the chapter discusses the differences between the US and EU approaches to the protection of IPRs in RTAs (regional trade agreements) and the degree to which these go beyond TRIPs in key areas such as pharmaceutical IPRs (data exclusivity and patents) and, somewhat more superficially, in copyrights and trademarks.

The complex nature of IPR economics

Economists explore ways of efficiently allocating scarce resources to unlimited wants, and find that private property rights are a plausible way of dealing with scarcity in an efficient manner. Knowledge, however, is a unique resource, given that it is not inherently scarce. Theoretically speaking, the potential use of existing knowledge is unlimited and may be diminished only when such knowledge becomes obsolete. Thus the use of any invention by one individual does not reduce its accessibility to others but is more likely to increase it.

Patents, copyrights, trademarks and other forms of IPRs establish exclusive ownership (monopoly) on varying types of knowledge, allowing its owners to restrict, and even prevent, others from using that knowledge. The result, as Hindley (1971) puts it, is that “the establishment of private property rights in these cases artificially creates the symptoms of scarcity; they do not derive from it”.

Before briefly describing the economic challenges associated with the international IP rule-making, it is important to note that there are fundamentally different types of knowledge resources.

The economics of IPRs from a social welfare perspective – IPRs in a closed economy

In principle, economists should be able to tell us whether, on balance, a system of IPRs generates a net loss or a net benefit to society. Unfortunately, thus far, or at least for the past 80 years, economists have been

unable to provide such an answer notwithstanding the availability of rich and in-depth literature on the economics of IPRs (Machlup, 1958; Primo-Braga, 1990). Consider, for example, two forms of IPRs: patents and trademarks. Common to these two forms of IPRs is the creation of market exclusivity (monopoly) in the use of existing knowledge inventions for patents and consumer information for registered trademarks. But a number of problems have precluded clear conclusions on the net benefit or loss to society from the use of patents (Machlup, 1958; Hindley, 1971: 1–31; Primo-Braga, 1990: 17–32).

Perhaps the most problematic aspect is the implied trade-off in the patent system between an increase in the available knowledge in the future and the efficient use of available knowledge in the present (Arrow, 1962: 609–626). Establishing property rights for inventions provides an incentive for firms and individuals to invest in future inventive activities. On the other hand, a patent system inhibits the free and rapid dissemination of existing knowledge, and once a firm has been granted a patent it essentially becomes a monopoly, since it has the exclusive right to control both the quantity and the price of its invention. Robinson's (1956: 87) "paradox of patents", coined as early as 1956, seems to capture the true nature of the patent trade-off: "by slowing down the diffusion of technical progress, patents insure that there will be more progress to diffuse".

The optimum term of patent protection is also highly contentious. A longer patent term increases the incentive to invent but prolongs the restriction on the use of existing knowledge. It is difficult to establish one patent term optimal to society as different inventions require different terms of protection. As a decision on a specific patent term for all inventions is bound to be arbitrary, there may be a term that is more socially desirable than the current period of 20 years (Nordhaus, 1969). As Fritz Machlup (1958: 79) argued in the 1950s, "no economist on the basis of present knowledge, could possibly state with certainty that the patent system, as it now operates, confers a net benefit or a net loss to society".

The economic utility of registered trademarks, although more coherent than that of patents, ultimately depends on the way in which trademarks are used. A system of registered trademarks may be considered an efficient source of information as long as it enables consumers to obtain additional and accurate knowledge on different products (UNCTAD, 1979; Chamberlin, 1966: 56–64; Hindley, 1971: 69–74). If this is not the case (for instance, when trademarks artificially differentiate between products that are for all purposes identical, such as in the case of generic pharmaceutical products, or when, due to extravagant advertising activities, the reputation of a given trademark exceeds the actual value of its product), trademarks can easily become a source of useless, inaccurate and even false information (Hindley, 1971: 69–74; UNCTAD, 1981: 8–14).

All of the above suggests that a pure economic approach cannot pro-

vide a sufficient and satisfactory explanation regarding the creation of IPRs.

IPRs in the international trade arena

Different countries will find it in their interests either to support or to reject a stronger international IP system, depending upon the effects of a stronger international system of IPRs on trade in IP-related products and the impact of IPR rules on the rate and magnitude of technology transfer and foreign direct investment (FDI). Countries, especially developed countries, with strong IP capabilities will not only improve their terms of trade by becoming an exporter of IP-related products, but will also benefit from higher prices thanks to their quasi monopoly in the IP products concerned (Vernon, 1957; Penrose, 1951; Chin and Grossman, 1990). On the other hand, countries with weak IP capabilities are likely to benefit most by not signing up to international rules on IPRs and thus leaving themselves free to exploit and imitate IP-related products in their own domestic economies. Where they are successful, these countries may even be able to compete with the original IP owners, thus becoming exporters of such products themselves (Penrose, 1951: 95–96).

Empirical data confirm the above picture. The global ownership and commercial exploitation of IPRs is completely dominated by a group of developed countries, notably the United States, the European Union and Japan. For example, UNCTAD (1975: 38) found that in the years 1964 and 1972 nationals of developed countries owned 97 per cent and 95.6 per cent of all patents granted to nationals and foreigners, respectively. In contrast, the foreign ownership of patents by nationals of developing countries in these years amounted to less than 1 per cent. In both 1964 and 1972, five developed countries owned approximately 80 per cent of patents granted to foreigners, with the United States holding around 40 per cent of these patents. The other 40 per cent were distributed between Germany (then the Federal Republic of Germany), Switzerland, the United Kingdom and France (UNCTAD, 1975: 39). Data gathered in 1996 and 2000 (based on statistics from WIPO, the World Intellectual Property Organization) suggest that developed countries have maintained their dominance, with a total of 95 per cent and 93 per cent respectively of all patents in these years (Pugatch, 2004: table 3.1).¹

A second dimension to the discussion concerns the extent to which a stronger commitment to IP protection will enable developing countries to secure a greater rate of technological transfer and FDI. Since technology transfer and FDI are very broad concepts, there is a need to be more precise about their relation to IPRs. Of particular importance is the distinction between the direct (or static) and indirect (or dynamic) effects of

IPRs on technology transfer and FDI. The former refers mainly to the argument that foreign IP owners, in exchange for obtaining protection in developing countries, are required to make the technology embodied in their products (or processes) available and accessible in these countries (Grundman, 1970: 193–207; Yankey, 1987: 15–19; Maskus and Konan, 1994: 401–454). The latter reflects the view that stronger IP protection creates a more secure and attractive environment in which various forms of FDI and technology transfer (mainly via licensing agreements and joint ventures) can take place (Sherwood, 1990; OECD, 1989: 11). These direct and indirect effects of IPRs may not be mutually compatible and may even be contradictory, thus it is important to discuss them separately.

Countries with weak IP capabilities may be better off not extending IP protection to foreigners. A notable example is the disclosure of information concerning the particulars of an invention by a foreign IP owner in exchange for obtaining patent protection in a developing country. Here it makes no sense for that country to grant patent protection to the foreign inventor as it can behave as a free-rider and obtain the same information from the patent office in his original home country (Grundman, 1970: 196; Subramanian, 1990: 509–521).

Empirical evidence suggests that many developing countries, particularly those with reverse-engineering capabilities, are able to copy IP-related products without relying on any disclosed data (Evenson, 1990: 325–356; Gadbow and Richards, 1988: table 1.2). Indeed, opting for patent protection may not mean that countries benefit. It is estimated that more than 90 per cent of patents granted in developing countries are not utilized, in part because information disclosed by patentees is incomplete in the sense that additional “know-how” is required for the successful exploitation of these products and processes. The same phenomenon exists in developed countries, although on a smaller scale (UNCTAD, 1975: 40; Economic Council of Canada, 1971: 62). With regard to the dynamic effects, it is highly plausible that a stronger IP environment is positively correlated with FDI and technology transfer. Many IP advocates argue that a stronger IP commitment would not only make developing countries more attractive to future technological investments but would also enhance their ability to climb up the technological ladder and become more innovative (Sherwood, 1990: 145).

But existing data do not enable one to conclude that a causal relationship exists between a stronger IP environment and greater technology transfer and FDI. Some studies argue that IPRs are extremely important to foreign technology licensing, while others conclude that the grant of such licences may take place despite weak IP protection. Views about the importance of IPRs to joint ventures and FDI also vary considerably

(Maskus and Konan, 1994: 441–446; Frischtak, 1990: 61–98; OECD, 1989; Mansfield and Lee, 1996: 181–186; United Nations, 1993). Furthermore, even in sectors where IPRs are considered essential, such as in the pharmaceutical R&D industry, it is still not possible to arrive at a method for assessing the quantity, in money terms, and quality, in innovative terms, of FDI and technology transfer decisions affected only by the level of IP protection.

In short, as in other fields of international trade, the rules on IPRs are influenced by a multitude of diverging and even conflicting interests. But the issues in the debate on IPRs are very different from those in the debate on trade policy, at the heart of which are well-known neo-liberal assumptions. As there is no a priori economic case for or against IPRs, the approach adopted here will be to focus on some of the major components of IP agreements and then try to track the political channels through which these components are translated or manifested across the multi-lateral and regional levels of international trade policy-making.

Key elements in IP rule-making

The first and most fundamental element in international IP agreements is the principle of *national treatment*, requiring member countries to treat the nationals of other countries no less favourably than their own. National treatment will thus enable foreigners to exploit their IPRs in countries other than their own. National treatment for IPRs was probably first introduced in the 1883 International Convention for the Protection of Industrial Property (Penrose, 1951; Ladas, 1975). The principle is also included in modern rules, such as article 3 of TRIPs and article 1703 of NAFTA. But national treatment is, by itself, insufficient because it only applies when countries provide protection for IP, and in many countries there are significant gaps.

There are also administrative elements in IP rules aimed at facilitating the *de facto* exploitation of property rights. The most basic requirement in this context is the establishment of an “entry point” for the registration of IPRs (patents, trademarks and plant varieties). An efficient patents and trademarks office is measured by the legal and technical expertise of its staff, as well as by its technological infrastructure. Furthermore, international IP treaties that focus on the operational dimension of IPRs at the cross-national level, such as WIPO’s Patent Cooperation Treaty (PCT),² are also heavily dependent on the effective administration and management of IPRs at the national level.

The administrative dimension of IPRs also encompasses informational and educational activities that aim to provide basic knowledge on the

different aspects of IPRs. This basic information, which deals with what is a patent, how to register a trademark, why the unauthorized copying of a disk is considered counterfeiting, etc., is pivotal to the implementation of an “IP culture”.

In this context there has been much discussion of the need to provide technical assistance to developing and least developed countries (LDCs) to help them implement IPRs. Many LDCs, as well as some developing countries, have inadequate resources and capacity. Trade agreements covering IPRs therefore often include provisions for technical assistance. There are also resources made available through WIPO, the World Bank etc. But the technical assistance provisions in IP rules, such as TRIPs article 67, are seldom seen to be binding, with the result that the level of technical assistance provided has generally been insufficient. This raises the question of what would happen if the developed countries were challenged in the WTO dispute settlement procedure for non-compliance with such measures (UNCTAD, 1996: 19–26; ESCWA, 1999: 15–20).

This brings us to the third crucial element in any IPR rules, namely *enforcement*, which typically has both domestic and international levels. The former focuses on the need to provide civil, judicial and criminal procedures in order to prevent, or at least inhibit, the infringement of IPRs. Common measures include injunctions “to prevent the entry into channels of commerce in their jurisdiction of imported goods that involve the infringement of an intellectual property right”, damages for injuries and the destruction of infringed goods without compensation of any sort (see TRIPs arts. 41–61 for the enforcement of IPRs and art. 64 for dispute settlement). Rules may also require signatories to agreements to adopt adequate border measures aimed at preventing the importation and circulation of counterfeit and pirated IP-related goods. The establishment or designation of specialized IP courts is also becoming a prerequisite in the international regulation of IPRs. At the international level it is important that IP agreements make use of consultation and coordination (such as in WIPO’s Arbitration and Mediation Centre, <http://arbitrator.wipo.int/center/index.html>) and do not “rush to court” in the form of the WTO or other dispute settlement mechanisms.

Level of protection in international IP agreements

The scope of IP rules can be represented in a three-dimensional matrix (fig. 7.1), with the X axis indicating the scope of protection, the Y axis the strength of exclusivity and the Z axis the duration of protection. The scope of protection (X axis) determines the degree of market exclusivity granted by any IPR agreement by means of national or international ex-

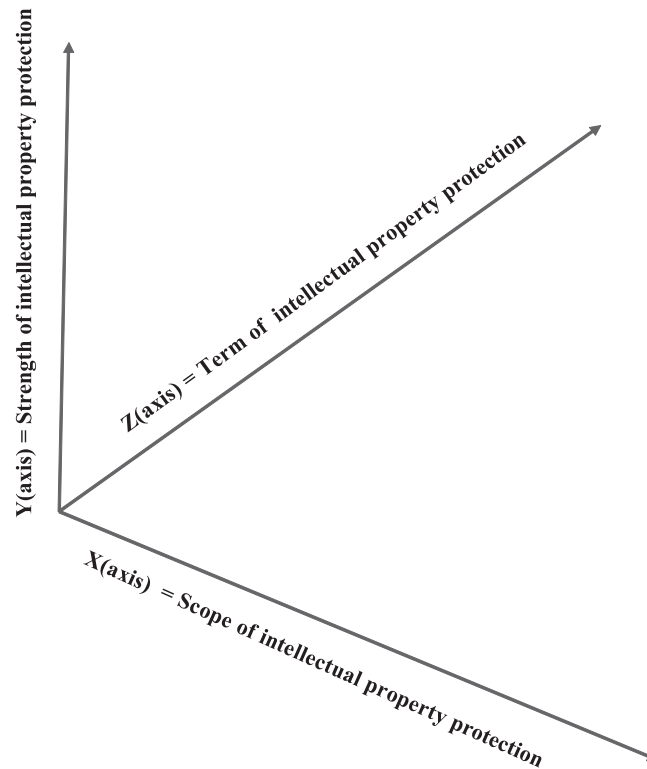


Figure 7.1 Geometric measurement of IP level of protection

haustion rules or provisions on parallel imports of IP-related products. The scope of the agreement will also be determined by whether it includes rules on competition or the anti-competitive effects of IP protection, such as in the TRIPs agreement. Finally, the scope will be determined by how broad or narrow is the definition of IPRs.

The second dimension (Y axis) concerns the *strength of exclusivity* (or the *degree of monopoly*) granted in an agreements. This dimension covers not only the strength of IP provisions *per se*, but also how easily they can be bypassed or not applied. For example, do the agreements include standards of protection that seek to close off opportunities to evade IPR protection, such as the inclusion of cyber copyrights, as in the new US Digital Millennium Copyrights Act (DMCA) aimed at preventing the downloading of songs and movies via the internet? The issue of access to essential medicines for LDCs is another example of where rules affected the ability of parties to bypass existing IP provisions. This very complicated case concerned the criterion of using compulsory licences as

a tool for overriding patented pharmaceuticals in order either to manufacture generic substitutes locally or to import/export such substitutes from/to other countries (Pugatch, 2003a: 31–41).

The strength of IP rules can also be measured by whether they allow for interpretations of their provisions that create new forms of protection for IPRs. One of the most interesting cases in this context is the extent to which trade secrets are treated as an independent and “stand-alone” form of IPRs. The best example of this is the potential use of data exclusivity provisions to protect data submitted by pharmaceutical companies to regulatory authorities for the purpose of obtaining marketing approval for new drugs (TRIPs art. 39.3). TRIPs article 39.3 did not specify a minimum or maximum period of data exclusivity (it is 10 years in the European Union and 5 years in the United States). Nor was article 39.3 clear on what use regulatory authorities may make of such data. For example, should regulatory authorities make available proprietary data from clinical or other tests of a pharmaceutical substance? Or should the use of such data be tightly restricted to (further) protect the patent holder from competition from generic products? The regulatory body may, for example, use such data in bio-equivalency tests on a generic substitute product.

The third dimension (Z axis) focuses on the *period of protection*. The most straightforward measure would be the periods of protection included any agreement (such as 20 years for patents, 50 or 70 years for copyrights and an indefinite period for trademarks). This needs, however, to be complemented by assessments of the potential extension of the basic term of protection, such as in the case of patents for pharmaceuticals and copyrights for artistic creations.

To sum up, an investigation of the trends in the rule-making in IPRs across the multilateral, regional and bilateral agreements should take into account both the composition or structure of the rules (national treatment, administrative procedures and enforcement mechanisms) and the level of IP protection as expressed by the scope, strength and term of IPRs.

Empirical analysis

Having set out the analytical framework, this section now turns to the question of the interaction between RTAs and the multilateral level of rule-making. The question that has dominated recent research in this area is the extent to which RTAs and bilateral agreements go beyond the level of protection provided by TRIPs (so-called TRIPs-plus provisions). There is growing evidence suggesting that regional and bilateral

trade agreements – between the United States and the European Union on the one hand and developing countries on the other – are based on TRIPs-plus provisions, including those in the field of data exclusivity. For example, an OECD study (2002) argues that most “RTAs dealing with intellectual property rights have more far-reaching provisions than those found in the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights”. Similarly, the World Bank (2005) finds that “in investment and intellectual property rights, North-South agreements have enjoyed considerable success in promulgating comprehensive new rules that go beyond multilateral agreements” and that the “embedded IPR in all FTAs are essentially ‘TRIPs plus’”. Other studies (Abbott, 2004; Vivas-Eugui, 2003; Roffe, 2004) have also reported that various elements of RTAs, such as patents, data exclusivity and copyrights, are TRIPs-plus.

Whilst identifying the ongoing trend towards TRIPs-plus agreements is crucial, this chapter seeks to take the analysis beyond the descriptive and look at the nature of the interaction between the multilateral, regional and bilateral levels of the international regulation of IPRs. Such an analysis might address a range of questions. In what way do regional and bilateral IP agreements differ from the multilateral level (TRIPs)? What are the differences between the US and EU approaches to strengthening the level of IP protection *vis-à-vis* developing countries? Which forms of IPRs – or more accurately knowledge subjects – are currently being strengthened? Who is driving US and EU efforts to go beyond TRIPs? Who are the main beneficiaries from the TRIPs-plus phenomenon? Has the weakening of the TRIPs agreement in the past few years benefited developing countries given that RTAs and FTAs are characterized by TRIPs-plus provisions?

Clearly, each of these questions requires substantial research which extends far beyond the scope of this chapter. Nevertheless, it is worthwhile addressing certain derivatives of these questions in order to get a clearer picture of the specific characteristics of the TRIPs-plus phenomenon. The chapter therefore looks at two elements of IPR rules that are particularly important to our understanding of the TRIPs-plus phenomenon. The first is the difference between the US and EU approaches to the protection of IPRs in regional and bilateral trade agreements. This dimension is important as it can increase our understanding of the way in which the main forces (the United States and the European Union) behind the current tendency towards TRIPs-plus wish to deal with the international regulation of IPRs. The second is the strength dimension of IP rules, which is explored by looking at the TRIPs-plus provisions on data exclusivity and patents that mostly affect pharmaceuticals, but also, though more superficially, copyrights and trademarks.

US and EU approaches to the protection of IPRs in regional and bilateral trade agreements

A comparison of US and EU approaches to IPR rules in RTAs with developing countries leads to the hypothesis that US-led RTAs and FTAs are much more detailed and comprehensive, both in terms of the agreements' structural frameworks (i.e. enforcement, administration, etc.) and the level of IP protection (relating the different forms of IPRs).

