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Legal Frameworks for North-South RTAs under the WTO System

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CONTENTS

I. Introduction

Since the 1990s, there has been a global trend toward bilateral and regional trade arrangements. The number of such arrangements that have been formed, or are currently being negotiated, has dramatically increased, and consequently, at present almost all countries are party to such arrangements. One of the characteristics of recent regional trade agreements (RTAs) are their comprehensiveness. Not only do they cover the reduction or elimination of tariffs and other non-tariff barriers on the trade of goods and services, but they also cover broader elements such as investment rules, intellectual property rights and so on.

Besides this comprehensiveness, a noteworthy feature of recent RTAs is that those formed between developed and developing countries (hereafter referred to as North-South RTAs) are on the increase in terms of both number and impact. In the Asian region in particular, North-South RTAs have become a hot issue owing to changes in Japan's trade policy. From the late 1990s, Japan actively began to promote RTAs in order to strengthen cooperative relationships between itself and other countries in the region. RTAs including Japan and other Asian countries inevitably fall into the category of North-South RTAs. In negotiations with Japan, Asia's developing countries seem to show an attitude that they do not necessarily oblige equal liberalization to Japan.

Under the current legal system of the World Trade Organization (WTO), there are two categories of rules on RTAs in the area of trade in goods: the first is based on Article XXIV of the General Agreement on Tariffs and Trade (General Agreement), which generally applies to all RTAs; the second is based on the so-called Enabling Clause, which, in exceptional circumstances, provides special and differential treatment (SDT) for RTAs among developing countries. Although both categories allow for deviations from the WTO guiding principle of non-discrimination, the necessary conditions of RTAs negotiated under the rules differ considerably. The criteria stipulated in Article XXIV are much stricter than the ones of the Enabling Clause. This dualistic legal framework means that developing countries tend to believe that they can be exempt from equal liberalization when they negotiate bilateral or regional RTAs with developed countries.

The kind of rules that govern North-South RTAs influences the kind of contents

and levels of liberalization to which the parties of such RTAs agree. In order to clarify the applicable rules on North-South RTAs, this paper considers why rules on RTAs and the concept of SDT were incorporated into the GATT/WTO legal framework so as to permit the derogation of most-favored-nation (MFN) obligations (Parts I and II respectively). This paper also looks at existing practices of North-South RTAs (Part III) and the way in which North-South RTAs are made compatible with WTO rules (Part IV).

II. Applicable Rules on RTAs

The General Agreement on Tariffs and Trade (GATT)[1] system was established in order to prevent the discriminatory trade practices contributed to the development of economic blocs before World War II. The GATT, therefore, adopted non-discrimination as a fundamental principle. An unconditional MFN clause was incorporated into Article I of the General Agreement, as this was conceived as the most effective measure for applying the non-discrimination principle to actual trade practices. Thus, the GATT strictly confined preferences to the practices that existed when it was established,[2] meaning that it would not in principle permit the creation of any new preferences. However, there is no principle without exceptions, and RTAs are formally recognized as exceptions to MFN obligations under the GATT/WTO system.

II-1. Background: Approving RTAs as Exceptions to MFN Treatment

In Article XXIV of the General Agreement, exceptions to MFN treatment are provided in three situations: traffic frontiers, Customs Unions (CUs), or free trade areas. It is the latter two arrangements which are usually referred to as RTAs. Even an interim agreement leading to the formation of a CU or a free trade area is included in this provision. As to frontier traffic and CUs, they have been recognized as exemptions to MFN obligations in many bilateral commercial agreements for more than two hundred

[1] Though the GATT was not originally an institution established under a treaty-based instrument like the United Nations, but merely a general agreement, it has had an actual secretariat and has functioned as a de facto international institution. In order to distinguish these two aspects of the term, in this paper, the term “GATT” will mean institution and the term “General Agreement” will mean international agreement.

[2] Article I simply allows preferential trading arrangements in force at the time of GATT’s establishment to last as exceptions to the MFN principle with the conditions listed in the Annex. Almost all are imperial preferences or preferences between neighboring states.

years. At the drafting process of the General Agreement, therefore, the inclusion of these exceptions in the agreement was uncontroversial.

Besides frontier traffic and CUs, the GATT broadly permits the formation of free trade areas as an exception to MFN treatment. Why did the GATT let a provision for free trade areas come into the agreement? The first Draft Charter for the International Trade Organization (ITO), which was put forward by the US government in 1946, recognized only CUs as exceptions to the MFN rule.[3] It was at the drafting conference that the original concept of free trade areas appeared (GATT 1970: 798). In 1947, developing countries proposed the initial concept of free trade areas where "two or more developing countries might be prepared to abolish all trade barriers among themselves, though not wishing to construct a common tariff towards the rest of the world" (Haight 1972: 393). Developing countries might have thought that non-discrimination principles did not always benefit them and a certain degree of preferential treatment would be necessary in order to promote their economic development. Moreover, they needed schemes more flexible than CUs because they regarded these as very poor measures for utilizing preferential treatment due to their strict conditions.[4] The concept of a free trade area received support from many participants in the drafting session, especially from European countries, and it was successfully incorporated into the draft agreement.

European countries regarded this concept of free trade areas as an extension of the bilateral preferential trade arrangements that had been a common practice in Europe before World War II. It was uncertain whether the first proposal of free trade areas had reciprocity as a feature. However, it came to absorb reciprocity as a feature after the European countries took the initiative and introduced their own free trade area. The GATT included this provision because it was recognized from the outset that member countries would want to establish certain reciprocally-preferential economic relationships (Baucus 1989: 19). In addition, it was pointed out that most of the GATT contracting parties had in effect taken the position that some discrimination would help to promote trade liberalization and that not all discrimination was bad (Haight 1972:

[3] In March 1948, the ITO Charter was adopted at the United Nations Conference on Trade and Employment in Havana. Since only two countries ratified the Charter, the plan to establish the ITO lost momentum. However, in order to enforce the results of the round, parts of the ITO Charter were selected to form the core of the General Agreement.