This can be illustrated by one of the most recent agreements negotiated by the United States, namely chapter 15 of the Central American Free Trade Agreement (CAFTA), negotiated in May 2004 (www.ustr.gov/assets/Trade_Agreements/Bilateral/DR-CAFTA/DR-CAFTA_Final_Texts/asset_upload_file934_3935.pdf). While the TRIPs agreement is based on the "minimum-level" approach – specifying the minimum IP commitments of WTO members – CAFTA is a "to-do list" approach (some would argue a "nanny" approach) identifying specific amendments and actions that CAFTA signatories should implement. CAFTA includes provisions on all the three structural elements mentioned above, namely national treatment, enforcement and administrative provisions.

With regard to national treatment, article 15:8 states that "in respect of all categories of intellectual property covered in this Chapter, each Party shall accord to nationals of the other Parties treatment no less favorable than it accords to its own nationals with regard to the protection and enjoyment of such intellectual property rights and any benefits derived from such rights". Article 15:9 allows signatories to derogate (text language) from the principle of national treatment in cases where it "is necessary to secure compliance with laws and regulations that are not inconsistent with this Chapter" and when it "is not applied in a manner that would constitute a disguised restriction on trade".

The enforcement rules in article 15:11 of CAFTA go to some lengths to elicit information that can facilitate effective enforcement, and require that final judicial decisions or administrative rulings of general applicability pertaining to the enforcement of IPRs shall be in writing and shall state any relevant findings of fact and the reasoning or the legal basis on which the decisions and rulings are based; each party shall publicize information that it may collect on its efforts to provide effective enforcement of IPRs; and in civil, administrative and criminal proceedings involving copyright or related rights, each party shall provide that the person whose name is indicated as the author, producer, performer or publisher of the work, performance or phonogram in the usual manner shall, in the absence of proof to the contrary, be presumed to be the designated right-holder in such work, performance or phonogram.

CAFTA signatories are required to strengthen their civil and administrative procedural remedies significantly. Special attention is given to the authority of the courts to order infringers to pay compensation to right-holders on the basis of a coherent and transparent calculation that takes into account “*inter alia*, the value of the infringed-upon goods or services based on the suggested retail price or other legitimate measure of value that the right-holder presents” (art. 15:11(7) *b*).

Articles 26 and 27 also require CAFTA signatories to strengthen their criminal remedies, such as imposing “sentences of imprisonment or monetary fines, or both, sufficient to provide a deterrent to future acts of infringement”, carrying out independent criminal investigation “without the need for a formal complaint by a private party or right holder” and granting incentives to service providers (usually internet providers) to cooperate with copyright owners in deterring the unauthorized storage and transmission of copyrighted material.

Similar comprehensive rules for the strengthening of IP protection can also be found in the US bilateral agreements with Chile (2003), Singapore (2003) and Morocco and to some extent in the US-Jordan FTA (2000).³

Compared to the United States, the IP provisions of new-generation FTAs (so-called association agreements) between the European Union and developing countries are much more general and less issue-specific. Typically EU-led RTAs (for example, EU-Israel 2000; EU-Chile 2002; EU-Jordan 2002; EU-Mexico 2001–2002) include two general provisions on the objectives and scope of the agreement’s rules on IPRs.

With regard to the objectives the EU approach requires signatories to “grant and ensure adequate and effective protection of the highest international standards including effective means of enforcing such rights”. In terms of scope the EU approach enumerates the various IPRs covered by the RTA, such as copyright, patents, industrial designs, geographical indications, trademarks, layout designs (topographies) of integrated circuits and the protection of undisclosed information.⁴

Instead of specifying the IP requirements that signatories should implement (as in the US model), EU-led FTAs specify the different agreements and treaties signatories should implement. For example, article 170(a) of the EU-Chile agreement requires signatories to “continue and ensure an adequate and effective implementation” of the obligations arising from the following (long list of) conventions: TRIPs; Paris Convention for the Protection of Industrial Property (Stockholm Act, 1967); Berne Convention for the Protection of Literary and Artistic Works (Paris Act, 1971); Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organisations (Rome, 1961);

International Convention for the Protection of New Varieties of Plants 1978 (1978 UPOV Convention) or the International Convention for the Protection of New Varieties of Plants 1991 (1991 UPOV Convention).

The EU-Chile agreement (arts 170(b) and (c)) provides a transition period for the implementation and ratification (by 2007–2009) of further conventions, such as the Nice Agreement Concerning the International Classification of Goods and Services for the Purposes of Registration of Marks (Geneva Act, 1977, amended in 1979), the World Intellectual Property Organization Copyright Treaty (Geneva, 1996), the Patent Co-operation Treaty (Washington, 1970, amended in 1979 and modified in 1984) and the Convention for the Protection of Producers of Phonograms against the Unauthorized Reproduction of their Phonograms (Geneva, 1971). Looser wording (art. 170(d)) requires signatories to implement at “the earliest possible opportunity” the Protocol to the Madrid Agreement concerning the International Registration of Marks (1989), the Madrid Agreement concerning the International Registration of Marks (Stockholm Act, 1967, amended in 1979) and the Vienna Agreement Establishing an International Classification of Figurative Elements of Marks (Vienna 1973, amended in 1985).

Finally, unlike the US model, EU-led RTAs do not have detailed provisions on enforcement, civil and criminal remedies or administration. Some EU-led agreements, such as the EU-Jordan RTA, provide for consultation. “If problems in the area of intellectual, industrial and commercial property affecting trading conditions . . . occur, urgent consultation shall be undertaken, at the request of either Party, with a view to reaching mutually satisfactory solutions” (EU-Jordan Association Agreement 2002, art. 56).

There are specific cases, however, in which the European Union has gone beyond the above pattern to demand a higher level of IP protection from its trading partners based on the EU standard of protection. For example, the Partnership and Co-operation Agreement (PCA) between the EU and Ukraine (1998) requires the latter to implement IP protection standards similar to that existing in the European Union by the end of 2003 (http://europa.eu.int/comm/trade/issues/bilateral/countries/ukraine/index_en.htm). It states, for example, that Ukraine “shall continue to improve the protection of intellectual, industrial and commercial property rights in order to provide, by the end of the fifth year after the entry into force of the Agreement for a level of protection similar to that existing in the Community, including effective means of enforcing such rights”. But even here the EU approach is based on existing international standards, and requires that “by the end of the fifth year after entry into force of the Agreement, Ukraine shall accede to the multilateral conven-

tions on intellectual, industrial and commercial property rights (referred to in Paragraph 1 of Annex III) to which Member States are parties or which are de facto applied by the EU Member States” (art. 50).

It should also be noted that the European Commission, perhaps mindful of the EU’s weakness in this field, is interested in becoming more proactive in the enforcement of IPRs internationally. For example, in June 2004 the European Commission (2004a) issued its new proposed strategy for the enforcement of IPRs in third countries. *Inter alia*, the Commission proposes to make a more active use of the EC’s Trade Barriers Regulation (TBR) mechanism in cases where the IP interests of European right-holders are compromised. The Commission’s position argues that:

no rule can be really effective without the threat of a sanction. Countries where IP violations are systematic could be publicly identified. As a last resort, consideration should be given to resorting to dispute settlement mechanisms provided for in multilateral and bilateral agreements. The existing Trade Barriers Regulation (TBR) mechanism could be a starting-point. TBR is a legal instrument that gives the right to Community enterprises and industries to lodge a complaint, which obliges the Commission to investigate and evaluate whether there is evidence of violation of international trade rules resulting in adverse trade effects. The result is that the procedure will lead to either a mutually agreed solution to the problem or recourse to dispute settlement. (European Commission, 2004a: 11)⁵

This new EU IP enforcement strategy was officially launched on 10 November 2004 and advocated by Trade Commissioner Pascal Lamy (European Commission, 2004b). This tougher policy has been used *vis-à-vis* Turkey (see below) and Israel.⁶

Level of IP protection in regional and bilateral trade agreements

A central question for this study is which elements of IP protection in RTAs go beyond TRIPs rules. There are three particular types of knowledge subjects (or fields of technology) that have been subject to a significant strengthening of IPRs at the regional level: data exclusivity and patents for pharmaceutical products and regulatory data; copyrights and related rights for artistic works and creations (music, software, books, etc.); and trademarks and geographic indications (GIs) as information for consumers on goods and services. Of these three, pharmaceutical IPRs remain the most contentious. Since TRIPs was adopted the controversial issue of access to patented medicines in developing countries and LDCs has been high on the agenda, and at times the only item on the ne-

gotiation table. Indeed, since the failure of the Seattle WTO ministerial at the end of 1999 and the much-publicized dispute over patented AIDS medicines in South Africa (2001), TRIPs has become more or less synonymous with pharmaceutical patents. The heated debate on pharmaceutical IPRs has at least temporarily paralysed the TRIPs agreement as a vehicle for negotiating, amending and even expanding other forms of IPRs. At the same time, and as elaborated below, US-led RTAs strengthened the IP provisions for pharmaceutical products and regulatory information to an extent that they may be considered “TRIPs-double-plus” agreements.

Data exclusivity and pharmaceutical patents

Data exclusivity

Data exclusivity is one of the most burning issues in the current discussion on pharmaceutical IP policy-making. Data exclusivity rules seek to protect and safeguard pharmaceutical registration files, which contain data submitted by pharmaceutical companies to regulatory authorities, such as the US Food and Drug Administration (FDA) and the European Agency for Evaluation of Medicinal Products (EMA), for the purpose of obtaining marketing approval for new drugs.⁷

Proponents of data exclusivity consider it an integral and inseparable part of the IP protection for pharmaceutical products, while opponents argue that it simply extends a monopolistic patent system. Data exclusivity rules are rapidly becoming a North-South issue, as they are being fiercely advocated by multinational research-based pharmaceutical companies operating in developing countries such as Israel, Jordan, Turkey, India and Thailand.

The underlying logic of data exclusivity suggests that it is an expression of trade secrets, and that as such data exclusivity should be independent of patents. Compared with patents, the market power of data exclusivity is, in theory, less restrictive, mainly because it does not legally prevent other companies from generating their own registration data. However, in practice the vast financial resources and extended time required for gathering and generating pharmaceutical registration data for a new drug create a market barrier that is too high for generic-based pharmaceutical companies.

The data included in the registration file of a pharmaceutical product are disclosed to the drug/health regulatory bodies. Without these data a drug cannot be approved for market use. “Unfair commercial use” of these data by the regulatory body can be prevented by rules on non-

disclosure designed to ensure that rival companies (usually generic companies) do not gain access to the registration file of the original product.

Less obvious are rules on non-reliance that aim to prevent the regulatory bodies themselves from relying on the registration file of an original in order to compare it to the chemical and toxic levels of a potential generic substitute (so-called bio-equivalence tests). The issue of non-reliance can be further complicated by issues of direct and indirect reliance or active and passive reliance. Suffice it to say that there are different views on how to interpret these rules: the United States and the European Union argue that any form of reliance is prohibited, while some countries, such as Canada, have a more nuanced view.

The TRIPs agreement (art. 39.3) states that “WTO members, when requiring, as a condition of approving the marketing of pharmaceutical or of agricultural chemical products which utilize new chemical entities, the submission of undisclosed test or other data, the origination of which involves a considerable effort, shall protect such data against unfair commercial use. In addition, Members shall protect such data against disclosure, except where necessary to protect the public or unless steps are taken to ensure that the data are protected against unfair commercial use.”

However, TRIPs rules leave three major issues unresolved. First, it does not specify the minimum period of data exclusivity required by WTO members (as discussed below, the term of data exclusivity in Europe and the United States is 10 and 5 years respectively). Second, TRIPs is ambiguous on the question of when a member country may choose to rely on the proprietary information of the original product in order to compare it to the chemical and toxic levels of a potential generic substitute (via the so-called bio-equivalence tests). Finally, it is not clear what types of activities are within the scope of “considerable efforts”.

In comparison, the equivalent rules at the national level are more clear-cut. Section 355 of the Federal Food, Drug, and Cosmetic Act of 1997 (25 USC 305(c)(D)(ii–iii), www.fda.gov/opacom/laws/fdcact/fdcact5a.htm) provides a five-year period of data exclusivity for new drugs and three years for new indications (or uses) of existing drugs. The EU rules in the upgraded directive 2001/83/EC provide a data exclusivity period of 10 years (or more accurately adopted the 8+2+1 formula: 8 years data exclusivity, 2 years of marketing exclusivity and an additional year of protection for new indications of existing products).⁸

Given the ambiguity in TRIPs rules the United States has been pushing for stronger and clearer rules in RTAs/bilateral agreements. Following the provisions in article 1711 of NAFTA, the United States has included protection of data exclusivity in RTAs. For example, article 15:10 of CAFTA requires a minimum five-year period for data exclusivity, non-disclosure and non-reliance, including cases in which marketing

authorization was granted to a third party in another country (www.ustr.gov/assets/Trade_Agreements/Bilateral/DR-CAFTA/DR-CAFTA_Final_Texts/asset_upload_file934_3935.pdf). Article 17:10 of the US-Chile FTA (2003) places similar mechanisms of data exclusivity (five years, non-reliance/non-disclosure), as does article 16:8 of the US-Singapore FTA (2003) and article 17.1 of the US-Australia FTA (2004).⁹ That said, as Roffe indicates, the data exclusivity provisions between the United States and developing countries are not identical (Roffe, 2004: 49–53). Variations are either a result of the United States becoming more specific over time (for example, the difference between US-Jordan and US-Singapore) or the ability of developing countries, such as Chile, to limit some of the US demands.

The United States has also used the threat of trade retaliation when the absence of data exclusivity legislation has resulted in a serious commercial clash between the local subsidiaries of (US-owned) research-based multinational pharmaceutical companies and local “national champion” generic companies. Such a clash occurred in Israel, where the multinational research-based pharmaceutical industry, backed by the US trade representative (USTR), clashed with the local generic industry, represented by Teva – the biggest generic multinational pharmaceutical company in the world (Gabizon, 2004). Lack of data exclusivity in Israel caused considerable commercial losses when, according to Pharma-Israel, the trade association representing multinational research-based pharmaceutical companies operating in Israel, at least 15 original products registered in Israel were almost immediately exposed to generic competition due to the absence of data exclusivity (Pharma-Israel, 2003: 15).¹⁰ The USTR argues that “although Israel has been obligated since January 1st 2000 to provide data exclusivity, it has failed to do so. This policy places it at odds with other OECD-level economies and many of its neighbors that have met their TRIPs Article 39.3 obligations” (www.ustr.gov/reports/2003/special301-wl.htm#israel).

Pressure from the United States and the research-based pharmaceutical lobby resulted in the adoption of a data exclusivity bill in September 2004 (Manor, 2004; Wagner, 2004; *The Marker*, 2004). But the USTR argued that the bill still does not meet the minimum US standard (USTR, 2004). Roffe (2004: 49) reports similar USTR pressure on the Chilean government and the pharmaceutical MNCs during the final phase of the FTA negotiations between the United States and Chile.

The European Union, on the other hand, seems to avoid referring to the issue of data exclusivity in its bilateral and regional negotiations. This is somewhat surprising given the fact that, as discussed earlier, the level of EU data exclusivity is much higher than that of the United States. A notable exception to this lax approach was the investigation by

the European Commission of Turkish rules following a 2003 complaint by the European Federation of Pharmaceutical Manufacturers and Associations (EFPIA). The investigation concerned obstacles to trade allegedly caused by Turkish practices and measures involving lack of transparency and discriminatory application of the pharmaceutical import, sales and marketing system, including a “lack of protection of commercially sensitive data submitted as part of the marketing approval procedure” (European Commission, 2003).

Pharmaceutical patents

On pharmaceutical patents the multilateral level (TRIPs) and the bilateral and regional levels show opposite trends. Since 2000 the TRIPs patent regime has been becoming weaker, and the 2001 Doha ministerial declaration on TRIPs and health has led to a reduction in the protection of patented medicines (WTO, 2001). Perhaps the most important element of this declaration is the overall statement in paragraph 4, which reads:

We agree that the TRIPs Agreement does not and should not prevent members from taking measures to protect public health. Accordingly, while reiterating our commitment to the TRIPs Agreement, we affirm that the Agreement can and should be interpreted and implemented in a manner supportive of WTO members’ right to protect public health and, in particular, to promote access to medicines for all. In this connection, we reaffirm the right of WTO members to use, to the full, the provisions in the TRIPs Agreement, which provide flexibility for this purpose.

On the specifics the Doha Declaration provides for compulsory licences, without preconditions, in times of national emergency (to be determined by each and every member; arts. 5b–c); reaffirms the right to adopt the principle of international exhaustion, i.e. to deal with the parallel importation of patented medicines (art. 5a); and grants LDCs an additional period of 10 years to implement their patent obligations under the TRIPs agreement (art. 7).

The Doha Declaration also acknowledged that countries with insufficient manufacturing capabilities would not be able to use the tool of compulsory licences (which would allow local companies to manufacture original patented drugs). It instructed the council for the TRIPs agreement to find an expeditious solution to this problem by the end of 2002. In reality, it took the WTO almost two years (until September 2003) of political negotiations to reach a solution on this issue (in its official title, “Implementation of Paragraph 6 of the Doha Declaration on the TRIPs

Agreement and Public Health”, WT/L540, dated 2 September 2003). A detailed analysis and discussion of this deal, which according to this author’s view is not very practical, is provided in Pugatch (2003a).

In stark contrast to this softening of TRIPs, US-led FTAs have been establishing higher levels of pharmaceutical patent protection than TRIPs, such as by imposing restrictions on signatories’ patent laws that permit commercial experiments in patented pharmaceutical drugs as part of the process of obtaining marketing approval for a generic substitute (so-called Bolar provisions). These restrictions aim to prevent a local interpretation of rules that would allow generic-based companies to produce or market, domestically and abroad, any substitutes for the original prior to patent expirations.

For example, as article 15.9:5 of CAFTA states:

if a Party permits a third person to use the subject matter of a subsisting patent to generate information necessary to support an application for marketing approval of a pharmaceutical or agricultural chemical product, that Party shall provide that any product produced under such authority shall not be made, used, or sold in the territory of that Party other than for purposes related to generating information to meet requirements for approval to market the product once the patent expires, and if the Party permits exportation, the product shall only be exported outside the territory of that Party for purposes of meeting marketing approval requirements of that Party.

RTAs are also TRIPs-plus in the sense that they allow pharmaceutical patent owners to extend the term (period) of their patent protection in two instances. First is if there was an unreasonable delay in the process of granting a pharmaceutical patent by the authorities. An unreasonable delay is usually defined as “a delay in the issuance of the patent of more than five years from the date of filing of the application in the territory of the Party, or three years after a request for examination of the application has been made” (art. 15.9:6a of CAFTA; art. 17.9:6 of the US-Chile FTA; or four years and two years respectively in art. 16.7:7 of the US-Singapore FTA). Second is when there is “unreasonable curtailment of the effective patent term resulting from the marketing approval process related to the first commercial marketing of the pharmaceutical product” (CAFTA, art. 15.9.5b). In other words, if there is an unreasonable delay in the process of authorizing a patented drug for market use, which in turn shortens the effective term of protection, the patent owner should be compensated by extending the patent term.

This desire to extend patent life clearly derives from domestic policy in the European Union and the United States, where a pharmaceutical patent may be extended by an additional period of up to five years. In the European Union, regulation EC 1768/92 allows such an extension as long

as the effective patent life does not exceed 15 years from the date of marketing authorization; this mechanism is called a supplementary protection certificate or SPC (Council of the European Communities, 1992). In the United States the 1984 Drug Price Competition and Patent Term Restoration Act (known as the Hatch-Waxman Act) increased the effective patent term of protection by an additional maximum period of five years (Mossinghoff, 1999: 187–194; Grabowski and Vernon, 1986: 195–198). These policies aim to allow originators to extend the effective term of patent protection for a new pharmaceutical product, given the gap between the time a patent is granted for a new substance and the time the drug is authorized for marketing.

A further example of TRIPs-plus provisions in RTAs allows pharmaceutical patent owners the right to prevent parallel trade in patent pharmaceutical products (US-Singapore, art. 16.7.2; US-Australia, art. 17.9.4; US-Morocco, art. 15.9.4). Activity of this kind relates mostly to the importation of patented pharmaceutical products from low-price countries into high-price countries through channels other than those authorized by the local patentee or licensee. This is a significant extension of the scope of the rules and is in stark contrast to the principle of international exhaustion of IPRs outlined in TRIPs.

In order to make the global parallel import of a patented pharmaceutical legal, countries must adopt the principle of international exhaustion. This provides that once a patentee has sold his product in one country, he has exhausted his right to prevent the resale of that product to other countries. Though not explicitly recognizing the principle of international exhaustion, the TRIPs agreement (art. 6) essentially allows for parallel imports to take place by denying members the possibility of bringing cases concerning international exhaustion to WTO dispute settlement. As previously explained, the ability of WTO members to adopt a regime of parallel imports was further strengthened by the Doha ministerial declaration on public health (2001).

As in the case of data exclusivity, EU-based RTAs are silent on parallel importation. Indeed, in October 2004 the European Union moved to implement the WTO paragraph 6 deal by proposing new regulations to allow generic pharmaceutical companies to produce and export patented medicines to countries without sufficient manufacturing capacity (European Commission, 2004c).

It is now possible to produce a comparison between the TRIPs agreement and US-led and EU-led RTAs in the field of pharmaceutical IPRs based on the analytical framework discussed above. Figure 7.2 provides a pictorial representation of this comparison, showing US-led RTAs placed highest in all of the three dimensions (term, strength and scope) of pharmaceutical IP protection. The TRIPs agreement and EU-led RTAs are

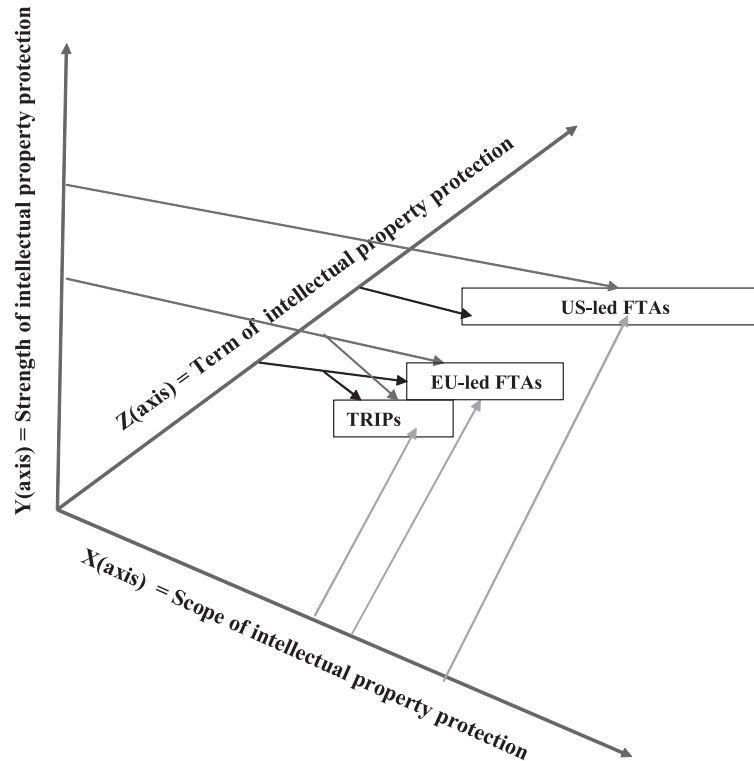


Figure 7.2 Pharmaceutical IP level of protection: Geometric comparison between the TRIPs agreement, US-led and EU-led RTAs and FTAs

closer together, although one might argue that EU-led RTAs might move higher if EU policy on enforcement of IPRs is strengthened.

Although not within the scope of this chapter, it would be very interesting to explore possible explanations for this difference in approach between the United States and the European Union on enforcement of pharmaceutical IPRs. Both are strong supporters of IPRs, and in some cases EU domestic protection exceeds that of the United States. Indeed, until 2000 the European Union was an active player in strengthening and enforcement of pharmaceuticals IPRs, such as in the case of the WTO dispute between the European Union and Canada on the issue of commercial testing of patented pharmaceuticals (the so-called Bolar provisions) and stockpiling (Pugatch, 2004).

Since the Doha Declaration of 2001 the United States has become more hawkish on pharmaceutical IPRs. This may be due to lobbying by the domestic pharmaceutical lobby in the United States (PhRMA). It is possible that after their relative failure in Doha pharmaceutical multi-

nationals decided not to sit quietly and watch their commercial interests be sacrificed, again, for the sake of world trade solidarity and put heavy pressure on the US government to reinforce pharmaceutical IP rules. For example, a typical article by the *Wall Street Journal* argued that “pharmaceutical companies shelled out some \$63 million to help Republicans win control of the US Congress last November”, and that “days after the election, when international trade talks threatened their profitable drug patents, the companies quickly sought help from Republicans and they got it” (Hamburger, 2003).

Copyrights and trademarks

US-led FTAs pay specific attention to copyright provisions, perhaps more than any other IP form (even patents). As a full treatment of copyrights is beyond the scope of this chapter, it provides illustrations of major provisions in RTAs drawn from two recent in-depth studies of IP provisions in US-Chile (Roffe, 2004: 53–66) and the prospective FTAA (Vivas-Eugui, 2003: 29–36). These studies suggest that, as in the case of pharmaceuticals, US-led RTAs extend the level of copyright and trademark protection beyond TRIPs.

US-led RTAs are TRIPs-plus in three main areas. First, they strengthen the ability of copyright-holders to prevent the reproduction of their works “in any manner or form, permanent or temporary (including temporary storage in electronic form)”. The wording “electronic form” used in the various US-led RTAs is of particular importance, as it allows right-holders to control the reproduction of their work – such as software – via temporary electronic copies (art. 15:5.1 of CAFTA; art. 17.7:3 of the US-Chile FTA; art. 16.4:1 of the US-Singapore FTA).

Second, US-led RTAs extend the term of copyright protection to a period that is equal to the author’s life plus 70 years from the time of his death, or in cases of works generated by legal entities (such as software), the period is set to 70 years from the end of the calendar year of the first authorized publication of the work (art. 15.5:4, CAFTA). In comparison, the related copyright terms in TRIPs (art. 12) are calculated on the basis of 50 years.

Third, the US-led RTAs set strict rules against the circumvention of technological protection measures (TPMs) used by authors, performers etc. to protect copyrighted works. For example, CAFTA requires each “to provide that any person who ... circumvents without authority any [TPM] ... shall be liable and subject to the remedies provided for in Article 15.11.14” (art. 15.5:6). These include criminal procedures and penalties. This provision is based on the 1998 US DMCA, which is considered

one of the most controversial laws to be adopted by the US Congress. One of the most celebrated cases concerning the use of the DCMA is the arrest and trial of a Russian computer scientist who in 2001 submitted a technical paper at a conference in Las Vegas which demonstrated that it is possible to develop a code for bypassing the copy protection features of Adobe's e-book software.

Further obligations concerning copyrights and related rights include provision of rights management information (RMI) and protection of satellite signals and internet domain names.

The European Union, in comparison, adheres to the multilateral approach. As mentioned earlier, a typical EU-led RTA requires signatories to accede to and ensure adequate and effective implementation of the obligations arising from a number of agreed multilateral conventions, such as the 1996 WIPO Copyright Treaty (WCT) and the WIPO Performances and Phonograms Treaty (WPPT) by January 2007, and the 1971 Convention for the Protection of Producers of Phonograms against the Unauthorized Reproduction of their Phonograms by January 2009.

Trademarks

US-led RTAs are also TRIPs-plus on trademark protection. First, they extend the types of identifying marks that are eligible for trademark registration. For example, article 15.2:1 of CAFTA states that "each Party shall provide that trademarks shall include collective, certification and sound marks, and may include geographical indications and scent marks". Similar provisions exist in the US-Chile FTA (art. 17.2:1), the US-Singapore FTA (art. 16.2.1) and the US-Jordan FTA (art. 4.6).

Second, US-led RTAs strengthen the demand that a trademark shall not be unjustifiably encumbered by special requirements, such as use with another trademark or the use of the trademark in a special form or manner. This requirement, which is particularly relevant to branded pharmaceutical products, builds on article 20 of TRIPs. Pre-TRIPs legislation in several developing countries sought to reduce the distinctiveness of branded pharmaceutical trademarks; for example, Brazil required that trademarks of branded pharmaceutical products be smaller than the name of the generic substance. TRIPs article 20 prohibits such measures, but in cases where foreign branded products are produced locally, article 20 does not allow WTO member governments to demand that trademarks of such products be accompanied by the names of the local producing companies.

The wording of RTA provisions places further restrictions by stating that "pursuant to Article 20 of the TRIPs Agreement, each Party shall

ensure that its provisions mandating the use of a term *customary in common language as the common name* for a product including, *inter alia*, requirements concerning the relative size, placement, or style of use of the trademark in relation to the common name, do not impair the use or effectiveness of a trademark used in relation to such products” (CAFTA, art. 15.2:2; US-Chile FTA, art. 17.2:1; US-Singapore FTA, art. 16.2.6; US-Morocco FTA, art. 15.2:3). However, these provisions also usually state they are not intended to affect the use of common names of pharmaceutical products in prescribing medicine, i.e. preventing physicians from using the common pharmaceutical name (usually by stating the active ingredient) when prescribing a drug.

Third, US-led RTAs extend the renewal period of trademark registration to a period of no less than 10 years (as a standard; trademarks can be reviewed indefinitely). The renewal period of TRIPs is no less than seven years (art. 18).

Finally, US-led RTAs strengthen the protection of well-known marks by stating that “Article 6bis of the *Paris Convention for the Protection of Industrial Property* (1967) (Paris Convention) shall apply, *mutatis mutandis*, to goods or services that are not identical or similar to those identified by a well-known trademark, whether registered or not, provided that use of that trademark in relation to those goods or services would indicate a connection between those goods or services and the owner of the trademark, and provided that the interests of the owner of the trademark are likely to be damaged by such use” (CAFTA, art. 15.2:5; US-Chile FTA, art. 17.2:7; US-Singapore FTA, art. 16.2.4; US-Morocco FTA, art. 15.2:6).

The European Union takes the same multilateral approach in the case of trademarks (referring to the need to adhere to multinational treaties), but it is much more specific on the issue of geographic indicators. For example, Roffe (2004: 17–18) finds that, as regards the EU-Chile FTA, “probably, the most significant intellectual property related provisions are contained in Annex V, on the ‘Agreement on the Trade in Wines’ and Annex VI concerning Spirits. These annexes include provisions on the reciprocal protection of geographical indications related to wines and spirits, and the protection of traditional expressions (of both Parties).” He concludes that “the Association Agreement between Chile and the EU is also a TRIPs-plus Agreement especially on the protection of geographical indications”.

Based on the above analysis, table 7.1 compares US-led and EU-led RTAs. Again, the comparison is based on the analytical framework set out above, including the structural elements (enforcement and administration) and the level of IP protection (scope of monopoly, strength of monopoly and term of protection). The table uses TRIPs as the baseline

Table 7.1 Level of IP protection in US-led and EU-led regional and bilateral agreements

	US-led RTAs and FTAs	EU-led FTAs and RTAs
Approach to the protection of IPRs	To-do list, “nanny approach”	Incorporating international treaties
New “standard” agreement on IP protection	Chapter 15 of the Central American Free Trade Agreement (CAFTA) May 2004	Association agreements – perhaps the Euro-Mediterranean Association Agreement; EU-Chile FTA; Partnership and Co-operation Agreement (PCA) EU-Ukraine
Enforcement provisions	1	No reference (with the exception of Ukraine)
Administration procedures	1	No reference
Data exclusivity (pharmaceuticals)	Scope of monopoly = 1 Strength of monopoly = 1 Term of protection = 1	Scope of monopoly = 0 Strength of monopoly = 0 Term of protection = 0
Patents (pharmaceuticals)	Scope of monopoly = 1 Strength of monopoly = 1 Term of protection = 1	Scope of monopoly = 1* Strength of monopoly = 0 Term of protection = 0
Copyrights	Scope of monopoly = 1 Strength of monopoly = 1 Term of protection = 1	Scope of monopoly = 1* Strength of monopoly = 1* Term of protection = 0
Trademarks	Scope of monopoly = 1 Strength of monopoly = 1 Term of protection = 1	Scope of monopoly = 1* Strength of monopoly = 0 Term of protection = 0
Geographical indications	Scope of monopoly = 0 Strength of monopoly = 1 Term of protection = 1	Scope of monopoly = 1 Strength of monopoly = 1 Term of protection = 1

* By reference to international treaties.

and attaches ordinal values to the different agreements. Ordinal values vary between 1 (TRIPs-plus), 0 (TRIPs equivalent) and –1 (TRIPs-minus).

Conclusion and suggestions for further research

This chapter addressed the question of the implications of the TRIPs-plus phenomenon on the international regulation of IPRs. It did so by first seeking to capture the theoretical components of the international regulation of IPRs and then by empirical investigation of characteristics of the TRIPs-plus phenomenon in recent RTAs.

Based on this analysis, the chapter suggests the following insights.

- The TRIPs-plus phenomenon is primarily driven by the United States, which is pursuing a more “hands-on” strategy with regard to the international regulation of IPRs at the regional/bilateral levels.
- The EU’s tendency to incorporate international conventions and treaties in its regional and bilateral agreements suggests that the European Union still favours the multilateral approach. That said, on the issue of GIs the EU’s approach is more proactive and specific, hence closer to the US approach.
- It is possible that the United States has grown “weary” of TRIPs (despite the fact it was the main force which sought to establish it in the first place) and does not currently intend to use it as the major mechanism and institution for the regulation of IPRs internationally. It should be noted that this statement is not based on any formal indication by either US government officials or business lobby groups. It is merely a deduction on the current state of affairs in the field of international trade negotiations.
- Although common wisdom suggested that a weaker TRIPs would serve the interests of developing countries, the recent surge in US-led TRIPs-plus agreements at the bilateral/regional levels suggests that weakening TRIPs (particularly in pharmaceuticals) was counterproductive. In this sense one might argue that the developing countries (and NGOs) which lobbied to make TRIPs more flexible have been “too effective”.
- A decade has passed since TRIPs entered into force, but rule-making in IPRs and related subjects remains to a large extent a “North-North” agenda. Subjects such as traditional knowledge, which may be categorized as a “South-North” agenda in the sense that they may benefit developing countries and LDCs, are lagging behind the more advanced technological issues, such as the internet, file sharing, encryption programmes and satellite broadcasting.
- IPR rule-making will in the future probably focus more on implementation and enforcement of IP protection in developing countries than on technical, technological and financial assistance. Not only do US-led RTAs contain extensive procedural measures that allow the United States to monitor rule implementation closely, but the European Union is also becoming more aware and active in enforcement of IP rights. Indeed, the EU’s strategy for the international enforcement of IPRs is one of the most important and comprehensive recent developments in the field.

Some of the above propositions are controversial and will require further work to confirm or disprove them. The evidence, however, clearly shows that the TRIPs-plus measures are not only procedural – that is, to do with administrative requirements – but also increase the level of IP

protection in a substantive sense. This is particularly evident in the area of pharmaceutical IPRs, copyrights and enforcement (in US-led FTAs).

This leads one to pose another more fundamental question: what explains the current tendency towards the TRIPs-plus regulation of IPRs or, more accurately, who or what are the main driving forces behind it?

Here we will have to rely on an international political economy (IPE) analysis that focuses on the linkage between the different interests and goals of specific groups (corporate, NGOs, consumers and even decision-makers and politicians) and international IP systemic outcomes. An IPE approach treats the international regulation of IPRs as an ongoing battlefield of interests, such as between those who create knowledge on the one hand and those who consume it on the other. Accordingly, it does not take the international system of IPRs for granted; rather, it explores and unveils the political route by which such a system is constituted and associates its outcome to the particular interests of different groups. By doing so we can increase our understanding of the ways in which IPRs are established, managed and exploited at the international, regional and bilateral levels.

In fact, it is this author's view that the IPE of IPRs is a necessary stage between the economic study of IPRs and the legal interpretation of such rights. In other words, placing IPRs in a political context enables us to understand the process by which economic interests are translated into legal realities. For example, let us assume there is a linkage between the recent US-led regional/bilateral trade agreements that grant stronger patent protection and data exclusivity for pharmaceutical products and the weakening of TRIPs, particularly after the 2001 Doha Declaration on TRIPs and public health and the patents deal of 30 August 2003. Our starting point in this case would be to identify first whose economic interests are being served or compromised (pharmaceutical companies). Subsequently we have to track the political process through which this pattern has emerged (for example, a stronger stand by the USTR). Finally, we should also focus on the extent to which institutional mechanisms (such as domestic regulations) are either used or modified in order to allow for the above outcome to occur. Indeed, this chapter briefly indicated that one plausible explanation for the US hawkish approach towards the protection of pharmaceutical IPRs lies in the actions and lobbying activities of research-based multinational pharmaceutical companies. It would also be interesting to investigate whether the difference between the US and EU approaches in this issue can be explained by the different behaviour and strategies of pharmaceutical trade associations in the United States and the European Union (the PhRMA and EFPIA, respectively).

By shifting our attention from the descriptive and analytical levels of the TRIPs-plus phenomenon to the explanatory level, we will be able to

learn more about its implications for the international regulation of IPRs and its consequences for developed and, more importantly, developing countries. Perhaps the most important lesson in the analysis of regional/bilateral IP-related agreements is that demands by developing countries to make the TRIPs agreement more flexible resulted in “too much” flexibility, and that this in turn led the United States, and to an extent the European Union, to fill in the void using regional and bilateral tools.

Notes

1. Data from 1996 suggest that developed countries owned 95.5 per cent of patents granted to foreigners in that year.
2. The PCT makes it possible to seek patent protection for an invention simultaneously in each of a large number of countries by filing an “international” patent application. For an overview of the PCT see www.wipo.int/pct/en/treaty/about.htm.
3. US-Chile FTA, chapter 17, www.ustr.gov/assets/Trade_Agreements/Bilateral/Chile_FTA/Final_Texts/asset_upload_file912_4011.pdf; US-Singapore FTA, chapter 16, www.mti.gov.sg/public/PDF/CMT/FTA_USSFTA_Agreement_Final.pdf; US-Morocco FTA, chapter 15, www.ustr.gov/assets/Trade_Agreements/Bilateral/Morocco_FTA/Final_Text/asset_upload_file797_3849.pdf; US-Jordan FTA, article 4, www.ustr.gov/assets/Trade_Agreements/Bilateral/Jordan/asset_upload_file250_5112.pdf.
4. EU-Israel Association Agreement (2000), chapter 4, http://europa.eu.int/eur-lex/pri/en/oj/dat/2000/l_147/l_14720000621en00030156.pdf; EU-Jordan Association Agreement (2002), article 65; EU-Chile Association Agreement (2002), title VI, article 168, http://europa.eu.int/comm/trade/issues/bilateral/countries/chile/euchlagr_en.htm.
5. Legislation concerning the Trade Barriers Regulation can be found in Council Regulation (EC) No 3286/94 of 22 December 1994, laying down Community procedures in the field of the common commercial policy in order to ensure the exercise of the Community’s rights under international trade rules, in particular those established under the auspices of the WTO. Available at www.europa.eu.int/comm/trade/issues/respectrules/tbr/legis/adgreg06a.htm.
6. European Commission, Directorate General for Trade. Letter to the Ministry of Trade, Industry and Labour, Israel (Brussels, 6 December 2004), Trade/D2/GP/pg, D(2004) 16226, in author’s records.
7. For a review of data exclusivity see Pugatch (2003b, 2004).
8. *Legislative Resolution on the Common Position Adopted by the Council with a View to Adopting a European Parliament and Council Regulation Laying Down Community Procedures for the Authorisation and Supervision of Medicinal Products for Human and Veterinary Use and Establishing a European Medicines Agency*, 10949/2/2003 – C5-0463/2003 – 2001/0252(COD), Strasbourg, December 2003, P5_TA-PROV(2003)0577; Directive 2001/83/EC of the European Parliament and of the Council of 6 November 2001 on the Community Code Relating to Medicinal Products for Human Use, *Official Journal of the European Communities*, 28 November 2001, L 311/67.
9. US-Chile FTA, note 3 above; US-Singapore FTA, note 3 above; US-Australia Free Trade Agreement, chapter 17, www.ustr.gov/assets/Trade_Agreements/Bilateral/Australia_FTA/Final_Text/asset_upload_file469_5141.pdf.
10. The following question was presented to member companies: “How many products that rely on effective data exclusivity (i.e. that would otherwise face generic competition due to the lack of data exclusivity) were registered in Israel?”