[4] In order that a preferential arrangement is authorized as a CU, it should meet at least three requirements: the elimination of duties among parties, the setup of common external tariffs, and the harmonization of foreign trade regulations.

394; Hudec 1991: 175–6).

During the ITO drafting session, the United States intended that preferences should be restrained and ultimately eliminated. Yet the US government also intended to apply the General Agreement as widely as possible in order to enhance its effectiveness. To realize this second objective, it was considered necessary to involve as many countries as possible. However, many countries attending the drafting conference placed more value on "reciprocity" than "non-discrimination." With the purpose of convincing nations to join the GATT, the drafters had to include several measures that would allow nations to pursue their national interests and ease their fears about yielding sovereignty to an international body (Baucus 1989: 5). As a result, the United States compromised on the issue of including new preferences and accepted free trade areas as an exception to the unconditional MFN clause.

The flexibility in the MFN obligation of the General Agreement was quite necessary (Hudec 1991: 175). Free trade areas were adopted in Article XXIV so that they could function as a control valve to reconcile the internal conflict between MFN treatment and reciprocity in the fundamental GATT principles.

II-2. General Rules on RTAs under the WTO System

In order to allow the establishment of RTAs as an exception to the guiding principle of non-discrimination, the GATT/WTO, depending on the type of RTAs, imposes specific conditions through three sets of rules. These are: Paragraph 4 to 10 of Article XXIV of the General Agreement,[5] Article V of the General Agreement on Trade in Services (GATS), and the so-called Enabling Clause. These are the only general rules regarding RTAs which have legally-biding power in the current regime of international economic law.

Article XXIV of the General Agreement

The provisions of Article XXIV of the General Agreement provide the basic rules on preferential arrangements covering trade in goods. A CU is defined as "the substitution of a single customs territory for two or more customs territories" between the territories of

[5] The original Article XXIV in the General Agreement is complemented by an additional Article XXIV in Annex I that describes notes and supplementary provisions. It is also clarified in the Understanding on the Interpretation of Article XXIV of the GATT 1994.

contracting parties, while a free trade area is described as "a group of two or more customs territories in which the duties and other restrictive regulations of commerce are eliminated" (General Agreement, Article XXIV: 8). In order to be identified as a CU or a free trade area, an agreement has to meet the condition, set out in the provisions of Article XXIV, that is usually phrased as "substantially all the trade." This requires that duties and other restrictive regulations of commerce must be eliminated on "substantially all the trade" between the constituent territories of a CU or a free trade area in products originating in such territories.[6]

Besides the condition, "substantially all the trade," Article XXIV further stipulates certain criteria for the formation of RTAs.

- A "stand still" condition: the duties and other regulations of commerce should not on the whole be higher or more restrictive than the general incidence of the duties and regulations of such commerce applicable in these countries prior to the formation of a CU or free trade area.
- "A reasonable length of time" condition: any CU or free trade area should be formed within "a reasonable length of time." This ambiguous term has lately been clarified to mean exceeding ten years only in exceptional circumstances.
- All RTAs and interim agreements must be notified to the Council for Trade in Goods (CTG) and be examined by the Committee on Regional Trade Agreements (CRTA) for their conformity to these criteria.

In addition to these criteria, a panel report in 1994 clarified several other conditions for RTAs (GATT 1994).

- Because of the use of the plural in the phrase "between the constituent territories" in Article XXIV: 8, all parties should liberalize their trade in products on a reciprocal basis.
- Article XXIV only covers RTAs "between the territories of contracting parties." In other words, any RTA involving a non-contracting party cannot be understood as an RTA in the terms of Article XXIV and, consequently, cannot be justified as an exception to MFN obligations. In order for RTAs involving

[6] Because of its unclear language, calculating "substantially all the trade" is at the center of the argument.

non-members to be approved, the procedure is expected to be in accordance with Article XXIV: 10.

The lack of precision and clarity of requirements generates problems in applying these rules to RTAs. The examination mechanism regarding the consistency of RTAs to WTO rules does not function properly, which exacerbates the problem. Accordingly, de facto deviation from GATT discipline and such a situation can and will be able to be observed as partial or discretionary RTAs have spread out.

Article V of the GATS

The GATS, which entered into effect in 1995 as a result of the Uruguay Round, stipulates MFN treatment as a general obligation under Article II, whereas the provisions of Article V allow member countries to enter into bilateral or regional agreements to liberalize trade in services. The basic conditions are equal to the terms of Article XXIV of the General Agreement:

- The "substantially all the trade" condition: agreements shall have substantial sectoral coverage;
- The "stand still" condition: agreements shall eliminate existing discriminatory measures and/or prohibit new or more discriminatory measures;
- Agreements shall be notified to the Council for Trade in Services (CTS).

Importantly, provisions of Article V of the GATS cover all RTAs concluded in the area of trade in services regardless of the status of its participants in the WTO. Whoever the parties to an RTA—that is North-North, South-South or North-South RTAs—every RTA is treated equally. This is the distinctive feature of Article V of the GATS that differs from the rules of RTAs in the sphere of trade in goods.