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International investment rules

Joakim Reiter

Introduction

Few international economic policy issues in the post-war era have been as contentious as investment. Investment in a broad sense (ranging from enterprises to equity and payments), and the right to control foreign investment more specifically, were long considered to lie at the very heart of sovereign policy-making. Up until the 1980s most, if not all, countries made extensive use of restrictions on foreign investment. In developed countries capital and exchange controls were part and parcel of the fixed exchange rate system under the Bretton Woods system. In the developing world protectionism was further fuelled by the process of decolonization, by which newly liberated countries nationalized many foreign-owned investment assets.

Since the 1980s there has been an almost complete reversal of these post-war policies. Providing an open and predictable investment regime has come to dominate the domestic reform agenda. While portfolio and other short-term flows are still treated with some suspicion in countries that are vulnerable to or have suffered from recent financial crises, foreign direct investment (FDI) has been wholeheartedly welcomed.

These unilateral policy changes have found their way into international rule-making, particularly through bilateral investment treaties (BITs), which quintupled during the 1990s. These have given rise to a patchwork of an international legal framework governing investment. At the multi-lateral level some investment-related issues were included in the global

trading system in the mid-1990s, but proposals for comprehensive multilateral agreement on investment have encountered determined opposition. Regional trade agreements (RTAs), and in particular investment provisions in RTAs (investment RTAs), stand at the crossroads of these two contradictory developments. Negotiating investment provisions in RTAs, therefore, requires policy-makers to find a path between expanding the rights of investors in line with the spirit of BITs and retaining the policy autonomy facilitated by the limited scope of multilateral rules. For most developed capital-exporting countries the decision should be straightforward. But the present surge in investment RTAs has raised questions for developed and developing countries alike.

Against this dualistic and contradictory environment, this chapter seeks to shed light on the choices made for, and critical developments in, the investment rules in RTAs. At the heart of the historically evolutionary analysis presented here lie the broader issues affecting both domestic politics and the emerging governance structures for investment, such as accountability, diversity and synergies between the various levels in investment rule-making.

Towards a patchwork investment regime

Given the ample transnational investment rules and regulations, the lack of a comprehensive multilateral framework does not *per se* preclude the existence of a global regime. But perhaps the best way of describing the evolving and emerging international legal framework governing investment is as a patchwork of international investment agreements on different levels.

This patchwork consists of a set of norms, principles and regulations in the form of:

- BITs
- regional (and bilateral) trade agreements
- plurilateral codes and decisions in the OECD
- multilateral rules under GATT/WTO and non-binding codes in the UN system.

All these agreements reflect, in one way or another, the internationalization of the domestic investment policy agenda.¹ In order to understand the context within which the new investment RTAs have evolved, this section first deals with the other three levels of investment rule-making.

The unprecedented success of BITs

The proliferation of BITs has been nothing less than remarkable. While BITs have their historical origin in the Treaties on Friendship, Com-

merce and Navigation, they were the first modern international agreements that dealt exclusively with investment and, more specifically, with investment protection. The first BIT was signed in 1959 between Germany and Pakistan. During the three subsequent decades there was a steady growth in BITs (72 in the 1960s, 166 in the 1970s and 386 in the 1980s). In the 1990s the number of BITs literally exploded. At the peak in 1994–1996 around 200 new BITs were being signed each year (UNCTAD, 1999). By the end of 2004 there were 2,265 BITs in force (UNCTAD, 2004).

In general, it has been the European countries that have driven this development. By 2002 the 15 members of the European Union had concluded a total of 908 BITs. For capital-exporting countries, BITs serve to protect investment assets, particularly against expropriation, in capital-importing (developing) countries. Germany, followed by France and the United Kingdom, has actively sought protection for its investors through BITs (ECFIN, 2002). This stands in sharp contrast to many, if not most, non-European capital-exporting countries (UNCTAD, 2003), which have been latecomers to BITs. The United States only began negotiating BITs in the early 1980s, signing its first BIT in 1982, and had a total of 45 BITs in 2002.² Despite signing its first agreement in 1977, Japan still has only 10 BITs and as of 2003 only half of these had entered into force. Other developed countries with relatively few BITs include Canada, Australia and Norway.

But the recent surge in BITs cannot be attributed to the EU member states. A new pattern began to emerge in the 1990s (UNCTAD, 2000, 2003). First, the number of countries involved in BITs increased from 102 at the end of the 1980s to 175 in 2002. Second, and perhaps more importantly, BITs among emerging markets and transition economies became more common. Developing countries began to use BITs as a way of borrowing credibility for their investment policy reforms and enhancing their attractiveness to FDI. UNCTAD promoted this development by assisting countries with the drafting and signing of BITs (Ferrarini, 2003). Thus, whilst many African and Latin American countries and the Caribbean lagged behind, the 1990s saw the growth in BITs between developing countries and between transition economies exceed the growth in North-South BITs. By the end of 1999 the original North-South or hub-and-spoke type of BIT constituted merely 40 per cent of BITs, compared to nearly 70 per cent at the end of the 1980s. The composition of China's BITs illustrates this evolution. By early 2000 China had 20 "traditional" BITs with developed countries, but 33 BITs with countries in Asia and the Pacific, 15 with African countries, 9 with Latin American and Caribbean countries and 17 with Central and Eastern European countries.

Perhaps surprisingly this spread in the use of BITs has not altered the

fundamental purpose and content of the agreements. On the contrary, one could argue that the uniformity in the rules and broad principles underlying the agreements suggests that developing country BITs have consolidated the model developed by the original capital-exporting countries. Investment protection still constitutes the core of BITs. This includes protection from nationalization or other forms of expropriation, the right to compensation, clauses providing for minimum standards of treatment (“fair and equitable treatment” and “full protection and security”), free transfer of payments and recourse to dispute settlement among the parties and international arbitration in case of a dispute between a foreign investor and a host country. Finally, most BITs have a very broad definition of investment, covering both tangible assets and intangible assets such as intellectual property rights and licences.

In addition to these standard provisions, BITs commonly have rules on non-discrimination in the form of national treatment and most-favoured nation (MFN) rules.³ Here it is possible to distinguish between two stylized models of BITs (see table 8.1): a “European model” in which non-discrimination only applies post-establishment, and the “US or NAFTA model” in which it also applies to entry or establishment of an investor. In the former, governments or regulators cannot discriminate between investors already inside the territory of the host country; in the latter non-discrimination at the so-called pre-establishment phase means the US or NAFTA model liberalizes investment. The US model also often includes provisions that facilitate access for personnel employed by the investor, as well as quite far-reaching restrictions on the use of performance requirements as a regulatory instrument in host countries. The typical European BIT has no such provisions on performance requirements (while they do tend to include so-called REIO clauses, i.e. exemptions of EU internal measures from non-discrimination).

The difference between the two model agreements can be explained in part by historical circumstances, and in part by European integration. European countries have been active in signing BITs for much longer and adopted their model at a time when protection was deemed feasible in agreements with capital-importing countries, but not liberal access or controls on performance requirements. Indeed, some EU member states themselves made use of restrictions on investment up until the end of the 1980s. But this does not explain why the European countries have not modified their approach and adopted something more like the US model as attitudes towards investment have changed and become more liberal. This is where European integration comes into play. If European BITs are to cover pre-establishment or access, the treaty establishing the European Community implies that the EU member states would have to sign Community/EU-wide agreements negotiated by the European Commis-

Table 8.1 Simplified comparison between different legally binding investment rules

	Bilateral agreements		OECD		WTO		RTAs	
	US BITs	EU BITs	Codes		GATS	TRIMs	NAFTA	EU-Chile FTA
Access, entry and establishment	Y	N	Y		Y	N	Y	Y
Treatment								
National treatment	Y	Most	N		Y	Y	Y	Y
MFN	Y	Y	Y		Y	N	Y	N
Fair and equitable	Y	Y	Y		N	N	Y	N
Transfer of funds and capital movements	Y	Y	Y		N	N	Y	Y
Protection								
Minimum international standard	Y	Y	N		N	N	Y	N
Expropriation and compensation	Y	Y	N		N	N	Y	N
Investor-state dispute settlement	Y	Y	N		N	N	Y	N
Other aspects								
Performance requirements	Y	N	N		N	Y	Y	N
Key personnel	Y	Some	N		Y	N	Y	Y*

Source: OECD, 2004: 16–17, annex 3; Ferrarini, 2003: 69, appendix table 7.

* Mode 4 under services section.

sion; but for political and legal reasons the EU member states are not prepared to cede the power to negotiate BITs to the Commission.

Despite the recent proliferation of BITs, the “European model” is still far more common than the “US model”. This is largely, but not entirely, due to the fact that European countries started earlier. The fact that the European model is limited to post-establishment also means that it raises less concern about loss of sovereignty in host countries (capital importers). Non-discrimination for existing (established) foreign investors is seen as unduly limiting host governments’ right to regulate, which is important for many developing country newcomers to BITs. Conversely, free admission for investors remains contentious for many governments, and many still screen investors on entry.

To sum up, a global network of BITs has emerged, but this network is still far from complete and would need more than 11,000 BITs altogether to cover all existing WTO members. Nevertheless, the broad scope and wide country participation in this network mean that BITs, and in particular the “European model” BITs, form the core of global investment rule-making.

The OECD: From leader to follower

The OECD was the main forum for investment rule-making, in both liberalization and investment protection, in the 1960s and 1970s. The draft Convention on the Protection of Foreign Property of 1967 – although in the end never opened for signature – served as a model for BITs. The Abs-Shawcross Draft Convention of 1959, which was endorsed by the OECD Council in 1962 (OECD, 2004), provided the model for the European BITs.

The OECD also took the lead in responding when calls for international rules on the activities of multinational enterprises from the United Nations and elsewhere were mounting in the 1970s. In their 1976 Declaration on International Investment and Multinational Enterprises, the OECD member countries established a balanced and *voluntary* framework for both governments and corporations. The declaration sought to reflect the interests of those critical to international investors as well as the concerns of the latter. It simultaneously set in place voluntary guidelines for multinational enterprises and commitments for governments to improve the investment climate by ensuring transparency for investment incentives and disincentives; according national treatment to established foreign corporations, the so-called National Treatment Initiative; and minimizing conflicting requirements on multinational corporations through international cooperation. All aspects of the 1979 Declaration have been periodically reviewed and improved upon. There has also

been follow-up, in the shape of peer review, of the various commitments in OECD committees.

But the OECD has been arguably most successful in its work on investment liberalization. In the early 1960s OECD member states negotiated two sets of binding rules on the progressive liberalization of capital movements on a non-discriminatory basis and the liberalization of current invisible transactions (primarily services). The Code of Liberalization of Capital Movements and the Code of Liberalization of Current Invisible Operations were adopted in 1961.⁴ Despite the two codes' *binding* nature, however, compliance has been ensured by peer pressure. Unlike BITs, the OECD codes do not contain specific provisions on dispute settlement or international arbitration, although they do not preclude the possibility of disputes being considered in general or *ad hoc* dispute settlement mechanisms if the parties so agree (OECD, 2004). Both codes have been successively revised and expanded, with the result that they have kept their relevance despite large improvements in investment rules elsewhere. For example, the Code on Capital Movements remains to this day the only plurilateral instrument covering the right of entry and establishment for foreign investors and related capital transfers.

Given this track record, it is perhaps not surprising that the organization was charged in 1995 with the task of developing a comprehensive global agreement on investment, the so-called MAI (Multilateral Agreement on Investment). The original purpose of the MAI was to combine, within one single framework, the highest standards for liberalization and protection of investment. The MAI was intended to be a legally binding and open-ended agreement to which non-OECD countries could later sign up. However, the negotiations deadlocked after three years and were suspended in 1998. The OECD members were unable to agree on rules for investment at this plurilateral level, due to the complex and controversial nature of the issues involved. The timing was not particularly favourable either, with the Asian financial crises raising concerns about the effects of further openness on flows of short-term portfolio investment. The MAI negotiations also received enormous attention from many civil society groups. Some fiercely criticized what they saw to be excessive intrusion in national sovereignty and a hand-over of power from the electorate to big corporations.

The failure on the MAI was a major challenge to the proponents of global investment rules. But it was also, rightfully or not, a challenge to the OECD. Even before the launch of the MAI negotiations, the OECD had become less prevalent as a forum for investment rule-making. The focus of OECD work had been gradually shifted towards developing best practices and providing a forum for peer review. The MAI underscored the problems of using the OECD for investment rule-making

when investment flows are truly global and the main target countries of these rules are not members of the organization.

After the obvious setback of the MAI, the OECD retains a somewhat less prevalent role in international investment rule-making. The organization's original investment instruments remain relevant for its members and serve as a benchmark for countries around the world. These are periodically reviewed and strengthened, as in the case of the guidelines for multinational enterprises in 2000. Following a more piecemeal approach, the OECD has also taken the lead in recent years in developing some issue-specific instruments related to investment, such as combating harmful tax competition and money-laundering, improving bank transparency and countering so-called hard-core cartels. In 1999 the OECD Anti-Bribery Convention entered into force, making bribery of a foreign public official a criminal offence. It is noteworthy that in all these important areas the OECD's work has focused on limiting the negative effects of globalization through some increased control of corporate activities rather than promoting investment protection and liberalization.

Two steps forward and one step back in the WTO

In the 1986–1994 Uruguay Round the world's leading trade negotiators endeavoured to reach agreement on certain investment-related rules. Simultaneously with the creation of the WTO in 1995, therefore, a number of agreements of more or less relevance for global investment came into force. These are the General Agreement on Trade in Services (GATS), the Agreement on Trade-Related Investment Measures (TRIMs), the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), the (plurilateral) Government Procurement Agreement (GPA) and the Agreement on Subsidies and Countervailing Measures (ASCM).

None of these WTO agreements even remotely resembles the type of comprehensive investment framework the MAI negotiations in the OECD sought to establish. But they are nevertheless important in the global investment architecture, especially GATS, which addresses entry and treatment of investment in services, and TRIMs, which deals with government control over investment activities.⁵

GATS covers trade in services, which includes *inter alia* the delivery of services through “commercial presence” and thereby regulates investment in services, which represent the predominant and growing share of world FDI stocks (UNCTAD, 2004: 16). A core provision in GATS is the MFN treatment that applies for all members and across the board. But members are allowed keep a limited number of MFN exceptions, which usually pertain to land ownership and equity requirements (OECD, 2003). Beyond MFN, GATS includes horizontal rules on transparency and

general principles for domestic regulation. More importantly, however, GATS also provides for the possibility of market access and national treatment for investment; but these are contingent on an explicit commitment to grant such treatment. Openness is not offered on an “all or nothing” basis. Members can and do still keep various conditions or qualifications to both market access and national treatment. Although developed countries have made commitments to open up services markets for foreign investors and provide national treatment in nearly 80 per cent of all services sectors, only about 30 per cent of these commitments are unconditional. As one would expect, full access and national treatment are even less common among developing countries, which have on average made commitments on services investment in 45 per cent of all sectors, out of which merely 14 per cent are free from limitations (OECD, 2003). Therefore, while GATS enhances liberalization of investment in services, the ample exemptions and conditions raise suggestions that it primarily serves to lock in reforms already implemented among its members rather than open new markets. Nevertheless, GATS constitutes an important part of the global investment rules, even though it leaves aside investment protection.

The main purpose of the TRIMs agreement was and remains to clarify the interpretation of existing GATT rules on national treatment and quantitative restrictions (GATT arts III and XI) to certain trade-distorting investment measures. The TRIMs agreement also includes an illustrative list of measures that are considered to be inconsistent with these GATT rules. The TRIMs agreement thereby interprets existing rules on a number of performance requirements by which governments seek to influence investors’ operations. It is far from a ban on performance requirements altogether. But the agreement prohibits those requirements that are in breach of national treatment or constitute unlawful forms of quantitative restrictions, such as local content requirements, trade-balancing obligations and the like. However, implementation of this global framework for performance requirements has been, at best, slow. Despite the long initial transition periods, many developing countries have requested and been granted additional time to phase out non-conforming performance requirements. In addition, a majority of WTO members have still not lived up to their commitment to notify those investment measures that are not in conformity with the agreement (OECD, 2003).

In conclusion, the WTO agreements of 1995 certainly represent important improvements, but fall short of establishing clear and effective investment rules that promote further openness and limit the scope for “illegitimate” government interference. A new attempt to create such rules and fill the gaps in existing agreements was made under the Doha Development Agenda (DDA), the ongoing WTO round launched in Doha,

Qatar, in 2001. The mandate for the WTO to work on investment issues dates from the 1996 Singapore ministerial meeting. But work could not begin effectively until the DDA was launched, and preparations for negotiations quickly ran into problems. As in the OECD, the issues at stake proved too controversial for some countries and civil society again lobbied hard to block negotiations. But perhaps more importantly, some of the main proponents of international investment agreements, notably the United States and the international business community, become increasingly lukewarm about the negotiations in the WTO as it became clear that the final outcome would not match what could be achieved in RTAs or elsewhere. In the end, therefore, after two years of preparatory negotiations and many more years of heated debate, the WTO membership dropped investment from the negotiating agenda.

The failure even to begin negotiations on investment in the WTO leaves the trading system with GATS and TRIMs as the only global rules for investment. This represents a patchy and structurally unbalanced system. In some areas, like services investment, there are clear-cut and ambitious provisions; in others, like performance requirements, there are basic disciplines that still need to be clarified and applied; and in other important areas, like entry for investment in manufacturing or investor protection, there are no global rules at all.⁶

The surge in investment RTAs

The spread of regional trade agreements (RTAs)⁷ with substantive provisions on access for – and domestic regulation of – foreign investors is arguably the most important recent phenomenon in international rule-making on investment. This new trend only really took off in the last decade, and coincided with the proliferation of cross-continental investment RTAs. The latter are agreements between trading partners anywhere in the world, i.e. irrespective of geographical proximity and differences in economic circumstances. Some earlier RTAs and cooperation arrangements did include investment provisions, not least where the RTAs served as a means of promoting regional integration, such as the European Union and the Andean Community.

Like the spread of RTAs in general, the evolution of investment RTAs can be seen as a dialectical process involving moves towards deeper commitments and broader participation. This process has progressed in bursts, with periods of stagnation in between. Over time it has come to add more and more issues to the core set of investment provisions, and it has been the result of the activities of an ever-greater number of actors in the world economy.

From a European-driven process . . .

The first RTA of importance for the development of investment rule-making actually pre-dated the first BIT. This was the treaty establishing the European Community in 1957 that, among other things, prohibited restrictions on the freedom of establishment through agencies, branches and subsidiaries (Heydon, 2002: 7). The treaty was important in many respects, but for the evolution of investment RTAs its primary legacy was that it served as a source of inspiration, or even a model, for subsequent integration efforts around the world.

The EEC had many followers. It appears to have been emulated in the creation of the Arab Economic Unity in 1957, the Customs and Economic Union of Central Africa in 1965, the Association of South-East Asian Nations (ASEAN) in 1967, the Andean Common Market in 1969 and the Caribbean Community in 1973.