The Enabling Clause

The GATT decision by the contracting parties on November 28, 1979,[7] usually referred to as the Enabling Clause, legalized derogations from MFN obligations in favor of developing countries. With respect to RTAs, paragraph 2(c) of the Enabling Clause

[7] The formal title of the decision is "Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries." The decision was one of result of the Tokyo Round (1973–9).

allows preferential trade in goods among developing countries without the need to fulfill all the conditions of article XXIV.[8]

- The Enabling Clause covers regional or global arrangements entered into "amongst less-developed contracting parties" for the mutual reduction or elimination of tariffs and non-tariff measures "on products;"
- Trade arrangements among developing countries are designed not to raise barriers to or create undue difficulties for trade with any other contracting parties;
- Trade arrangements among developing countries shall not constitute an impediment to the reduction or elimination of tariffs and other restrictions to trade on an MFN basis;
- Trade arrangements among developing countries are to be reported to the Committee on Trade and Development (CTD). Notification and examination of the consistency of such arrangements with WTO rules are not essentially required.[9]

The introduction of the Enabling Clause into the GATT/WTO legal framework implies approval of two different rules applicable to preferential trade arrangements in goods. Which rule applies to the relevant RTA depends on the status of participating parties. RTAs that include even one developed country as a participating party are governed by Article XXIV, whereas RTAs between developing countries fall into the Enabling Clause category. From the viewpoint of the current WTO legal system, North-South RTAs are covered by Article XXIV. However, as the number of North-South RTAs increases, and as recognition of the usefulness of such RTAs spreads among developing countries, these countries are requesting extensions to the applicable range of the Enabling Clause to North-South RTAs.

[8] The lack of definition of a "developing country" within the GATT/WTO leads to another problem of what countries can enjoy the rights granted by these provisions.

[9] However, some cases were or are examined for their compatibility with WTO rules by the related committee. For example, Mercado Común del Sur (MERCOSUR) is under examination by the CRTA.

III. Normative Influences of SDT on RTAs

The provisions of Article XXIV were originally incorporated into the General Agreement at the drafting stage, as a result of a compromise between two principles, non-discrimination and reciprocity. By contrast, the Enabling Clause was added to the GATT/WTO legal framework later, as a consequence of the strong demand for preferential treatment in favor of developing countries. It should be noted that the grounds for justifying such a deviation from the MFN obligation through the Enabling Clause differ from the grounds for such a justification under Article XXIV. The Enabling Clause is based on the SDT normative guideline in favor of developing countries.

III-1. The Developmental Process of the SDT Concept

As widely recognized, the GATT adopted a non-discrimination principle as the most appropriate concept in order to establish a stable and liberalized international trade system. An unconditional MFN clause was deemed the only approach for realizing the non-discrimination principle in multilateral trade. These thoughts reflected the prevailing ideas when the General Agreement was drafted—that "MFN treatment transposes equality under international law into the economic field" (Espiell 1971: 35). The principle of sovereign equality under traditional international law was based on the assumption that each nation state had identical abilities. This assumption did not take into account de facto inequality, such as different stages of development between countries. It essentially supposed that international society consists of homogenous and consequently equal nation-states, and it considered that de facto inequality could be eliminated as long as it did not significantly prevent nation states from excising their rights (Ida 1985: 612).

In the mid-1950s, however, a new idea arose against this entrenched belief. Its proponents argued that the single legal framework based on a false assumption of equality between states should be replaced with a two-tier structure: one tier would apply to relations among developed countries, while the other would apply to relations between developed and developing countries. This idea of differential treatment was based on the argument that equal treatment could secure equality only among identical

parties, but it was only unequal treatment which could correct inequalities between different parties. The resulting view was that "the operation of a MFN clause is not an adequate or expedient means of ensuring that international trade becomes an instrument of progress, especially for the benefit of the developing countries, as it is now universally agreed that it should be" (Espiell 1971: 29).

The original General Agreement did not include any SDT provisions for developing countries, even though the ITO Charter, which was a prototypical agreement of the General Agreement, permitted, in exceptional circumstances, the exemption of developing countries from the Charter's legal obligations on the basis of "economic development."[10] The developing countries were never satisfied at receiving equal treatment under the initial GATT system, and began to advocate obtaining special status. The active and organized demanded to have provisions securing SDT for developing countries started in 1964 when the first conference of the UNCTAD was held. In this sense, the UNCTAD was aimed at restructuring the ITO Charter (Kasahara 2001: 25–6). In the following year, the GATT added provisions regarding trade and development, as Part IV of the General Agreement, with the strong backing of the UNCTAD.[11] In response to the addition of Part IV, it was Australia that first provided preferences to developing countries on a non-reciprocal basis. The noteworthy change that took place with the addition of Part IV was the shift of relations between developed and developing countries from reciprocal to non-reciprocal relationships. Article XXXVI specifies that "developed countries do not expect reciprocity for commitments in trade negotiations to remove tariff and other barriers to the trade of the less developed contracting parties."

Tissue (1987: 29) considers that the incorporation of Part IV introduced a radical change to GATT principles. Hudec (1987: 58) also points out that "the major significance of Part IV was its force as an agreed statement of principle." At the level of rules, however, there was no immediate change because Part IV did not impose any legal obligations on developed countries to grant SDT to developing countries.

[10] The ITO Charter contained exceptional provisions in favor of developing countries that were approved because they were expected to help with the economic development of these countries. For example, Article XV of the ITO Charter provided that "new preferences could be granted in the interest of economic development or reconstruction of one or more of the parties." However, these articles relating to developing countries were not included in the General Agreement (Hudec 1987: 7–18).

[11] These movements had as their theoretical background the idea of international law of development. Tovias (1988: 513) describes the reason why SDT in favor of developing countries was accepted in the General Agreement: "because it was considered to be a step in the right direction, namely switching gradually from a principle of formal non-discrimination to substantive-discrimination."

Preferential trade arrangements in favor of developing countries were still a voluntary option. Delegates from developed countries tended to regard Part IV as a general and elusive declaration and, consequently, as having no value in a negotiating venue where governments dealt in concrete and meaningful trade actions (Hudec 1987: 58). In such circumstances, the enjoyment of the benefits of trade preferences for developing countries was very precarious. Subsequently, developing countries merged their different goals and aimed instead at obtaining legal grounds for a Generalized System of Preferences (GSP), which brought benefits to all developing countries, albeit to varying degrees. The fact that Part IV was not legally binding also led to legal instability for developed, preference-giving countries. They were still bound by their treaty obligations under Article I, and the implementation of a GSP would violate this MFN clause.

On June 25, 1971, the GATT granted a "waiver" for a ten-year period to developed, preference-giving countries which could justify their deviation from the MFN clause on the basis of having to implement a GSP.[12] Soon after, the European Community (EC) put the first GSP scheme into operation, followed by Japan, the United States and other developed countries. However, the utilization of a waiver procedure, pursuant to Article XXV: 5, to approve a GSP implied that non-reciprocal preferential treatment was still considered a special case in the GATT legal system (Takashima 1995: 271). It was not until the adoption of the Enabling Clause in 1979 that developed countries could avoid criticism that they were deviating from their obligations under the MFN clause in giving SDT to developing countries.

In the 1960s and 1970s, the style of negotiations in the GATT was conditioned by the structural outline of contraposition between developed and developing countries. In order to introduce the new legal relationship embodied in the SDT concept, therefore, unified cooperation among developing countries was needed. However, differences among developing countries had the potential to weaken their bargaining power at the GATT. As a result, demands for SDT inevitably included the idea that developing countries should be treated as a unit and that every developing country could benefit from SDT, which meant non-discrimination among developing countries. A GSP scheme, through which developed countries would grant tariff preferences equally to all

[12] The incorporation of a GSP into the GATT system was strongly attributed to the UNCTAD elaboration of the "Agreed Conclusion of the Special Committee on Preferences," which initiated the establishment of GSPs in the global trading system.

developing countries, albeit allowing for the possibility of providing more generous preferences to all least-developed countries, most clearly reflected this feature. Besides non-reciprocity between developed and developing countries, MFN treatment governing relations among developing countries was adopted as another operating principle of SDT.

III-2. The Introductory Process of the Enabling Clause

The Enabling Clause has created a permanent legal basis for SDT in favor of developing countries. However, it does not cover all forms of preferential treatment from developed to developing countries, being confined to only three types of trade preferences:

(a) preferential tariff treatment accorded by developed contracting parties to products originating in developing contracting parties in accordance with a GSP;
(b) regional and global arrangements amongst less-developed contracting parties for the mutual reduction or elimination of tariffs and non-tariff measures on products imported from one another;
(c) special treatment for the least developed among the developing countries in the context of any general or specific measures in favor of developing countries.

The coverage of the Enabling Clause shows that it does not establish a legal basis for trade preferences from developed countries to limited groups of developing countries, even if they are formed for development-oriented purposes. Thus, the question arises as to why the Enabling Clause does not cover North-South RTAs. In order to clarify this issue, it is helpful to observe the process by which the Enabling Clause was finally incorporated into the GATT legal system.

The Enabling Clause was primarily aimed at granting a perpetual legal basis to two types of preference schemes—the GSP and trade preferences among developing countries—and the application of MFN treatment to these two schemes was waived for ten years from 1971. Because the waiver expiration date was approaching, the implementation of a GSP by developed countries and the exchange of tariff preferences among developing countries would be in violation of their treaty obligations. Therefore, there was a pressing need to find a way by which these preferences could be made

compatible with Article I of the General Agreement. In this sense, the coverage of the Enabling Clause was strongly influenced by the fact that the GATT adopted waivers on MFN treatment in 1971.

When the GSP waiver was recognized, some developing countries brought forward an objection to the *generalized* system from which all developing countries could benefit evenly. Some limited groups of developing countries had already enjoyed preferential market access to developed countries. For example, eighteen African countries were allowed preferential tariff rates in the EEC markets through the Yaounde Convention, which was concluded in 1963.[13] These countries were concerned about losing existing preferences and insisted that a GSP should provide them with at least equivalent advantages as compensation for sharing their preferential market with other developing countries and to redress any adverse effects resulting from the introduction of a GSP (Krishnamurti 1971: 50). In reality, they might want to call for SDT on North-South preferential arrangements for limited group of developing countries. However, the African countries finally accepted the generalized form of preferences in order to establish a GSP in the GATT framework. For developing countries as a whole, the highest priority was put on the introduction of a GSP.

The number of North-South RTAs was still very small after the waiver for a GSP was approved, even though some cases existed, such as the arrangement of the first Lomé Convention between the EC and African, Caribbean and Pacific (ACP) countries in 1976. At the time, North-South preferential schemes were not such a hot item.[14] Therefore, there was almost no discussion in the GATT as to whether North-South RTAs should be covered by the Enabling Clause.

So, why were South-South RTAs, let alone a GSP, included in the Enabling Clause? In the context of SDT, much more attention was likely to be paid to a GSP than preferential arrangements among developing countries. However, the latter were

[13] The Yaounde Convention was an ancestor to the Lomé convention. Eighteen members are former African colonies of EEC member states: Burundi, Central African Republic, Cameroon, Chad, Congo (Brazzaville), Congo (Kinshasa), Dahomey, Gabon, Ivory Coast, Madagascar, Mali, Mauritania, Niger, Rwanda, Senegal, Somalia, Togo, Upper Volta. These African countries set up the "Associated African States and Madagascar (AASM)." However, because this agreement was based on the principle of reciprocity, members of AASM had to undertake obligations to provide preferences on imports from the EEC (Maeda 2000: 17–20).

[14] It was after the Enabling Clause was introduced that attention was paid to the Lomé convention for its geographical discrimination (Tovias 1988: 504).

deemed to have a significant effect on economic development[15] and were concluded in 1965 after the addition of Part IV to the General Agreement. For example, India, the United Arab Republic (present Egypt) and Yugoslavia signed a preferential trade agreement on December 23, 1967.[16] Another example, evaluated as "the most important preferential arrangement among developing states concluded within the framework of the GATT" (Yusuf 1980: 491), was the Protocol Relating to Trade Negotiations among Developing Countries (PTN), which was enforced in 1973. These two arrangements were not intended to fulfill the criteria for forming a CU or an FTA as stipulated under Article XXIV. Nor did Part IV of the GATT grant any legal basis for preferential arrangements among developing countries. A working party was established at the GATT to discuss the measures to be taken regarding a preferential trade agreement among India, the United Arab Republic and Yugoslavia, and the GATT permitted these countries to proceed with their agreement by a 1968 *decision* but not by granting a waiver (GATT 1969: 17).