Many of these, and subsequent, regional integration schemes also contained a common framework for investment. Although the EEC treaty probably served as the inspiration for these, they also introduced novelties. In some cases special regimes were put in place to promote cooperation between firms within a region, by granting certain regionally based enterprises particularly favourable treatment. Beyond internal liberalization, attempts were made, notably in the Andean Common Market, to promote harmonization of investment policies *vis-à-vis* third-country investors, including more stringent (performance) requirements on foreign investment.

In the 1970s and early 1980s, however, deep integration in the form of investment agreements waned in the face of financial turmoil, dramatically higher oil prices and increasingly aggressive attitudes to foreign corporations. As a consequence the impetus behind many regional agreements was lost and they were not fully implemented or adequately enforced, which resulted in them having little relevance for investors.

The next step in the evolution towards more ambitious investment RTAs began in the mid-1980s. As in the 1960s, Europe took the lead. The establishment of the single market, through the Single European Act in 1986 and various regulations implementing EU treaty provisions (e.g. Council Directive 88/361/EEC of 24 June 1988), provided fresh momentum to regionalism worldwide. For outsiders, European integration constituted both a model and a threat. It was seen as a threat by those who believed the redoubling of efforts would result in internal liberalization but a “fortress Europe” *vis-à-vis* third countries. This stimulated the establishment of new regional agreements, such as MERCOSUR (1991), the ASEAN Free Trade Area (1992), the African Economic Commu-

nity (1991) and the Common Market for Eastern and Southern Africa (COMESA) in 1993.

This trend also spurred renewed efforts to deepen existing regional agreements, and in time the instruments related to investment were also strengthened and expanded. Substantial revisions were, for example, made in the Andean Community in 1991, in the Economic Community of Western African States (ECOWAS) in 1993, in MERCOSUR in 1994, in the amendment of the CARICOM (Caribbean Community) treaty in 1997 and by the revision of existing ASEAN instruments in 1987 and 1996.

These new and revised investment RTAs often contained improved rules on the right of establishment and the free movement of capital. The amendments to CARICOM included both a “standstill” and a “roll-back” on restrictions to access for investors. Removal of obstacles to the free movement of capital and the free transfer of funds was commonplace, including in COMESA, the African Economic Community and ECOWAS, to name but a few. However, as in the 1960s and 1970s, there were also provisions that departed from European practice, such as rules that differentiate between regional and third-party investors in order to promoting regional enterprises in the case of the Andean Community and rules on investment protection in MERCOSUR.

To sum up, these regional agreements and investment RTAs were to a greater or lesser degree modelled on the internal market of the European Community, and all followed the broader trend towards regionalism set in motion by European integration.

This Europe-driven second wave of regional integration continued throughout much of the 1990s. The European Union also began negotiating trade agreements and investment RTAs with its neighbours during this period. In 1992 the European Economic Area (EEA) agreement was signed with the EFTA countries (except Switzerland), which extended the single market to these countries. With the fall of the Berlin Wall, the European Union embarked on and concluded the so-called Europe Agreements with the East and Central European countries. Moreover, from the mid-1990s the EU RTA initiatives were extended to the countries around the Mediterranean under the so-called Barcelona Process. It should also be recalled that the European Union was active on many more fronts other than RTAs. From the 1960s onwards, the EU member states have continued to sign BITs in ever-increasing numbers.⁸

But in parallel with this trend, from the end of the 1980s and initially in the shadows of the dominance of EU activism on BITs and RTAs, a new phase in investment RTAs started to emerge. Agreements contained vastly more elaborate regional investment rules. What is more, this new

trend ultimately involved a new set of actors and efforts to establish cross-continental RTAs. Even the European Union's more recent RTA initiatives with advanced developing countries, not least in the cases of Mexico, Chile and MERCOSUR, were in part reactions to this changing pattern in RTA activism. At its core was the fundamental shift in US attitudes towards RTAs.

... to a US-driven NAFTA approach ...

During the 1960s and 1970s the United States had refrained from signing not only BITs but also RTAs in general. But in the early 1980s these policies were reversed. The United States signed its first BIT (with Panama) in 1982, followed three years later by the first US FTA (with Israel) in 1985. Even so, it was only in the early 1990s that the new policies for BITs and RTAs fully came into force.

Contrary to the case of the European Union, US initiatives on BITs and RTAs were linked. The United States gradually came to apply its BITs model to the new RTAs it was negotiating. The first step towards such a new "model" for investment RTAs was taken with the US-Canada FTA in 1988 (entered into force in 1989). This model was consolidated with the signature of NAFTA between Mexico, Canada and the United States in 1993.

Since NAFTA effectively codified the US-model BIT (i.e. "BITs-plus"), it was more comprehensive in scope and depth than most previous investment RTAs (Dymond, 2002; table 8.1). But the importance of the agreement was not only its unprecedented level of ambition on investment RTAs. NAFTA set in motion a proliferation of new RTAs, including the spread of more ambitious investment rules, around the Pacific, in Latin America and elsewhere (Bark, 2002: 38). In 1994 the Asia Pacific Economic Cooperation (APEC) agreed upon the vision of a free trade area by 2020 (2010 for developed countries) and the leaders of the Western hemisphere, excluding Cuba, decided to launch negotiations on a future Free Trade Agreement of the Americas (FTAA). The former included dismantling of investment barriers, and to that end the APEC Non-Binding Investment Principles were established, covering many of the issues of the NAFTA investment chapter.

On the bilateral front there was also a plethora of initiatives. Initially these efforts to conclude bilateral FTAs were limited to the Western hemisphere, but they soon spilled over into cross-continental negotiations on FTAs.

Having signed NAFTA, Mexico pursued very actively a new regional strategy by signing free trade agreements with, *inter alia*, Columbia and Venezuela in the so-called G3 (1994), Bolivia (1994), Costa Rica (1994),

Nicaragua (1997), Chile (1998) and El Salvador, Guatemala and Honduras, in the so-called Northern Triangle (2000). With regard to investment rules, most if not all of these built on the NAFTA model (see below for more detail). From the end of the 1990s, Mexico's RTA activities also included negotiations across the Atlantic and the Pacific. FTAs were concluded with the European Union and EFTA in 2000 and Japan in 2004, and negotiations are still ongoing with Singapore (started in 2000). For most of Mexico's trading partners a main driving force for negotiations has been to safeguard their shares of the Mexican market and/or to use Mexico as a gateway to the United States through the establishment of NAFTA parity.

Canada also gradually became more active on the bilateral front by first emulating the US-model BIT and then entering negotiations on RTAs. The FTA with Chile in 1996 contained almost a carbon copy of the NAFTA provisions on investment. However, in Canada's 2001 agreement with Costa Rica, the second of Canada's FTAs after NAFTA, investment was left aside with a reference to the existing BIT between the parties. This could, in part, be explained by the very vocal opposition against NAFTA and investment in general among Canadian civil society and left-wing groups that was stimulated by a number of highly controversial investor-state disputes under NAFTA that targeted Canadian regulations. This raised concerns, shared by the United States, about the tendency towards judicial activism on part of international arbitrators given the broad scope of NAFTA. In 2001, therefore, the parties of NAFTA adopted a "Note of Interpretation of Certain Chapter 11 Provisions" to clarify the provisions related to standards of treatment ("fair and equitable treatment") and bring the interpretation of these NAFTA rules in line with customary international law.

While these concerns about the NAFTA investment provisions and the possibility of US regulations being the target of investor-state disputes are shared in some US political circles, they have so far had little impact on the US administration's BIT and RTA strategies. During the 1990s the United States consistently signed high-standard BITs and embarked on a very proactive RTA policy under the first Bush administration. As for RTAs in general, US BITs and investment RTAs have become instruments of broader foreign policy, trade and economic objectives. They have been used to promote pro-market economic reform, promote and protect US investment abroad and provide favourable treatment for US security allies.⁹ In some cases they have also served as models for future negotiations, such as with ASEAN and within the FTAA.

The deadlock at the WTO ministerial meeting in Cancun in 2003 appeared to have reinforced the US emphasis on RTAs. To date the United States has concluded FTAs with, for example, Jordan (2001), Chile

(2003), Singapore (2003), Morocco (2004), the Central American Common Market and the Dominican Republic (2004), Bahrain (2004) and Australia (2004). In addition, the United States is presently negotiating FTAs, or is preparing for negotiations, with SACU, Thailand and Oman, to name just a few.¹⁰

Of course, given the very asymmetric character of many agreements and the US interest as a capital exporter in securing access and protection for investment in its RTA partners' markets (and not the reverse), the United States has everything to gain from applying the open-ended disciplines of the NAFTA model in combination with investor-state dispute settlement. In asymmetric agreements such stringent rules pose no real threat to US interests in terms of the risk of legal challenges from foreign investors. NAFTA-type investment rules are therefore typically part and parcel of the US FTAs (and BITs). However, it is noteworthy that the United States – in applying the NAFTA model – has also included the Note of Interpretation from 2001 (see above) in some agreements, such as that with Singapore. This did not stop the United States pressing for and obtaining limits on and penalties for restrictions on capital transfers in its agreements with Singapore and Chile (Hilaire and Yang, 2004: 609).

A more important break with the original NAFTA model was made in the US FTA with Australia, which does not include investor-state dispute settlement. Officially this has been justified by the confidence that the parties have in each other's domestic legal system. This is certainly true. But Chile and Singapore also have functioning domestic legal systems and the US FTAs with these include investor-state dispute settlement. The main difference with the US-Australia FTA is that it regulates investment between capital-exporting countries, just as NAFTA does for investment between the United States and Canada. The experience from legal challenges by investors under NAFTA cannot therefore be precluded as a key factor behind the decision to exclude investor-state dispute settlement in the agreement with Australia.

To sum up, there is little doubt that NAFTA has played a major role in the more recent surge in RTAs, and particularly in the evolution of investment RTAs. The spillover effects from NAFTA have, however, affected other non-NAFTA signatories. Just as NAFTA created a push for FTA negotiations between Mexico and the European Union, EFTA and Japan, the subsequent launch of the FTAA provoked many countries to reconsider their trading arrangements with the countries of the Western hemisphere in general. For example, the launch of the FTAA contributed to the European Union's decision to launch trade negotiations with MERCOSUR and Chile.

... towards a process by all for all?

In recent years more and more countries have started to negotiate RTAs in general and investment RTAs in particular. The trend towards cross-continental RTAs irrespective of geographical proximity and differences in economic development has also been further advanced. As a consequence, quite a number of investment RTAs have been established. Many of these are either North-South agreements without the United States or the European Community as parties, or South-South agreements among advanced developing countries. Strikingly, both forms of agreements (North-South and South-South) have often proved to include a surprisingly high standard of commitments on investment.

The most remarkable policy shifts towards RTAs have occurred in Asia. With the exception of ASEAN (and AFTA, the ASEAN Free Trade Area), most Asian countries showed little interest in the “regional track” up until the Asian financial crises. But since then a number of Asian countries have concluded RTAs and an even greater number of states are in the process of negotiating new agreements with both other Asian countries and trading partners worldwide. ASEAN and its members have been key drivers of this development. On the bilateral front among the ASEAN countries, Singapore in particular has taken the lead (discussed in more detail below), followed by Thailand. But other countries that had previously refrained from RTAs are now joining the surge, such as India, Japan, Korea and China, as well as Australia and New Zealand. With the possible exception of India (despite the fact that its recent FTA with Singapore contained substantial investment provisions), many of these actors have also opted for higher-than-average investment rules. Even though many of these RTA initiatives are still to be concluded, there are already cases of “borrowing” from the NAFTA model, while not necessarily matching NAFTA’s level of ambition. Illustrations of this novel phenomenon are the ASEAN Investment Area of 1998, the Japan-Singapore New-Age Economic Partnership Agreement of 2002, the Japan-Korea Investment Agreement, the Korea-Chile FTA of 2002 and the Japan-Mexico FTA of 2004, to name but a few.

While the Latin American states have always been heavy users of regionalism, more and more Latin American countries have in recent years, as in Asia, sought more ambitious investment RTAs with NAFTA-type rules. Also as in Asia, these activities have occurred both within existing regional or hemispheric integration schemes and within cross-continental RTAs. Undoubtedly, the most visible drivers of this development are Mexico and Chile (see next section). MERCOSUR and particularly Brazil have also begun to seek cross-continental RTAs, at least as a tool for

political profiling, but it is still very unclear whether many of these initiatives by Brazil and others will result in any comprehensive commitments with regard to investment. Judging from the EU-MERCOSUR and FTAA negotiations, some MERCOSUR countries appear to be hesitant about ambitious investment RTAs. This suggests that the gap in activities on investment RTAs between the early movers and the laggards will remain or possibly widen in the (near) future.

Paradoxically, the European Union is among the laggards in the most recent race towards high-level investment RTAs.¹¹ Even the EFTA countries, despite their historical tendency to follow the European Union, have been ahead of it on RTAs, including investment, in recent years. An amendment of the EFTA Convention in 2001 involved adopting key elements of NAFTA (OECD, 2002), and thus cleared the way for more ambitious investment RTAs with third parties.

Conversely, the investment rules in the EU's agreements with third parties have, in general, been strikingly weak, especially in the cross-continental RTAs. For example, the investment provisions of both the EC-South Africa FTA in 1998 and the EU-Mexico FTA in 2000 fell far short of other countries' investment RTAs at that time, even compared to RTAs between developing countries. The European Union's most ambitious agreement to date, namely the 2002 EU-Chile Association Agreement, represented an important qualitative leap forward on investment rules. This agreement was the first time that an EU RTA featured reasonably ambitious commitments on investment that went beyond provisions on payments and/or capital movement. The coverage of the EU-Chile agreement was, however, limited to pre-establishment, based on a "positive" list of commitments for which the parties granted national treatment (see table 8.1).

Up to that point, the Commission and the member states had generally not been able to agree on a clear and ambitious common position on investment in RTAs.¹² Member states were, for different reasons, hesitant to grant the European Commission the mandate to negotiate a comprehensive investment agreement. The internal conflict was already acute during the EU-Mexico negotiations, when the ambition of seeking parity with NAFTA collided with (some) member states' defensive interests and concerns over competence. In the EU-Mexico agreement the European Union in the end had to settle for some very basic provisions (notably elimination of restrictions on payments). However, when the internal disagreements resurfaced in the EU-Chile negotiations during the Swedish presidency of the European Union, Sweden and France, which represented the two opposite perspectives on the issue, managed to reach a common line that mobilized sufficient support among member states at large. This ultimately paved the way for the Commission to pursue more

ambitious investment rules. But the Commission still had to stay in line with the distribution of competence within the European Union, and hence was not given any mandate to negotiate provisions on protection similar to those in BITs. The end result was an agreement that, contrary to the EU-Mexico agreement, had meaningful commitments on pre-establishment. But post-establishment investment protection and enforcement through investor-state dispute settlement were once more left aside with a reference to BITs between individual member states and Chile.

In summary, although only a partial victory the EU-Chile agreement represented a breakthrough for the European Union. Since it was negotiated the European Community has persistently aimed for investment RTAs with pre-establishment commitments. Nevertheless, in a post-NAFTA world and compared to many other countries, even some advanced developing ones, the European Union's investment RTAs remain fairly limited in scope. The precedent of BITs involving individual EU member states still prevails.

Illustrations of a new phenomenon – New drivers for investment RTAs

In the last decade or so, RTAs covering investment rules have proliferated. While the United States (and NAFTA) has played an instrumental role in this development, other countries at different levels of development have become just as important. Three such countries are Mexico, Chile and Singapore. All have become major “users” of RTAs since the second half of the 1990s, and all of these countries have opted for ambitious investment rules in their RTAs that largely emulate the existing investment rules in agreements with both developed and developing countries.

Mexico – From American puppet to regional semi-hub?

NAFTA has proved important for a number of reasons. It set the precedent for ambitious investment provisions and for the incorporation of BIT rules and practice in RTAs. The fact that one of the NAFTA signatories, Mexico, was an advanced developing country also had large ramifications for the future.

First, NAFTA showed that it was possible to include high investment standards in trade agreements between parties with very different levels of development. One could say that Mexico paved the way for North-South investment RTAs in which the southern partner assumes the lion's share of the stringent commitments. Before NAFTA such forms of highly

asymmetric “burden-sharing” between capital-exporting and capital-importing countries had been limited to BITs.

Second, with NAFTA Mexico departed from the Calvo Doctrine, which had historically been undisputed in most Latin American legal systems. The Calvo Doctrine precluded privileged treatment for foreign investors and stipulated that foreigners would have to rely solely on local remedies, not international law or arbitration. Before Mexico signed NAFTA the Calvo Doctrine had constituted a major impediment to the conclusion of investment agreements, as well as to the application of investor-state dispute settlement. The Mexican departure from the doctrine constituted an important precedent for other Latin American countries (OAS, 1999).

Third, as discussed above, NAFTA stimulated efforts by other countries to level the playing field, which in turn spilled over in additional RTA initiatives. Some developing countries, like those of the Central American Common Market, became anxious to secure similar preferential access to the United States or even to become members of NAFTA (in the case of Chile), while some developed countries sought to achieve NAFTA parity on the Mexican market (e.g. the European Community, EFTA and later Japan). This made Mexico a very attractive RTA partner.

Finally, for Mexico NAFTA was the starting point of a new policy on RTAs. Having signed NAFTA, Mexico began aggressively to pursue bilateral FTAs in the region and with its other trading partners globally. The aim was to spur economic growth and industrial diversification by becoming the centre of a network of RTAs and a gateway to important markets like the United States. Openness to investment was very much at the core of this strategy and, with the legal adjustments to NAFTA under way or already completed, extending NAFTA treatment to other parties was in reality not a difficult “concession” to make.

In the first phase of this new post-NAFTA RTA policy Mexico opted for FTAs with various Latin American countries (such as Columbia and Venezuela, Bolivia, Costa Rica, Nicaragua, Chile and El Salvador, Guatemala and Honduras). These agreements were concluded with the framework of ALADI (Latin American Integration Association). Given that ALADI had been notified to GATT under the enabling clause of the WTO rules on RTAs, this gave Mexico and its partners the possibility of establishing RTAs with very limited scope and depth. But this possibility of circumventing the more stringent WTO rules on RTAs seems to have had little effect on the investment provisions of the FTAs: many of the agreements built on the NAFTA investment model. Some even replicated the NAFTA (BITs-plus and WTO-plus) provisions on the controversial is-

sue of performance requirements, such as in the case of Mexico's agreements with Nicaragua and with El Salvador, Guatemala and Honduras.

In fact it is Mexico's more recently concluded RTAs with developed countries that reveal a greater variation in investment rules. Mexico's RTA with Japan, signed in September 2004, contained very ambitious NAFTA-type provisions on investment, but the EU-Mexico FTA (and EFTA-Mexico) fell far short of NAFTA and provided neither preferential access nor protection for investors. As discussed above, this was not due to Mexico. In the negotiations with the European Union, Mexico tabled an ambitious draft investment chapter indicating its willingness to grant NAFTA parity.

The striking feature of Mexico's RTA policy is therefore that it appears to favour the use of NAFTA-type provisions in its investment RTAs, including agreements with other developing countries in the Western hemisphere. Through these agreements, Mexico has become a real semi-hub and an attractive RTA partner. More importantly, it has ultimately meant that the original US-model BIT that was consolidated in NAFTA has broken with the typical North-South pattern of agreement and become an integral part of many South-South FTAs involving Mexico.

Chile – From Mexican follower to liberal prophet?