It is impossible to compare RTAs among developing countries with RTAs among developed countries. Developing countries have come to demand that their RTAs should be authorized even when they fall short of the conditions stipulated in Article XXIV. Moreover, when Part IV of the General Agreement came into force, a distinction was made between the possible systems applicable to negotiations between developed and developing countries and those applicable to negotiations among developed countries. Similarly, GATT members recognized the need to apply different criteria to each case in the context of RTAs rather than to apply absolute and general rules (Espiell 1971: 38). The provisions for RTAs among developing countries were inserted into the Enabling Clause in order to confirm the operation of existing preferences among these countries.

By contrast, some believe that North-South RTAs provisions were intentionally excluded from the Enabling Clause.[17] If the Enabling Clause covers both South-South and North-South RTAs, two conditions should be necessary. The UNCTAD, which was

[15] As mentioned in Part II, the first advocates of preferential trade arrangements in the drafting process of the General Agreement were developing countries.

[16] These countries presented the agreement to the GATT as "a modest pioneering effort in trade expansion" which had "evolved in pursuance of obligations under Part IV of the Agreement" (Yusuf 1980: 489).

[17] Interview with a UNCTAD official, November 2003.

the main proactive institution to insert the Enabling Clause into the GATT system, did not insist on differentiation among developing countries, and developing countries did not necessarily stand together regarding the provision of North-South preferences to limited groups of developing countries.[18] Consequently, developing countries started their struggle to obtain SDT with South-South RTAs, while North-South RTAs were excluded from the negotiations on the Enabling Clause from a strategic viewpoint.

International organizations, especially the UNCTAD, continued to take a negative stance toward differentiation among developing countries. If North-South RTAs were excluded from the coverage of the Enabling Clause for strategic reasons, it is difficult for SDT to be introduced into North-South RTAs on the initiative of the UNCTAD. On the other hand, if North-South RTAs were not intentionally excluded from the Enabling Clause, the applicability of SDT to North-South RTAs is open to question, because the situation has changed considerably and the number of North-South RTAs is rapidly increasing.

IV. Practices of North-South RTAs in the WTO System

In the current world trade system, there are non-generalized and non-reciprocal preferential agreements between developing and developed countries. Such agreements are not RTAs categorized in Article XXIV; nor are they generalized preferential schemes justified by the Enabling Clause. A representative example is the Cotonou Agreement, a successor to the Lomé Convention, which was signed by the EC member states and the ACP countries.[19] In addition, the United States offers duty-free non-reciprocal access to most Caribbean and sub-Saharan countries through the US-Caribbean Basin Economic Recovery Act (CBERA) and the African Growth and Opportunity Act (AGOA), both of which were enacted under federal US law. In this part, the focus of the paper turns to how these trade arrangements remain compatible with WTO rules.

[18] When the Yaounde Convention negotiations started, some developing countries feared that they would be bypassed by the institutionalization of a system of preferences. As a representative of excluded countries, India objected that "the negotiations that are taking place with a view to association of the 18 African and Malagasy states with the EEC are a deviation from GATT rules" (Tussie 1987: 28).

[19] Currently the ACP group consists of seventy-seven members.

IV-1. The Lomé Convention and the Cotonou Agreement

In 1975, the EC and the ACP countries concluded a framework agreement known as the Lomé Convention, which has subsequently provided the structure for trade and cooperation between these two groups. This convention was designed on the basis of the EC's aid policy for the ACP countries (former colonies of some EC member states). Since 1975, the Lomé Convention has been renewed four times in order to strengthen the integration of ACP states into the global economy. The last agreement under this name (Lomé IV) expired at the end of February 2000 and was replaced by an agreement which serves as the framework for new and more comprehensive relations between the EC and the ACP countries. This new agreement, known as the ACP-European Union (EU) Partnership Agreement, was signed in Cotonou, Benin, on June 23, 2000.[20]

The main objective behind the Lomé Convention was not to form a free trade area in terms of Article XXIV but to lay the legal foundation for a development assistance scheme from the EC to the ACP countries. Therefore, the Lomé Convention set up a preferential and non-reciprocal trading system favoring the ACP countries by allowing them almost free access to EC markets for nearly all industrial goods and for a wide range of agricultural products. Moreover, regarding banana imports, in accordance with the Lomé Convention, the EC granted preferential trade arrangements to ACP countries by imposing no duties and introducing a preferential quota only for ACP countries.[21] However, these preferences became the subject of arguments as to whether they violated MFN treatment. In April 1993, five Latin American countries[22] filed a compliant before the GATT concerning the EU's banana import regime.

In the banana dispute, there were two points of debate concerning North-South RTAs: firstly, whether the Lomé Convention fell under the category of free trade areas defined in Article XXIV; and secondly, whether Article XXIV: 8, which provides

[20] The official name of this agreement is *Partnership Agreement between the Members of the African, Caribbean and Pacific Group of States of the One Part, and the European Community and Its Member States, of the Other Part*. The Agreement entered into force in June 2000 and will be valid for a period of twenty years, subject to revision every five years.

[21] The EU has allowed a significantly larger amount of imports from ACP producers because of a historical relationship between the exporting countries and European nations. Carew (2002) considers "the fact that the preference exists for ACP producers is a remnant of European colonial policy. The EU is bound to this policy by the Lomé convention."