Chile's first steps towards a more active RTA policy largely sprang from the creation of two important regional trading areas in the Western hemisphere in the early 1990s – NAFTA and MERCOSUR. With the prospect of becoming marginalized and facing trade diversion, Chile reacted by seeking agreements with the parties of these two agreements. Chile signed an association agreement with MERCOSUR in 1996 that established a free trade area. At the same time Chile expressed its interest in becoming a partner to NAFTA. As there was not much support for this approach, not least in the United States, Chile pursued FTAs with the NAFTA countries individually as a way of facilitating future accession to the trade bloc. It signed agreements with Canada in 1996 and with Mexico in 1997. Naturally, both FTAs contained investment provisions based on the NAFTA model.

Subsequently Chile has continued to use RTAs to promote its offensive interests, such as those of the private sector in gaining access to the Central American (1999) market. The RTA with Central America appears to have been negotiated, at least in part, to ensure that access for Chilean exporters matched that for Mexican producers after the Mexico-Central American FTA. The same can be said about the sub-

sequent Chilean RTAs with the European Community (2002), EFTA (2003) and the United States (2003).

At the same time, there can be little doubt that Chile increasingly began to use RTAs as part and parcel of an overall foreign trade policy strategy to promote the country's economic growth actively, as well as its standing and attractiveness for international investment. As a small, trade-dependent and open economy with a favourable business climate (and a not-too-favourable geographical location), high standards on investment access and protection were seen as integral to this strategy. Not surprisingly, therefore, Chile has adopted the NAFTA model, initially introduced in its agreement with Canada, as a basis for future investment RTAs. The RTA with the European Union was perhaps the main exception to the rule of ambitious investment provisions, but as in the EU-Mexico agreement this had nothing to do with Chile's interests. The recent agreement with the United States reveals how the NAFTA model has evolved. The US-Chile FTA includes a number of improvements to the provisions on investment protection that reflect the US experience with NAFTA. Notwithstanding these changes, the NAFTA model, albeit with some variations, has been a dominant feature of Chile's RTA policy.

In its pursuit of a proactive strategy to promote economic growth and compensate for its disadvantageous location, Chile has recently turned to Asia. With the aim of serving as a bridge between Asia and the Western hemisphere, Chile concluded a series of FTAs with Asian trading partners: with Korea in 2003 – Korea's first-ever RTA; with Brunei, Singapore and New Zealand (P4) in 2005; and with India (only a partial-scope agreement) and China (only goods) in 2005. For Chile, this is a matter of hedging risks. A broad range of cross-continental RTAs with its major trading partners provides market access, but also reduces the country's vulnerability, promotes more stable growth prospects and provides a buffer against economic turbulence (Matus, 2004). This policy was influenced, among other things, by Chile's experience with contagion from the Asian financial crises, which led to economic downturn and rising levels of unemployment.

In its negotiations with the Asian countries, Chile so far seems to have tried to pursue high-level investment RTAs, although the more recent partial-scope agreements must raise some doubts about the continuation of this policy. Chile's agreement with Korea, the only one of Chile's Asian RTAs in force, contained very ambitious commitments on investment, especially if one takes into account the track record of Asian FTAs and the fact it was Korea's first RTA. The Korea-Chile RTA was also much more ambitious than the 1996 BIT between the parties that entered into force in 1999. The investment provisions in the Chile-Korea

RTA were broadly based on the NAFTA model but with some of the improvements of the US-Chile RTA (including a more precise definition of minimum standard of treatment and very specified rules for investor-state disputes). The agreement also provided for the possibility of applying regulatory safeguards with regard to transfers, thus replicating the provisions in the Japan-Korea investment agreement of 2002. Chile was also allowed to maintain some controls on financial transfers, something that Chile agreed to give up in the US-Chile RTA.

To sum up, while Chile was not one of the initial leaders in the spread of ambitious investment RTAs, it has certainly played an active role in the proliferation of cross-continental RTAs. Chile has opted for NAFTA-type investment provisions in its RTAs, although the more recent agreements raise some doubts about the continued consistency of Chile's approach to investment in RTAs.

Singapore – From attempted leadership to enlightened self-interest?

Singapore seems to be for Asia what Chile is for Latin America. It portrays itself as an ideological free trader, albeit also reflecting real economic interests as a small, trade-dependent country, and has pursued closer integration with its neighbours while at the same time opting for a large number of comprehensive and ambitious RTAs with trading partners worldwide.

Up until the Asian financial crises, Singapore's only RTA was with ASEAN. Within AFTA, Singapore was (and continues to be) a key advocate of further dismantling of trade and investment barriers. The ASEAN Investment Area (AIA) was signed in 1998, in the midst of the financial crises, with the objective of ensuring the free flow of investment by 2020. To that end the AIA stipulated that ASEAN investors, in line with the NAFTA approach, should be granted non-discriminatory treatment (MFN and national treatment) and accorded immediate access. ASEAN members were, however, also allowed temporarily to exclude industries and measures from these commitments until 2010 (2013 for Viet Nam and 2015 for Laos and Myanmar). While most ASEAN countries have made use of this possibility, Singapore and Malaysia have no exclusions.

ASEAN integration and ASEAN's increasing RTA activities no doubt remain a key priority. But quite clearly the integration process within ASEAN has been too slow and patchy for Singapore's taste. It is also difficult for ASEAN to reach common positions on RTAs between ASEAN and other countries. Consequently, in the years following the Asian financial crises, Singapore embarked on a very active bilateral RTA policy as a complement to ASEAN integration and ASEAN RTAs with third

countries. As a first priority, Singapore chose to negotiate agreements with its main trading partners and countries that seek an access point into South-East Asia. By the end of 2005 RTAs had been concluded with New Zealand (2000), Japan (2002), Australia (2003), EFTA (2003), the United States (2004), Jordan (2004), New Zealand, Bahrain and Chile (2005), Korea (2005) and India (2005). During the same period Singapore began negotiations on RTAs with a long list of additional countries – Mexico, Canada, Sri Lanka, Bahrain, Egypt and Panama. Singapore has also sought, so far unsuccessfully, bilateral FTAs with the European Community and China (to complement the China-ASEAN agreement).

In all these negotiations, Singapore has advocated openness for trade in goods and services as well as for investment. As in the case of Chile, this is based on Singapore's limited defensive interests and its recognition that the promotion of inward investment has played, and will continue to play, a central role for the country's economic development. For Singapore, therefore, the RTAs are intended to consolidate its attractiveness as an investment location. In its coverage of investment in RTAs Singapore has consistently placed great emphasis on the fact that these rules do not simply benefit domestic business, but also foreign-owned investors with substantial business operations on the customs territory. This is, of course, commonplace for BITs and BITs-like RTAs, but it is less common for governments actively to market this element of RTAs.

In fact, investment promotion seems to be the bread and butter of Singapore's RTA strategy. This becomes even more apparent if one considers Singapore's recent RTA initiatives with, for example, Egypt and Jordan. At a first glance, the economic motives for these initiatives are not entirely clear, given the limited bilateral trade. But by concluding these RTAs, foreign investors can choose to channel their investment to Egypt and Jordan through subsidiaries in Singapore rather than through the mother company in the United States and/or the European Union.

It is therefore in Singapore's self-interest to favour high-standard investment provisions in its RTAs or investment RTAs. The track record shows that Singapore has even opted for more extensive commitments on investment than its RTA partner by, for example, fewer exemptions to non-discrimination than its RTA partner, such as in the case of the Singapore-Japan RTA.

Although the liberal objective is clear, the model used for Singapore's investment rules in RTAs has evolved more gradually. Singapore's first non-ASEAN RTA, with New Zealand, fell short of comprehensive NAFTA-type rules. Although it did provide for non-discrimination, free transfer of funds and investor-state dispute settlement, most provisions were not particularly precise and it lacked rules on *inter alia* investment protection (expropriation and compensation), key personnel and perfor-

mance requirements. It was only in subsequent agreements that rules covered liberalization and investment protection. There have also been some important differences between the investment provisions in Singapore's agreements. The agreement with Japan followed the NAFTA model closely, but with the addition of a safeguard in line with the Japan-Korea investment agreement. The Singapore-Australia RTA followed the NAFTA model, but excluded MFN and performance requirements while adding safeguards and more flexibility with respect to commitments. Likewise the RTA with EFTA follows the broad NAFTA approach but also excluded performance requirements, provided more scope for domestic regulation and taxation and only contained more detailed procedural rules on investor-state dispute settlement. In contrast the RTA with the United States had very ambitious provisions in all aspects of the NAFTA model and, like the US-Chile RTA, contained improvements, such as more precise definitions of the minimum standard of treatment. The section on investor-state dispute settlement was also expanded.

In the recent RTA with the United States, Singapore has moved to adopt new model investment rules. It remains to be seen, however, whether Singapore will, like Mexico and Chile in Latin America, play an important role in spreading this model in the region and globally. RTAs concluded by other Asian countries, such as Thailand (e.g. with Australia and New Zealand) and Malaysia (with Japan in December 2005), include less ambitious investment disciplines than those in the Singapore RTAs. Other Asian countries face more serious domestic opposition to the liberal NAFTA model. So while there may have been some policy spillover from Singapore's bilateral RTA activities in general, there is – to date – little evidence that Singapore has had any real influence on the appetite (or lack thereof) for investment liberalization and protection among other key Asian countries, within ASEAN or elsewhere.

Conclusion: The politics of investment rule-making

The sheer number of BITs concluded between a large and growing number of countries in the last decade has made BITs the main pillar of the global investment regime. Neither the OECD nor the WTO (nor the United Nations) has kept pace with this bilateral rule-making, despite repeated efforts to broaden and deepen multilateral rules.

But the regional level is catching up. EU integration was emulated in various RTAs worldwide. But the real breakthrough for regional rule-making in investment came with the shift in policy by the United States, and more specifically the conclusion of NAFTA in the early 1990s. By

consolidating the “US BIT model”, NAFTA raised the bar for investment rules and went beyond earlier efforts. NAFTA has also had important spillover effects on investment rule-making in general, with, for example, striking similarities between NAFTA and the scope of the MAI negotiations in the OECD (Ferrarini, 2003). New cross-continental RTAs and revisions of existing RTAs have also borrowed from NAFTA, which has functioned as a benchmark in the recent surge of RTAs.

Mexico and to a lesser extent Chile and Singapore have played a pivotal role in spreading investment rules, including NAFTA-type rules, in RTAs both within their respective regions and across continents. And others are catching up.

These trends raise a number of pertinent and interrelated questions, to which one can only suggest some tentative (and potentially speculative) answers based on the findings of this chapter. The first question concerns the role of domestic politics and the issue of the political accountability and legitimacy of the surge of investment rules worldwide. The second question relates to the degree of homogeneity in approaches to investment rules in RTAs and the extent to which these rules have been adjusted to fit the specific circumstances of the parties to investment RTAs. The third and final question has to do with the interaction, if any, between different levels of rule-making in investment, particularly between the rapid expansion of investment rules at the bilateral and regional levels and multilateral rule-making.

Few investors and many lawyers, but no politicians?

The surge in investment RTAs tends to resemble the pattern of international politically driven “me-too regionalism” and/or a new “domino theory” (Jae Lee, 2004). Strategic economic and political interests formulated on the part of central governments and, to a lesser extent, investors have pushed the development forward, with governments influenced in their strategic vision by the activities of other countries. A race to the top has been set in motion, often initiated by developed countries, notably the United States but also in a historical perspective by European countries, concluding comprehensive and ambitious agreements. This “race” has quickly found new drivers that have, in turn, provoked further RTA initiatives, and so on.

Consequently, traditional domestic politics seems to have been secondary in the spread and/or the content of investment RTAs, and probably BITs. In fact, most activities on investment RTAs and BITs have occurred at the sidelines of, and been rather insulated from, domestic politics and public scrutiny. The obvious exception is NAFTA, which spurred

much debate over its investment provisions in Canada and the United States. But it remains the exception to the rule. Paradoxically, this contrasts sharply with the widespread and in many instances heated political debate on investment negotiations in the OECD and later in the WTO, even though any WTO rules would almost certainly have been far less comprehensive than BITs and most investment RTAs.

However, there are reasons to believe that BITs and ambitious investment RTAs will come under increasing public scrutiny and become more politicized, which could lead to a reversal of policies. First, questions have been raised over the benefits in the form of additional investment inflows that developing countries can derive from investor protection. Some have claimed that the economic gains from such flows are minimal at best (World Bank, 2003: 131). Others have suggested that the benefits can be important, albeit mainly for poorer countries that lack credible domestic institutions. Yet other observers have pointed to the potential gains while underscoring the primacy of a number of factors that shape the economic benefits that are unrelated to the investment rules as such (see for example World Bank, 2004: chap. 5). All in all, the inconclusive nature of the various assessments raises the issue of whether the limits on sovereignty inherent in BIT investor protection and more modern investment RTAs are a price worth paying. As investment rules in RTAs also limit governments' ability to regulate establishment of investors, the issue is potentially even more incendiary.

Second, there is a growing debate about the inclusion of investment in the ongoing negotiations on economic partnership agreements (EPAs) between the European Union and its former colonies in the ACP states. Parts of civil society in the European Union and some of the ACP countries have already voiced the criticism that the negotiations aim to establish rules in areas which have been taken off the agenda in the WTO round. The mobilization against the so-called Singapore issues in the WTO, of which investment is one, seems thus to begin gradually to spill over into RTA negotiations like the EPAs, but also into RTA negotiations with countries such as Thailand. The NGO campaign launched against investment rules in EPAs, drawing the attention of parliamentarians and the general public, could just as easily be broadened to the existing BITs of European member states, as well as RTAs more generally.

Third, and perhaps most importantly, serious concerns have been voiced over the increasing number of compensation claims under BITs. Investor-state disputes are rapidly becoming an attractive niche for lawyers. Given the multitude of BITs and more recent investment RTAs that provide for international arbitration, there are ample opportunities for forum shopping. Investors can actively seek the most attractive venue

for bringing their claims against a government, or even file multiple complaints for one case under different agreements (OECD, 2004). In some instances the disputes have resulted in large fines on governments for breaching their commitments under the agreements. Some of the rulings in the disputes have also been strongly contested. For example, simultaneously with the IMF's efforts to solve Argentina's debt default and establish a sovereign debt restructuring mechanism, Argentina faced many arbitration cases from investors (World Bank, 2004). Therefore, given the similarity of the rules on arbitration between BITs and many of the more recent investment RTAs, there are no reasons to expect that investor-state disputes under RTAs will be either less prevalent or less controversial. The disputes under NAFTA give some indication of what the future could hold.

New drivers – Towards a different approach in the future?

Like in the case of BITs, the recent pursuit of ambitious investment RTAs among new actors seems more often than not to have had little effect on the content of these agreements to date. The high degree of homogeneity in investment rules worldwide probably reflects the tendency among actors to build on or emulate prevailing models (such as NAFTA). Few governments have the capacity and the preparedness to alter models to fit their circumstances.

The broader consequences of the "copy" approach to investment rules are significant, because it has led to a range of (advanced) developing countries contributing to the spread of the higher-level investment RTAs worldwide. As shown above, Singapore, Chile and Mexico have all used NAFTA (the US BITs model) as a template for RTA negotiations on investment.

However, the devil is in the detail. While "copying" has been common, there are still variations. Among countries actively involved in investment rule-making, the most extreme example is the European Union, which has still rather limited investment rules in its RTAs, albeit progressively improved, not least compared to other capital-exporting countries. There are also a number of cases in which countries have defended their right to temporary regulatory safeguards on capital movements or have excluded commitments on performance requirements and/or the free movement of key personnel.

But, in most instances, these deviations from BITs and the NAFTA model are variations on a theme and often do not challenge the core of the model. In many cases the variations have gradually been reduced over time. It would also seem that it is often the OECD countries rather

than countries at lower levels of development that have instigated the variations. In other words, in the RTAs with Mexico, Chile and Singapore, the lower-level commitments on investment reflected the concerns or internal problems of the richer parties. Deviations from or modifications of the prevailing models are more likely to be initiated by the large developed countries; most other countries are model-takers.

But many if not most developing countries have still not jumped on the (latest) bandwagon for ambitious investment RTAs. This means we have a dualistic system. On the one side we have the early starters that have adopted rather homogeneous investment rules. On the other side we have the laggards, whose policy choice will, ultimately, determine whether a different approach to the prevailing model rules for investment will appear in the future. This will in turn depend on some powerful large host countries, such as India and China, that are already important locations for investment and may be less convinced of the urgency to agree on far-reaching investment provisions in RTAs. For example, so far MERCOSUR, and in particular Brazil, have shown little interest in following the path of Mexico and Chile. The key question in Asia is thus: will China agree to extensive investment rules, in line with Singapore's approach, in its negotiations with Australia, New Zealand and ASEAN?

Increased politicization also points to the potential of greater diversity in investment rules in BITs and RTAs. In Canada and the United States, the number of politically sensitive investor disputes has added to the initial controversy over NAFTA's investment chapter. This seems to have led to a (limited) reconsideration of elements of the NAFTA model for their agreements with third parties (Faundez, 2002). To date such domestic-politics-driven pressure on the rules has been rare, but the greater the number of disputes (and the larger the fines that governments find themselves faced with), the more likely it is that there will be a public backlash against ambitious investment RTAs and BITs – also in developing countries.

Synergies between levels of rule-making?

Starting with NAFTA, among those countries that pursue investment RTAs the extent to which BITs and BITs-plus provisions have been incorporated into RTAs worldwide seems to suggest that there has been significant positive interaction between the bilateral and regional levels of rule-making. The European Union is, however, an exception to this pattern of positive interaction, and spillover, from the bilateral to the regional level. The evolution of the European Union as a unitary actor internationally has taken place in parallel with, or even after, the surge in

BITs between EU member states and third parties, and member states have been hesitant about transferring competence in the area of investment to the Community level. BITs could therefore be said to have constituted a stumbling block for the European Community's capacity to conclude comprehensive and more ambitious investment RTAs.

The interaction of BITs and RTAs with the plurilateral and multilateral levels of rule-making suggests a somewhat more complex picture. On the positive side, one can argue that the greater the number of countries that sign BITs and investment RTAs, the easier it should be to reach an agreement on a core set of rules at the global level (Faundez, 2002; Kline and Ludema, 1997). For example, the MAI drew heavily on the NAFTA (and US BITs) model. But the experience to date has been, if anything, less encouraging. In the end the MAI failed, and so did the recent attempt to negotiate a very basic investment framework in the WTO. In both cases there have been indications that BITs have been partial responsible for these failures, because the business community and some countries were unwilling to agree on lower levels of ambition at a global level than at the bilateral or regional level (see e.g. World Bank, 2003: 124). In other words, forum shopping was more important than any positive synergies. If BITs and RTAs have already locked in domestic reform, what is the value of another layer of weaker rules? One could therefore argue that "regional negotiations clearly seem to be fulfilling the role of a partial substitute for a wider multilateral agreement" (Banda and Whalley, 2005: 17).

Ultimately, while there have been dramatic changes in governments' attitudes toward investment during the last 30 years or so that have paved the way for BITs and subsequently investment RTAs, there has been less progress in multilateral rule-making. Perhaps counterintuitively, the development of global rules has been delinked from the proliferation of BITs and investment RTAs. Moreover, there are no obvious reasons to suggest that bilateral/regional and multilateral investment rule-making will become more mutually supportive in the (near) future. Quite the opposite: one might just as well expect some negative spillover, in terms of politicization, from the heated debate on investment in the WTO. With an increasing number of investment disputes, it seems likely that BITs and investment RTAs will draw more and more public attention. And with the arrival of the laggards in RTA negotiations, not least countries with strong economic performance like China, as well as increasing fear of RTAs in some developing countries, the present trend on investment rule-making in RTAs may be increasingly challenged. Therefore, rather than the bilateral and regional model agreements providing a basis for global rules, it cannot be precluded that we will see some future backtracking in the area of BITs and investment RTAs.

Acknowledgements

The views expressed in this chapter are exclusively those of the author, who is presently working as national expert (from the Swedish Foreign Ministry) at the European Commission, and do not necessarily represent the views of the Commission or the Swedish government. The author would like to thank Steve Woolcock, Pierre Sauvé and colleagues in DG Trade and the Swedish Foreign Ministry, as well as contacts in Chile, Singapore and UNCTAD, for their helpful comments in the process of writing this chapter.