[22] The members who requested the panel were Colombia, Costa Rica, Guatemala, Nicaragua and Venezuela.

essential requirements for free trade areas, could be interpreted as adhering to the spirit of Part IV of the GATT.[23] Based on the GATT Dispute Settlement Rules and Procedures, a panel was established to examine these matters, and it concluded that the EU's preferences for ACP countries constituted Article I MFN violations and, as such, could not be justified on the grounds of Article XXIV (GATT 1994). The panel also deemed that Article XXIV: 8 could not be read in conjunction with Part IV. On the first issue, the panel described its reasoning—that the Lomé Convention was a non-reciprocal agreement which do not meet the definition of a free trade area in the sense of Article XXIV—in the following manner:

> [T]he use of the plural in the phrases "between the constituent territories" and "originating in such territories" made it clear that only agreements providing for an obligation to liberalize the trade in products originating in **all** of the constituent territories could be considered to establish a free-trade area within the meaning of Article XXIV:8(b). … The [Lomé] Convention … did not provide for any liberalization of trade in products originating in the EEC. … This lack of **any** obligation of the sixty-nine ACP countries to dismantle their trade barriers, and the acceptance of an obligation to remove trade barriers only on imports into the customs territory of the EEC, made the trade arrangements set out in the Convention substantially different from those of a free trade area, as defined in Article XXIV:8(b).
>
> (GATT 1994: paragraph CLIX)

As to the relationship between Article XXIV and Part IV, Article XXXVI: 8 limits the right of developed contracting parties to demand reciprocity from developing contracting parties in procedures under the General Agreement. The panel interpreted the phrase, "in procedures under the General Agreement," as not including procedures leading to the formation of a non-reciprocal free trade area between developed and developing countries (GATT 1994: paragraph CLX).

Moreover, the panel made reference to a previous panel report which stated that the spirit and objectives of Part IV could not be cited as justification for actions violating obligations under Part II.[24] The view of the panel was that:

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[23] Five Latin American countries claimed that the EEC measures were not justified under Article XXIV, since the Lomé Convention did not meet the conditions of a free trade area as set out in that Article. The claim of the EEC was that its banana import measures, even if inconsistent with Article I, were justified under the provisions of Article XXIV and, also, that the conditions set out in Article XXIV: 8(b) had to be read in the light of Part IV of the General Agreement.

[24] The panel noted the drafting history of Part IV of the GATT as supporting its interpretation. During the negotiations of Part IV, the authorization of special preferences to developing countries had been suggested but had not been included in the final text, which, according to the panel, meant that non-reciprocal agreements between developed and developing countries had not been considered

> Article XXXVI:8 and its Note were not intended to apply to negotiations outside the procedural framework of the General Agreement, such as negotiations of a free trade area. …
> That [previous] panel had found that the provisions of Part IV cannot override obligations, in particular the obligation to accord most-favoured-nation treatment, owed under other parts of the General Agreement. …
> [T]he wording and underlying rationale of Article XXXVI:8 and its Note, and also its drafting history and subsequent interpretation in GATT practice, made clear that it was neither intended to modify Article XXIV:8(b) nor to justify preferences inconsistent with Article I:1 other than those specially provided for in Article XXIV.
>
> (GATT 1994: paragraph CLXI, CLXII)

After the release of the panel report on the banana dispute, the EU and ACP countries requested that a waiver be granted for the Lomé Convention based on the procedures of Article XXV of the General Agreement, and this waiver was granted by the WTO until the Lomé Convention was replaced by the Cotonou Agreement in 2000.[25]

Even though EU member states undertook a fundamental review of their relationship with ACP countries when they replaced the Lomé Convention, they still considered the Cotonou Agreement as a part of their policy to aid and assist in the development of those countries.[26] Consequently, the Cotonou Agreement inherited the non-reciprocal preferential trade arrangement from the Lomé Convention, which was incompatible with WTO rules. In order to avoid a recurrence of the same disputes that had plagued the Lomé Convention, participants to the Cotonou Agreement obtained a seven-year waiver from WTO rules at the Doha Ministerial Conference in November 2001. However, most parties to the Cotonou Agreement anticipated much difficulty in renewing the waiver owing to the deep-rooted criticism against preferential trade arrangements from GATT contracting parties who had been excluded.[27] Before 2008,

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justifiable in the provisions of Part IV (GATT 1994: paragraph CLXII).

[25] The GATT members decided that "the provisions of paragraph 1 of Article I of the General Agreement shall be waived, until 29 February 2000, to the extent necessary to permit the European Communities to provide preferential treatment for products originating in ACP States as required by the relevant provisions of the Fourth Lomé Convention, without being required to extend the same preferential treatment to like products of any other contracting party" (GATT 1994).

[26] The EU explained the reason for reconsidering the Cotonou Agreement as a result of a fundamental turnaround of EU trade and aid policy and not as a result of the agreement's incompatibility with WTO rules. The EC started a comprehensive approach to assist in the economic development of developing countries not only in trade but also in other fields, such as finance and human resource development, which made it necessary to revise the Cotonou Agreement (Interview with an EU official, November 2003).

[27] Under article XXV of the General Agreement, a waiver requires approval by a two-thirds majority of the votes cast and one-half of the contracting parties.

therefore, the Cotonou Agreement would have to be made into a new agreement compatible with WTO rules. The EU proposed to replace preferential trade provisions in the Cotonou Agreement with reciprocal free trade agreements (FTAs) in order to meet the requirements of Article XXIV. Because of the difficulties involved in concluding one broad FTA among all the countries concerned, the new scheme divides the ACP countries into seven groups by region, with FTAs concluded between the EU and each of these groups. The first phase of negotiations between the EU and ACP countries as a whole, in which all participants reached an agreement in principle on shifting the Cotonou Agreement toward separate FTAs, was carried out from September 2002. The second phase of negotiations, between the EU and each of the seven groups, began in October 2003 and is currently ongoing.

IV-2. CBERA

The CBERA, commonly referred to as the Caribbean Basin Initiative (CBI), was enacted as a domestic law of the United States in August 1983 and was implemented from 1984.[28] It authorizes the United States to provide unilaterally to eligible Caribbean countries preferential trade and tax benefits including duty-free access to the US market for eligible products. Its main objective is to help the Caribbean Basin countries diversify their economies and expand their exports (USTR 1999: 8). Twenty-four countries and territories are currently designated as beneficiaries corresponding to the purpose of the CBI.[29]

At the inauguration of the CBI scheme, the United States sought a GATT waiver for its obligations under Article I because the application of the CBI would potentially constitute an MFN violation. In addition, the Enabling Clause did not justify geographically-limited preferences such as the CBI (Jacobs et al 2000:2–3).[30] There

[28] The Act was originally scheduled to remain in effect until September 30, 1995, but was amended in 1990 by the Caribbean Basin Economic Recovery Expansion Act, known as CBERA II or CBI II, in order to make the CBERA a permanent program. Moreover, in May 2000, the U.S.-Caribbean Trade Partnership Act (CBTPA) was enacted, thereby expanding the list of duty-free products and offering greater access to the US market for eligible countries.

[29] Presently, the eligible countries are Antigua and Barbuda, Aruba, Bahamas, Barbados, Belize, Costa Rica, Dominica, Dominican Republic, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Montserrat, Netherlands Antilles, Nicaragua, Panama, St. Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Trinidad and Tobago, and the British Virgin Islands.

[30] Jacobs et al (2000: 3) point out that the quota-free provisions and the tariff-rate quotas in the CBI involve discrimination under Article XIII and that the United States needs to request a waiver of

was much deliberation in the examination of the proposed CBI waiver under the GATT, but with the strong support of the beneficiary countries and territories, the United States successfully received a waiver of Article I in 1984.[31] The waiver has been renewed several times and is currently valid until December 31, 2005 (WTO 1995b).

One of the key questions surrounding the CBI has concerned the eligibility criteria for designation as a beneficiary country. On the basis of the CBI criteria, not only Asian or African countries but also several Central American and Caribbean countries were excluded from CBI benefits. Some GATT members have claimed that such exclusions were incompatible with MFN treatment and even Part IV of the General Agreement, which aims to promote the economic development of *all* developing countries. Although they regard the CBI objective of promoting economic and political stability among the Caribbean Basin countries as desirable, other GATT member countries, especially those excluded, have argued that this objective should not be viewed as sufficient justification for a waiver (South-North Development Monitor 1984).

Some members have further stated that they prefer the strengthening of a GSP as the best way of promoting trade by developing countries. However, during the examination of the proposed CBI waiver, the United States argued that the CBI was one element of its GSP scheme. The US view was that its special preferences under the CBI could be covered by the Enabling Clause. In response to this stance, the GATT secretariat suggested that "the Enabling Clause covered only specific arrangements laid down in it and not those envisaged under CBERA" (South-North Development Monitor 1984). At present, the United States distinguishes the CBI from a GSP in the following terms: "The CBI program is … independent of the U.S. GSP program as a matter of statute and a matter of policy" (WTO 1995a).

IV-3. AGOA

The AGOA is a constitutive part of the US domestic legislation, entitled the Trade and Development Act of 2000, which also contains the CBI scheme.[32] The Act identifies certain sub-Saharan African countries as being eligible for AGOA benefits and offers

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Article XIII for these provisions and quotas.

[31] For details of discussions with respect to the first CBI waiver, see South-North Development Monitor (1984).

[32] The Act entered into effect in October 2000 and will continue until September 2008.

them preferential access to the US market. Specifically, the AGOA expands the list of duty-free products under the GSP program of the United States only for AGOA eligible countries, as well as quota-free exports of textile and apparel products to the United States (Washington Trade Report 1999).

Along with the CBI, the objective of the AGOA itself is generally considered positive. However, several issues of concern have arisen.[33] In terms of WTO compatibility, the AGOA faces problems because beneficiaries have been chosen in a limited and arbitrary manner. The criteria for eligibility under the AGOA are divided into two stages. Firstly, the AGOA extends the possibility of favored trade status in accordance with *geographical* criteria, or forty-eight sub-Saharan African countries. Secondly, the AGOA recognizes a country as eligible when the governments of these countries follow the pre-determined *social and economic* criteria. To be eligible, a country must have established or be making continual progress toward establishing: a market-based economy, the rule of law, the elimination of barriers to US trade and investment, economic policies to reduce poverty, the protection of internationally-recognized worker rights, and a system to combat corruption. Additionally, a country is examined to see whether it adopts policies that: do not interfere with US national security or foreign policy, do not violate internationally-recognized human rights, do not support international terrorism, and eliminate the worst forms of child labor (USTR 2003: 9).[34] In the WTO trade policy review of the United States, the EC points out that "the eligibility to AGOA is not only dependent on objective criteria related to the development status of individual countries." Where political and non-objective criteria are used to determine AGOA benefits, the EC is skeptical of whether these criteria are "square with the applicable WTO rules governing such arrangements" (EC 2004).

Like the CBI, the AGOA offers a more expansive range of duty-free treatment than a GSP (Washington Trade Report 1999), which means that the AGOA program is sometimes regarded as an extended version of a GSP scheme. The AGOA program,

[33] Skeptical views of the AGOA have appeared in various fields. Apart from doubts over its compatibility with the WTO, the issue of rules of origin is the most controversial problem. For details on this matter, see Flatters (2002).

[34] Under the AGOA, for their eligibility status to be determined, forty-eight potential beneficiaries have their cases reviewed annually. For 2003, thirty-eight countries met the requirements, up from thirty-six previously (WTO 2003b: 26).

however, does not apply to all developed or least developed countries. Moreover, if the AGOA were to be modified in the same way as the GSP of the US, the US, as a WTO member, would have to notify the relevant changes to the CTD, which is in charge of GSP schemes. However, there is no report from the Untied States regarding such a modification.[35] Thus, the AGOA can be recognized as a non-reciprocal and geographically-based preferential trade arrangement which needs a WTO waiver. As with established practices in the CBI and other preferential schemes for limited groups of developing countries conducted by the United States, it is most likely that the United States will request a waiver for the AGOA.[36] When the AGOA scheme was introduced, the US government also showed its intention to obtain a waiver for the AGOA's preferential access provisions (Jacobs et al 2000:3–4). However, as of June 2003, the United States has not yet requested a WTO waiver for the AGOA (WTO 2003b: 26).