Notes

1. While these four levels are key to the development of a global framework of investment, this is not to say that unilateral reforms have been less important – quite the contrary. The evolution of transnational norms and rules has often been a product of prior changes in attitudes and policies in individual countries. Like many areas of economic policy-making, domestic and unilateral reorientation with regard to investment tends to precede international change. In some cases, of course, governments can use international agreements as a way to promote and lock in reforms when faced with tough internal opposition. The area of investment is no exception. With the exception of the exercise of coercive power by one party, some minimal convergence of interests and ideas among the parties involved is necessary for the cooperation to take place in the first place. This is also true for BITs, despite the obvious unequal power relationship that usually exists among the parties to these agreements.
2. It should be noted, however, that the United States had investment-related provisions in its Treaties of Friendship, Commerce and Navigation.
3. While being covered, the provisions on national treatment also allow for exceptions, normally through a “negative list” approach whereby the parties of BITs notify all non-conforming measures.
4. It should be noted that the first version of the Current Invisibles Code was adopted in 1951.
5. The other relevant WTO agreements do not have investment as their primary focus. However, TRIPs and the GPA, like GATS, have provisions of importance for entry and treatment of investment and the ASCM, like TRIMs, also affects the ability of governments to influence the operations of investors (Heydon, 2002).
6. At the same time, it should also be recalled that the WTO is hardly the only, or the first, multilateral forum that has endeavoured to establish international principles and rules relevant for investment. The draft Havana Charter for the creation of the International Trade Organization (ITO), for example, contained some basic provisions on investment. While the charter was never ratified, it is illustrative of the fact that there have been numerous attempts to create international investment rules prior to the WTO agreements of 1995, the Doha Development Agenda or the OECD’s MAI. These earlier efforts have often been made under the auspices of the United Nations, or members of the UN family such as UNCTAD and the ILO, as well as the World Bank. A number of initiatives stemmed from the 1970s and the ideologically charged debates over the “new international economic order”. In many cases the focus was on the right of host

countries and/or the obligations of investors. But, in the end, they proved largely ineffective. Despite similarities in purpose between the UN decisions and simultaneous efforts in the OECD, such as the declaration and guidelines for multinational enterprises of 1976, only the latter have had a significant legacy to this date. Nevertheless, from the second half of the 1990s there have been renewed calls for more UN engagement in regulating the activities of multinational firms. So far, the UN response has primarily been to promote non-binding codes of conduct. The UN Global Compact, launched by Secretary-General Kofi Annan in 1999, and the embracement of private-public partnerships at the World Summit on Sustainable Development in Johannesburg in 2002 are important initiatives to that effect. But demands from civil society to move beyond self-regulation and promotion of best practices are increasing. A recent report of the so-called World Commission on the Social Dimension of Globalization, set up by the ILO, supported these demands. The Commission went so far as to call for renewed efforts to create a framework for FDI, but that the negotiations needed to be balanced – reflecting all interests – and should be conducted in “a generally agreed multilateral forum” (ILO, 2004: 114). Thus one cannot preclude the United Nations as a rule-making body for investment in the future, although the track record of the organization underscores the many problems of finding a consensus on binding rules on economic matters in the United Nations. In the meantime, however, the bits and pieces of investment-related rules in the WTO will continue to constitute the main multilateral framework governing investment.

7. RTAs in this chapter refer to the term used in the WTO, which covers all preferential trade agreements between two or more parties that are reciprocal in nature and fall under GATT articles XXIV or V or the enabling clause. RTA is thus a generic term covering all free trade agreements irrespective of the geographic proximity between the parties and/or the number of parties to the agreements. In consequence, the concept “investment RTAs” is here used to describe those RTAs that have specific provisions on investment. However, since services RTAs will be dealt with in another chapter, investment RTAs here will only focus on rules on investment besides services.
8. The European Community early on also began to establish cooperation agreements. These were important to promote deeper economic relations, particularly through aid (development cooperation) and preferential trade. However, the earlier versions of cooperation agreements typically lacked any commitments on investment. Later versions, such as the partnership and cooperation agreements between the European Union and many Central Asian countries, do include the right to establishment for investors. But it remains unclear whether these commitments have had any practical implications for investors.
9. The US State Department and the USTR provide on their websites good overviews of the policy and its core objectives.
10. With the Middle Eastern countries, the United States has begun to establish so-called Robust Trade and Investment Framework Action Plans, under the so-called Middle Eastern Free Trade Initiative. While these are not FTAs (yet), they promote protection for investors.
11. The exceptions to this rule were the EEA as well as the Europe Agreements with Central and Eastern Europe from the early and mid-1990s. However, this is hardly surprising given these agreements’ overall aim of approximation with the Community *acquis* and, in the case of the Europe Agreements, potential future membership in the European Union.
12. It should be noted, however, that the EU RTA with Jordan did include the right of establishment, although only on the basis of MFN treatment, with a list of excluded sectors (negative list approach).

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Conclusions

Stephen Woolcock

The questions addressed

This book has looked at the interaction between RTAs and other levels of rule-making in international trade and investment regimes. Its contribution to the literature is that it addresses this question by analysing the detail of rule-making at the different levels. Whilst the interplay between regional and multilateral levels has been addressed in the debate on building versus stumbling blocks, there has been relatively little work on how the two levels interact in detailed areas/case studies of rule-making. Arguments, such as the debate over whether regional negotiations or agreements detract from multilateralism, tend to be based on broad generalizations. The approach used in each of the chapters in this volume is based on the assumption that some aspects of rule-making could well detract from multilateralism while others may strengthen multilateralism.

The chapters also all addressed the question of what elements of regional or bilateral rule-making in each policy area go beyond the WTO rules. The issue here is to be able to differentiate between different elements of rule-making. Some may go further beyond WTO rules than others. This comparison is facilitated by the analytical framework provided in the Introduction. Drawing on this framework the Introduction proposes the thesis that exceeding agreed international rules, such as WTO rules, in some elements of rule-making is likely to be more problematic for the evolution of a multilateral order than in others. For example, going beyond WTO rules in promoting transparency is benign

because this constitutes no preference and can contribute to the development of sound national regulatory policies. Going beyond the WTO in areas of substantive rule-making, i.e. to set norms or standards, can lead to divergent regional norms and result in regulatory regionalism.

Each chapter has also addressed the question of whether it is possible to establish any general differences between the approach to rule-making in the major hubs, which at the moment means North America, or more accurately the United States, and the European Union.¹

Finally, there are the issues regarding governance questions and in particular whether the approach developed in this volume can contribute to work on the question of *global subsidiarity*, or what issues should be subject to agreed rules and at which level.

Rule-making is multilevel

Before addressing these questions is worth stressing that all the case studies support the view that rule-making is multilevel. It is also clear from the case studies that there is an important interaction between rule-making in RTAs and efforts to establish multilateral rules. Rule-making is therefore, to a greater or lesser degree, multilevel in nature, so that any discussion of questions such as the desirability of common rules or policy harmonization must consider the various levels on which policy harmonization or approximation takes place. Only to discuss whether harmonization of rules makes sense in the WTO (or other global regimes) means that much of the activity in the rule-making process is missed.

The interaction between levels of rule-making is complex and does not easily lend itself to a simple classification. For example, one cannot say that RTAs (or FTAs/bilateral agreements) are clearly building or clearly stumbling blocks with regard to the evolution of multilateral rules. As in the case of customs union theory, preferential agreements in rule-making can be beneficial (to the parties, third parties and the trading system as a whole) or detrimental. It depends on the specific circumstances.

The case studies that have looked at the historical evolution of rules all show that rule-making is an iterative process that involves various levels of negotiation or agreement. This is shown clearly in the cases of investment, procurement, services, SPS measures and IPRs, although there is also evidence of some interaction in agriculture and rules of origin. This means that to understand the factors shaping rule-making in trade and investment it is necessary to consider what has been done before and what has been done on other levels. Precedent appears to play an important role in policy-making, with the provisions being often closely modelled

on rules or norms developed at other levels. Causality does not always flow in the same direction. For example, regional rules may well be used as models for wider multilateral rules, as in the cases of investment and public procurement, but there are also cases in which rules developed at the plurilateral or multilateral level are applied more effectively at the regional or bilateral level, such as is arguably the case in telecommunications services. Even in SPS measures, rule-making began at the regional level in the 1960s before being transferred to the multilateral level in the Codex Alimentarius in the late 1960s and to the WTO in 1995. Rules established in one regional or bilateral agreement are also likely to be used as a precedent for other regional negotiations. The EU approach to rules was emulated by some other regions in the 1960s and again in the 1980s. In the case of public procurement, enforcement provisions such as bid challenge were first introduced in the CUSFTA and then emulated in the EU programme on public procurement. More recently, there is clear evidence in the investment case of NAFTA-type rules being emulated by countries like Singapore, Mexico and Chile in their RTAs with non-NAFTA partners. This suggests that precedent should be seen as an important factor in shaping policy alongside other explanatory variables such as sector interests or rational political actors maximizing their utility.

Evidence of interaction from the case studies

All the case studies illustrate the dynamic interaction between rule-making on the different levels, and at the risk of some oversimplification one can group the cases into a number of categories:

- those that emphasize how divergent approaches to rule-making at the regional/bilateral level can hinder the evolution of agreed multilateral rules or threaten to undermine existing multilateral rules
- those that suggest a synergy between the regional and multilateral levels of rule-making
- those that show how the regional/bilateral level might be used strategically to shape the evolution of rules and offer an alternative to multilateral rules.

Divergent regional rule-making ...

The *rules of origin* case chapter is the classic case of how a number of regional preferential agreements can create the kind of “spaghetti bowl” effect described by Bhagwati (1993). As chapter 4 illustrates, a number of clearly distinguishable types of preferential rules of origin have emerged. Divergent rules are costly, as exporters have to comply with different rules of origin.

A closer, more detailed look at the evolution of rules of origin, however, suggests that two dominant models of rules of origin are emerging, one centred on the North American (i.e. NAFTA) rules and one centred on the EU (pan-Euro) rules. These rules are finding progressively wider application as the NAFTA parties and the European Union conclude FTAs with other countries using their respective RoO. Whilst other preferential RoO exist, and indeed there remain a large number of different rules in Latin America in particular, the data plotting the various RoO used suggest that there is a trend towards two dominant sets of rules. Garray and De Lombaerde also suggest that there might be a third model, which they call the Indian Ocean model because it is applied by a range of regions bordering on the Indian Ocean. These rules, like other preferential RoO among developing countries and some developed countries such as Australian and New Zealand, are more straightforward than the NAFTA and pan-Euro models. The NAFTA and pan-Euro systems of RoO include a range of different criteria for determining origin (or defining what is substantial transformation). It is the complexity of the more “advanced” RoO that has provided the scope for them to be used for protectionist purposes. The expansion of the dominant models may not therefore be beneficial. There also remain the difficulty and costs of having two dominant systems of RoO rather than one agreed multilateral system.

The RoO case illustrates what can happen when there are no effective multilateral rules and no ongoing efforts to establish such rules. The vacuum left by the absence of any multilateral dimension to rule-making is filled by different regional rules, which then make any efforts to devise multilateral rules more difficult because of the vested interests in retaining the existing rules.

The case of *sanitary and phytosanitary* (SPS) rule-making also shows that two dominant regional models for rule-making are emerging. As noted above, rule-making in the SPS field started at the regional level and in particular with European regional standards for food safety back in the 1950s, then moved to the international level in the shape of the Codex Alimentarius in the 1960s.² A major change in the nature of the multilateral rules occurred in the Uruguay Round when the Codex standards were effectively integrated into the trade regime with the SPS Agreement. This was done by using Codex standards as criteria in assessments of whether regulatory safeguard actions by WTO members are justified.

The SPS case appears to be an instance in which the interaction between regional and multilateral levels is predominantly shaped by the nature of domestic regulatory regimes. Chapter 3 illustrates clearly the distinction between the “scientific rationality” behind North America

regulation and the “social rationality” that has come to shape EU domestic rules. Although domestic factors shape the divergence, both the United States and the European Union seek to ensure that their own respective approaches to rule-making are promoted through the RTAs they conclude. In other words, there is some danger of the divergent approaches to rule-making leading to “regulatory regionalism” or the emergence of divergent, competing approaches to rule-making in major world regions.

In the case of SPS measures, like that of intellectual property (see below), this divergence is occurring despite the existence of strong multilateral rules in the shape of the SPS Agreement. The WTO rules are based on the scientific rationality approach used in North America, so it is pressure from the European Union for more flexibility in these rules to allow scope for the social rationality model that appears to be the greatest threat. The issue is to what extent regional or other agreements will be used by the European Union to push its agenda. The SPS case study therefore shows that agreed multilateral rules may be undermined if there are divergent approaches to rule-making that find expression at the regional or other levels. There will always be scope for differing interpretations of multilateral rules. In the SPS case this ambiguity is being used by the European Union to push its social rationality model and by the United States and Canada and others to strengthen the existing scientific rationality.

Positive synergy between regional and multilateral rule-making

The case studies of telecommunications services and public procurement point to a positive synergy between regional and multilateral rule-making in which developments at one level have complemented developments at the other. Both these case studies argue that international rules have been built up by a kind of iterative process in which regional/bilateral, plurilateral and multilateral levels of negotiation have all played a role. For example, in the case of public procurement work at the plurilateral level of the OEEC in the 1960s led to the plurilateral/multilateral code of the Tokyo Round. The approach and principles established in this code were then applied at the regional level, first in the European Union and then in the CUSFTA and NAFTA agreements. But the regional/bilateral level of rule-making introduced improvements and generally implemented the rules more effectively. Enhancements at the regional level were then incorporated in the 1994 GPA plurilateral rules.

The procurement case also shows that this synergy between the regional and plurilateral/multilateral levels was particularly marked during the Uruguay Round. This appears to have been due to the multilateral

negotiations serving as a reference point for the simultaneous regional rule-making. The procurement case was in particular characterized by very close EU-US cooperation. After the Uruguay Round the interaction between the regional and multilateral levels seems to have changed. The regional/bilateral agreements that have been concluded since the Uruguay Round appear to have been mainly used to increase the reach of the plurilateral 1994 GPA-type rules. Both the European Union and the United States seek compliance with rules that are broadly in line with the GPA in their regional or bilateral negotiations. In some cases signature of the GPA is a condition for concluding an RTA.

The case of telecommunications services exhibits some of the same features as that of procurement. This case also shows that the interaction between the levels of rule-making has tended to be synergistic, with developments at the regional/bilateral level facilitating more progress at the multilateral level. As in the case of procurement, the period during the Uruguay Round negotiations appears to have been one in which developments at the regional and multilateral levels complemented one another and resulted in the emergence of a set of broadly liberal norms for regulating the telecommunications sector. The case study illustrates this in the form of the Telecommunications Reference Paper (TRP) agreed upon within the GATS sector negotiations. This TRP has subsequently been used as the basis for RTAs, including telecommunications. Here, then, one has a similar picture to that in procurement, where (plurilateral) norms and approaches to rule-making agreed at a multilateral level but not implemented by all WTO members are used as the basis for RTAs and bilateral agreements.

The services sector more generally illustrates how the coverage of RTAs can be wider than multilateral rules. Sector commitments in services are often wider in RTAs than in GATS. This is especially the case for NAFTA-type FTAs that use negative lists to define coverage. The RTAs concluded by the European Union tend to be more GATS-compatible than GATS-plus. In the case of procurement, regional agreements tend to have greater coverage, including, for example, more entities such as the subnational purchasing entities that were excluded from the coverage of the plurilateral rules. Here there is a clear case of regional preferences, but one that is likely to be subject to erosion over time as the coverage of the WTO rules is extended.

The use of RTAs and bilateral agreements to pursue strategic, commercial aims

Finally, investment and intellectual property are two case studies that tend to show how regional-level agreements feature in forum shopping.

The case of investment illustrates how a *de facto* international regime of investment rules is emerging from a patchwork of rules at different levels. Similar to the procurement and services case studies, investment shows how the bilateral, regional, plurilateral and multilateral levels have all played a role in establishing investment rules. This case study goes back to the 1950s to show how bilateral investment treaties formed the model for investment protection agreements. The plurilateral OECD Codes were the main instrument for investment liberalization until the 1980s, when regional agreements began to include investment. Finally, the multilateral-level agreements on GATS and TRIMs provided rules for investment in services and performance requirements.

The investment case also appears to show how sequential negotiations at different levels or forum shopping can be used to promote the desired model of investment rules. Thus a dialogue between the US administration and US international business first brought together the investment protection provisions of bilateral investment treaties with liberalization rules developed in the plurilateral OECD to establish a comprehensive model for investment. This model was then applied at the regional level in the CUSFTA and perfected in NAFTA, before efforts were made to have the model adopted at the plurilateral level in the MAI negotiations from 1996 to 1998.³ When the MAI failed the United States opted to promote the NAFTA model for investment rules in regional and bilateral agreements rather than in the multilateral setting of the WTO, because opposition from developing countries stood in the way of any high-standard rules for investment in the WTO.

In contrast the EU approach to investment rules has made less use of such sequential negotiations. First the European Union favoured negotiations in the WTO over the OECD in the late 1990s, and second it has not used RTAs or bilateral agreements to promote a coherent model for investment rules. This appears to be due to “domestic” factors in the European Union relating to the question of which level of policy-making in the European Union (i.e. European Community or member states) has competence over investment in international negotiations.

Compared to the procurement and telecoms cases, therefore, investment appears to be a case in which RTAs/bilaterals offer a clear alternative to multilateral or plurilateral agreements for those seeking a high standard for investment rules. RTAs are thus likely to detract from any efforts to agree multilateral-level rules that will inevitably be much more modest. The fact that a range of developing countries have been willing to sign up to RTAs that include investment whilst blocking any substantive progress in the WTO on a wider investment agreement has contributed to this use of RTAs to push investment rules.

Intellectual property is a case notable for the fact that RTAs and bilat-

erals still include IPR provisions despite the strong, binding, multilateral rules adopted in the shape of the TRIPs agreements during the Uruguay Round. In IPRs existing international standards in the WIPO were integrated into the trading regime through the TRIPs agreement. This is analogous to the SPS case in which Codex standards were integrated into the trade rules. The reasons why this integration should occur with IPRs (and SPS) rather than in industrial, labour or environment standards, where there were equally agreed international standards, is clearly due to the balance of pressure from interest groups in a number of key countries.

But a multilevel analysis of IPR rule-making is helpful in understanding the longer-term dynamics of rule-making in this policy area. Such an approach can help to understand the factors that might influence the sustainability of the multilateral rules in IPRs. Similar to the SPS case, the TRIPs agreement in the Uruguay Round established binding rules of considerable scope and rigour, but inevitably left a number of ambiguities. An issue that emerged early on in the interpretation of the TRIPs agreement concerned the provisions of essential medicines in cases of national emergencies (see chap. 7). One of the implications of the Doha Declaration on TRIPs, which interpreted the TRIPs rules on this issue, has been a growth in the TRIPs-plus provisions in RTAs. As with other case studies it is important to look at the detail of the IPR provisions in RTAs. If one does it is possible to discern an attempt to use FTAs/RTAs as a means of regaining some of the ground lost at the multilateral level in the sense of introducing binding rules favouring the owners of IPRs. In other words the major sectoral interests, such as in the pharmaceutical sector, may have become disillusioned with the WTO following the Doha Declaration on TRIPs and subsequent developments, and shifted the focus of their lobbying to FTAs. Here one can therefore find elements of a more mercantilist forum shopping in which major interests switch between forums in order to further their own narrower agenda. In comparison, the forum shopping that has clearly taken place in investment might be seen as pursuing more liberal motives, but there is a fine dividing line between the two interpretations.

Both the US and EU RTAs have been used to promote sector interests. In the case of the United States the pharmaceutical sector appears to have captured US policy in the sense that FTAs have been used to promote the specific interests of the sector, such as on the issue of data exclusivity.

Different models of rule-making in the major “hubs”

The case studies suggest that although there are important similarities in the approaches of the United States and the European Union to RTAs,

it possible to identify a number of general distinctive features as well as important differences in detail.

The United States has tended to pursue a consistent (NAFTA) model for RTAs, one it has promoted fairly aggressively in bilateral FTA negotiations. More recently agreements such as the US-Singapore FTA have made advances on the NAFTA model and are likely to form the somewhat revised model for future negotiations.

In contrast the European Union has much less of a clear strategy or model for FTAs. There is one approach for the EU's immediate neighbours, in which closer political relations play an important role and the EU's domestic *acquis communautaire* provides the reference point for rule-making. In the case of accession states the *acquis* has an immediate bearing on the structure of association agreements. In the case of the EU agreements with its Mediterranean partners, parts of the *acquis* appear to be used as the basis for rule-making on trade and investment, but on the assumption that the developing country partners of the European Union will approach conformity with these rules only after a considerable time. Beyond its immediate neighbours, however, the *acquis* ceases to be a valuable point of reference and, perhaps as a result, the policy areas covered in RTAs negotiated with Mexico, Chile and South Africa have varied.

In very broad terms the US approach to FTAs continues to be one that might be characterized as "policed non-discrimination". In other words the US approach tends to eschew policy approximation in favour of non-discrimination, policy competition and national treatment. In this sense the degree of integration is not especially deep, although there are specific sectors or policy areas where the US-centred FTAs contain binding obligations to applied specific standards, such as in the case of IPRs, investment and some aspects of services. Outside of these sectors there is no attempt to lay down specific standards or rules, which leaves full scope for regulatory autonomy, but policy competition implies that there will be policy emulation, and the case of investment shows that this may well follow the US-determined norms. In other words non-discrimination leaves the US Congress with policy autonomy by virtue of the asymmetric relationship between the United States and its partners in FTAs, but the size and importance of the US market obliges *de facto* policy approximation to the US rules on the part of the smaller parties.

This contrasts with the EU approach that places more emphasis on efforts to establish agreed rules. This can be shown in the cases of technical barriers to trade and competition, which have not been discussed in this volume. It also finds expression in the EU's comprehensive trade agenda for the Doha Development Round, including rules on investment, competition, procurement and trade facilitation. With some notable excep-

tions, such as the Codex Alimentarius or rather the EU's attempts to inject more discretion into the SPS rules, the European Union has tended to favour the use of agreed international standards. This is also evident in the EU-centred RTA provisions on intellectual property, where RTAs refer to existing international standards when it comes to defining the substantive provisions on agreements. The European Union clearly also benefits from the asymmetric power relationship when it negotiates free trade or association agreements with third countries. But unlike the United States this power does not seem to have been used to promote a clear model FTA. By promoting region-to-region agreements the European Union also dilutes its relative power (albeit rather ineffectively to date) by encouraging third parties to negotiate jointly with the European Union.

Another area in which there appears to be a clear distinction between the US and EU approaches to RTAs is with regard to dispute settlement and enforcement. In line with the concept of "policed non-discrimination" the US-centred FTAs tend to have strong enforcement mechanisms to ensure that non-discrimination is effectively "policed". All the case studies show evidence of significantly more elaborate enforcement provisions in US-centred FTAs than EU-centred agreements, except of course when accession to the European Union is involved. Perhaps the best example is that of the investor-state dispute settlement provisions in FTAs involving the United States. Indeed, the provisions on enforcement are of such a detailed and comprehensive nature that the articles dealing with the procedural aspects of the investor-state dispute settlement take up half the "model" chapter on investment included in NAFTA and the US-Singapore FTA. But investment is by no means the only case. In procurement the United States has championed "bid-challenge" mechanisms that provide companies which believe they have been unfairly treated with direct access to reviews of contract award decisions. In intellectual property and telecommunications FTAs involving the United States have also included stronger enforcement provisions.

In contrast the agreements including the European Union do not provide for a significant role for private rights of action. There is no investor-state dispute settlement in any EU-centred FTA, and with regard to resolving disputes on other policy areas the European Union tends to rely more on interstate conciliation in Association Councils.

This comparison of the US and EU approaches to rule-making raises the question of the impact of "policed non-discrimination" or "policy approximation" in the longer term. National treatment leaves participating countries more scope for national policy autonomy *de jure*. But the effects of rigorous enforcement provisions and rights for legal persons to bring cases that interpret the inevitable ambiguities in trade agreements

can open the door to “legal activism” or litigation bringing about a *de facto* policy convergence. On the other hand, efforts to promote policy approximation have had distinctly mixed results.

Finally, in addition to this general comparison of the dominant models for deeper integration, each of the case studies shows a greater or lesser degree of divergence on specific issues. When the divergence is significant, as in the case of SPS measures, there is a danger that this will lead to divergent sets of rules as the dominant “hubs” shape rules in their own image or interests. This is most pronounced in the case of SPS measures, but there are divergences between the NAFTA and EU approaches to rule-making in each case study.

RTAs complementary to multilateralism in the 1980s and early 1990s

Taking the case studies as a whole, the general impression is that much of what has happened during the “second phase” of regionalism from the mid-1980s until the mid-1990s in terms of rule-making at a regional level has been broadly supportive of – and compatible with – multilateralism. The spaghetti bowl analogy of incompatible rules accurately describes the position in the important field of RoO. Apart from RoO, the other case studies suggest that rule-making was the result of a more complex and broadly more positive form of interaction during this period. For example, in services and government procurement work at the plurilateral and multilateral levels shaped regional/bilateral initiatives, which in turn facilitated progress towards wider multilateral or plurilateral agreements. Investment rule-making at the regional level was shaping efforts to promote new plurilateral and multilateral disciplines. In IPRs and SPS measures the focus was on multilateral rule-making. Furthermore, rule-making in RTAs resulted in greater transparency and promoted better and less discriminatory regulatory practices that generally led to more open and competitive markets. In any case regional rule-making seldom went beyond the WTO rules or agreed international norms, so that the degree of regional preference in regional rule-making was not pronounced. In other words the costly duplication and frictional trade costs that are implied by the spaghetti bowl analogy did not really apply in the other case studies.

A number of factors contributed to this compatibility between RTAs and multilateral rule-making during the period. First, active multilateral negotiations were under way on rule-making, affecting most of the case studies. There is evidence that negotiators were at pains to ensure that any regional initiatives were compatible with the emerging multilateral

rules. The existence of efforts to negotiate multilateral rules therefore helped keep RTAs within the multilateral framework. It is noteworthy that the only policy area in which there were no multilateral efforts was preferential RoO, and this was the area in which divergence continued throughout the period of the Uruguay Round negotiations.⁴

The mid-1980s to the early 1990s was also a period in which the tide of trade and investment policies was flowing towards the new liberal paradigm. This helped ensure that the RTAs did not result in preference concentration, but rather preference dilution. To put it another way, the rule-making provisions in RTAs that addressed various anti-competitive practices did not become “fortresses” aimed at keeping out third-country suppliers and investors. The preferential agreements were seen by the majority of major interests as a step towards further liberalization, as indeed they proved to be.

Third, the period under discussion was marked by close transatlantic cooperation between the United States and the European Union. These two actors had long been influential in shaping the international trade regime, and the influence of the transatlantic economic diplomacy in the field of rule-making was particularly pronounced. The United States and the European Union were the main demanders of new trade rules. In all the policy areas discussed in this volume the rules that emerged were dominated by US and EU interests and the need to accommodate these two main protagonists. It is therefore not surprising that the two approaches remained broadly compatible.

Post-1995 developments more questionable

There are reasons to believe that the “current phase of regionalism”, starting in the early to mid-1990s, looks rather more threatening than the “second phase” from the mid-1980s to the early 1990s. There are a number of reasons for this. First, there is the significant growth in the number of RTAs starting in the early 1990s. Second, as the case studies all indicate, there has been an increased tendency for RTAs to “go beyond” the existing WTO provisions in more and more areas. Third, a number of the case studies suggest that the use of RTAs in forum shopping has been on the increase. These developments combined with the fact that none of the factors mentioned above, which helped ensure RTAs and multilateral rule-making were compatible in the earlier period, seems to be as important today. The DDA’s ambition on rule-making is far less than was the case in the Uruguay Round. The general tide of liberal policies is not as strong as it was, and transatlantic cooperation on rule-making is neither particularly successful, despite repeated efforts to

strengthen it, nor sufficient to shape international rule-making in the way it was during the Uruguay Round.

Governance issues

The introductory chapter also raised the central but elusive issue of global subsidiarity. In other words, at what level should common rules be adopted, if at all, or what type of rule-making should be done at which level? On this topic it is possible to make only general comments given the relatively limited scope of the empirical work reported in the case-study chapters. But one or two quite interesting points emerge.

First, there is evidence that movement between levels of rule-making is not all in one direction. In other words, it is not a question of issues being first addressed at a bilateral, then regional and then multilateral level. The movement may be downwards as well. More importantly, one cannot assume that rule-making is permanently designated at the multilateral level once strong multilateral rules have been adopted. In the case of SPS measures and IPRs the Uruguay Round established strong multilateral rules, but in both cases regional and bilateral agreements have subsequently used remaining ambiguity in the rules to “relegate” rule-making back to the regional or bilateral level. If this happens with strong rules, then one must expect the same to happen in all areas of multilateral rule-making. This “relegation” of issues does not mean that the WTO is a failed experiment in multilateralism. It does, however, illustrate that rule-making is indeed multilevel, and to some degree in a state of flux between the different levels.

Second, breaking down rule-making into its component elements as set out in the analytical framework suggests there is scope to develop criteria for a “division of labour” between different levels according to the different functions of the rules. In other words, global subsidiarity should not be seen as immutable decisions on the designation of issues to the bilateral, regional, plurilateral or multilateral levels of rule-making, but decisions on which level is most suitable for a particular function. Just how this might work is set out in the following section as it concerns policy prescription.

Prescription

The introductory chapter set out a number of premises on which this volume has been based. One of these was that the international trade and investment regimes of the future will, as in the past, be shaped by rules

devised at different levels. The key issue therefore is how to ensure that these are compatible. Arguing for multilateralism over regionalism does not have much operational value given the pervasiveness of regional agreements. In any case, there is evidence that rule-making at a regional level may sometimes be beneficial for both the regional partners and third parties.

In the literature on RTAs there is a view that deeper integration rules may not constitute such a risk of trade diversion as tariff preferences or other border measures. This view rests on the assumption that rules can enhance transparency and predictability and generally promote better regulation in economies. This benefits the countries concluding an RTA, and also third parties, which can trade and invest in the markets concerned with greater predictability and be subject to less discrimination, discretionary interference and even corruption. At the same time there is clearly scope for preferential rule-making to result in trade or investment diversion analogous to classical trade diversion resulting from tariff or other border measures. As pointed out above, there is a further danger of RTAs resulting in “regulatory regionalism” in which competing regional approaches result in divergent rules for trade and investment. The challenge is therefore to provide operational guidelines for regional agreements that maximize the beneficial effects but minimize the risk of adverse effects on the RTA parties, third parties and the multilateral system.

The contention here is that this can be done by breaking down rule-making into its constituent elements and assessing the impact of each. Consideration of the impact of various elements of rule-making in RTAs can then contribute to the ongoing discussions on the impact of RTAs and what sort of new disciplines, if any, should be applied to RTAs. The latter is being considered in the WTO Committee on Regional Trade Agreements (CRTA) on how article XXIV of GATT and article V of GATS might be made more operational with regard to rule-making aspects of trade.⁵

Whilst rule-making can benefit all interests by providing a predictable framework for international trade and investment, just as national regulations do for each national economy, it can also be used to promote vested interests. This can happen at the regional and multilateral levels just as it can at the national level. Unfortunately, rule-making at the international level has been captured by vested interests, or at least skewed in favour of certain interests, such as in the case of the TRIPs agreement in the Uruguay Round. This has contributed to the opposition to new rule-making initiatives from developing countries that have understandably become sceptical of the motives behind proposals for new rule-making initiatives at the multilateral level.

The areas in which rule-making at any level is likely to be benign rather than serve specific vested interests are those that promote better regulation. Note that the issue here is better regulation, and not necessarily less regulation. Rule-making that promotes greater transparency falls into this category, as do rules that promote “due process” or fair and open decision-making regarding the application of rules. Provisions in regional agreements that promote such transparency of rules or procedures will also not constitute a significant “preference”, since the information and access will tend to be available to all. Regional or preferential agreements that go beyond the WTO with regard to transparency or due process are therefore likely to have a benign effect. Such “WTO-plus” provisions in RTAs should benefit the parties to the agreement and will not pose a challenge to the trading system. Indeed, regional transparency rules tend to be more effective than those in the WTO, for example, and will therefore further the aims of international transparency.

Regional agreements do constitute a preference, however, if their coverage exceeds that of the multilateral rules. For example, if the sectoral commitments in services or investment exceed those made in GATS there is clearly a regional preference. Likewise if entity coverage is greater, with the effect that more regulators or more levels of government are covered by rules, such as in regional public procurement rules compared to the (plurilateral) Government Procurement Agreement (GPA), there is also a regional or bilateral preference. If the regional agreement only exceeds the WTO in terms of coverage but retains the same rules, the preference is subject to erosion provided further progress can be made in multilateral negotiations. In other words there may be a temporary disadvantage for third parties and some trade or investment diversion, but this will not constitute a major threat to the integrity of the multilateral system as long as regional liberalization has the effect of diluting protectionist preferences rather than consolidating them. Consolidation of protectionist preferences occurs when, for example, sectors or subsectors are excluded from liberalization at the regional level and thereby create vested interests that oppose further multilateral liberalization.

In most cases negotiations on coverage will form part of a reciprocity-based bargain. This is in line with traditional trade negotiations and probably also inevitable for sector coverage of rules. But the rules themselves should be agreed, and not forced on unwilling parties through trade-offs between issues. Multilateral rules will only hold if the parties are committed to them and recognize the benefits of such rules. The use of deals linking issues, such as the acceptance in the Uruguay Round of multilateral rules on IPRs in the TRIPs agreement in return for market access for textiles and clothing, is not a solid basis for multilateral trade rules.

More problematic is the case when regional or bilateral agreements es-

tablish substantive regulatory norms or standards. Given the difficulty negotiating on rules in the WTO with 150 members, regional rules that go beyond agreed existing international rules risk resulting in regulatory regionalism or the emergence of divergent regional substantive norms or standards. Such a divergence will then jeopardize the prospect of agreement on international rules in the future, because the regional norms will become entrenched and difficult to harmonize. As noted above, RoO are a case in point, where the vacuum left by the absence of multilateral rules was filled by a plethora of divergent regional rules that are now being “rationalized” into a number of dominant types. The same could be said for agricultural liberalization prior to the Uruguay Round Agreement on Agriculture, and then again after the attempt of the AoA to consolidate.

Substantive rules at the regional level should therefore be treated with some caution. On the other hand, some barriers to market access cannot be adequately addressed unless there is some degree of policy approximation or harmonization. This has been shown to be the case in deeper integration agreements, as well as in the WTO in the shape of rules and standards for telecommunications, for example. Harmonization of rules or standards at a regional level can not only facilitate enhanced market access within the region, but the fact that third-country suppliers need only satisfy one rule or standard should also benefit these suppliers. Regional rules can, as noted in the Introduction, have an effect equivalent to trade creation in such cases. Ideally, therefore, substantive rules or standards should be based on agreed international standards so as to gain the benefits of harmonization or approximation whilst minimizing the risk of regulatory regionalism.

The test as to whether this prescription is relevant is whether there are adequate international norms available. In the case studies considered this condition is only partially met. There are no agreed international rules for preferential RoO. There are agreed international rules for the protection of intellectual property and food safety, but these are not considered adequate by the United States and the European Union respectively. In the case of IPRs the United States does not appear willing to accept existing agreed international substantive standards for IPRs (see chap. 7). In the case of SPS measures the European Union is not willing to accept the existing Codex standards as adequate. This prescription would therefore imply that the United States use only existing international standards for intellectual property in its FTAs, as the European Union does, and the European Union accept Codex rules for food safety as the United States does in its FTAs. In the case of government procurement and telecoms services there are plurilateral rules agreed under the WTO framework. This seems a reasonable basis for the substantive rules in RTAs. With more and more difficulties getting all 150 WTO members

to agree to common standards, the use of rules agreed by a majority of WTO members or even the major WTO members would be better than nothing and should help ensure that the rules used in regional agreements do not diverge. The search for perfection in terms of a purely multilateral set of rules may well be detrimental. This suggests therefore the (continued) use of plurilateral rule-making. As this volume has shown, rule-making is and is likely to continue to be multilevel in nature, so there is a need to recognize this and accept that a single undertaking in the WTO does not mean the end to plurilateral approaches. Indeed, there are *de facto* forms of plurilateralism even under the WTO, such as in the Telecommunications Reference Paper, not to mention the GPA, despite the single undertaking concept.

Finally, it would be necessary to maintain a watching brief on the interpretation of regional rules by regional legal or quasi-legal bodies. Just as WTO legal activism can lead to interpretations of the rules that go beyond what has been agreed by the General Council of the WTO, the interpretation of rules at a regional level, in particular the scope for regulatory safeguards, can raise questions about the compatibility of the emerging regional regimes and the respective WTO doctrine.

In summary, an assessment of the detailed elements of RTAs can help in assessing the likely long-term impact of the rule-making aspects of these agreements on the trade and investment regimes. If the emphasis is on transparency and other provisions that are likely to promote good regulatory practice then regional agreements should be complements to the multilateral rules. With regard to substantive rules or norms, RTAs should be judged by whether they are implementing existing agreed international norms. If this is the case then again they are more complementary to the multilateral system rather than in conflict with it, even when the norms and rules have only been adopted as plurilateral agreements. When regional rules diverge from existing rules there is a danger of divergent regulatory regionalism developing. Whatever happens, there remains a need for rule-making to progress at the multilateral or at least plurilateral level. Otherwise regional preferences through the coverage of rules will not be eroded and there will be no agreed rules to implement at the regional level.

Notes

1. Based on RTAs notified to the WTO it is projected that the European Union will be involved in 30–36 RTAs and North America in 10–19. The role of these two hubs is especially important in rule-making, because many of the proposals for inclusion of rules in RTAs emanate from them.

2. International industrial standards-making has also been driven by European regional initiatives, with the International Standards Organization and the International Electrotechnical Commission built on European foundations.
3. The US negotiators made a clear and conscious choice in favour of the plurilateral OECD as a forum rather than the multilateral WTO. This was strongly influenced by past vain attempts at establishing rules. In the late 1800s, the 1920s, at the time of the International Trade Organization (ITO) and in GATT the United States had sought agreed international rules for investment but failed to get them. This experience shaped the US approach because a genuine multilateral forum in the WTO might ensure more countries signed up to any agreement, but the rules would have been weaker.
4. In terms of rule-making one could argue that the outline of 90 per cent of the results of the Uruguay Round were discernible by the time of the Dunkel text of December 1991. After this date the issue was essentially negotiations on reciprocal market access or the coverage of the framework rules, such as in services. From this point on those with interests in specific areas, such as investment, would have a pretty good idea of what the Uruguay Round would and would not deliver. It is interesting to note that the increase in RTA activity and interest starts in the early 1990s. This was due in part to the FTAs with the Central and East European countries, as part of the post-Cold War reordering of trade and investment, but was possibly also partly due to a realization that the WTO would not deliver all that was sought in terms of rule-making.
5. Currently there is no consensus on how to go about interpreting the provisions in GATT article XXIV and GATS article V with regard to regulatory measures.

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