Interestingly, the AGOA also contemplates the future negotiation of an FTA between the United States and AGOA beneficiaries, but as yet no action toward negotiations on such an agreement has started (Washington Trade Report 1999). It remains to be seen whether the United States has a strategy or intention to change preferential trade arrangements into FTAs in order to achieve consistency with WTO rules. However, this would be one of several possible ways for non-reciprocal North-South RTAs to be authorized in the WTO legal framework.

V. North-South RTAs and Issues of WTO Compatibility

In view of the current legal system of the WTO, it is impossible not to conclude that specific trade preferences for limited groups of developing countries are incompatible with WTO rules. Countries concerned with North-South RTAs, therefore, have strived to create various measures in order to achieve compliance with the WTO.

V-1. Possible Options for WTO compatibility

The essential characteristics of North-South preferential schemes, which provide benefits to limited groups of developing countries, are their non-generalized and

[35] Interview with a WTO official, November 2003.
[36] Interview with a WTO official, November 2003.

non-reciprocal features. The former feature excludes such North-South RTAs from the coverage of the Enabling Clause. On the other hand, due to the second feature, North-South RTAs cannot fulfill the criteria of FTAs as stipulated in Article XXIV. Therefore, North-South RTAs inevitably come into conflict with Article I. There are three possible ways for states to justify their preferential schemes as deviations from MFN treatment: (a) by obtaining a WTO waiver pursuant to Article XXV: 5; (b) by extending specific preferences to all developing countries; and (c) by creating free trade areas, as specified in Article XXIV.

In the past, countries have maintained these specific preferences usually by obtaining waivers. However, gaining a waiver under the WTO has lately become a more difficult process. This is partly because in 1995 the reform of the GATT into a new institution, the WTO, brought about the enhancement and expansion of the "rule of law." As a result, there was an increasing belief that exceptions which could erode the legal system had to be restrained minimally. Even if the WTO grants waivers for North-South RTAs, the waiver period is now shorter than most cases in the past. Those preferential schemes that have not yet received waivers are likely to be examined by the Dispute Settlement Body (DSB) for their consistency with WTO rules.[37]

The second option for attaining WTO compatibility for preferential trade schemes has become of little effect. GSP preferences are to be non-discriminatory across developing countries except for those favoring the least developed countries (LDCs). In order to assimilate geographically-limited preferences into GSP schemes, some preference-giving countries have attempted to generalize these schemes. The Everything But Arms (EBA) initiative of the EU, which grants duty- and quota-free access for all goods exported by LDCs, and the AGOA scheme of the United States are often cited as prominent examples (FAO 2003; Hoekman et al 2003: 5–6). However, such schemes should be distinguished from the generalization of North-South RTAs. The EBA precludes advanced developing-countries that are eligible for the Cotonou Agreement, and the AGOA limits its geographical range to sub-Saharan African countries. Moreover, both sides to North-South RTAs share negative views about the extension of

[37] For instance, India called for the establishment of a panel under the DSU that would examine the EU's special tariff preferences to the so-called Drug Arrangements, under which only twelve developing countries could benefit. The WTO issued a panel report on December 1, 2003, and found the EU's arrangement to be in violation of trade rules because it discriminated against other developing countries (WTO 2003a).

limited preferences to all developing countries. Developing countries might lose existing preferences. On the other hand, developed countries might lose their strategic measures for assisting specific groups of developing countries.

In these circumstances, countries in recent years have actively attempted to substitute specific preferences with free trade areas, which are officially permitted in the WTO system. The EU's policy to replace the Cotonou Agreement by seven FTAs is a good example. The United States also considers the AGOA as a first step toward FTAs with sub-Saharan African countries (IPC 2003: 2). However, the criteria for concluding FTAs are not defined precisely, and the examination mechanism for determining their consistency with WTO rules does not function properly. In addition, some degree of "flexibility" is permitted in FTA practices, which makes it likely that WTO members will utilize FTAs as a tool for obscuring the incompatibility of North-South RTAs with WTO rules.

V-2. Flexibility in North-South RTAs

North-South RTAs would be approved as FTAs only if all participants reciprocally liberalized their trade practices. However, it is difficult to apply symmetrical obligations, such as tariff elimination, among participants which are unequal in the terms of economic strength. Thus, developing countries, in particular ACP countries, often request limitations to the degree of reciprocity in FTAs or seek techniques to avoid granting full reciprocity. As Onguglo and Ito (2003: 1) point out, "there exists a legal lacuna in terms of availability of SDT" in respect to North-South RTAs. Past experiences in the WTO suggest that a certain degree of flexibility is allowed in the formation of North-South RTAs. For example, a transitional period of twelve years is provided in the framework of the FTA between the EU and South Africa (Bilal 2002: 5–6). In the cases of the EU-Tunisia FTA and the Canada-Chile FTA, developing countries are permitted to take more than ten years for liberalization and set aside sensitive products from their liberalization list, whereas developed countries have to liberalize immediately on substantially all the trade.

The concept of flexibility is legally based on the term "exceptional cases" in the Understanding on the Interpretation of Article XXIV. Paragraph 3 of the Understanding states that "[t]he 'reasonable length of time' referred to in paragraph 5(c) of Article

XXIV should exceed 10 years *only in exceptional cases*" (author's italics). In Article V paragraph 3 of the GATS, moreover, the term "flexibility" for developing countries is explicitly mentioned:

> Where developing countries are parties to an agreement of the type referred to in paragraph 1, flexibility shall be provided for regarding the conditions set out in paragraph 1, particularly with reference to subparagpaph (b) [this means the condition "a reasonable length of time"] thereof, in accordance with the level of development of the countries concerned both overall and in individual sectors and subsectors.

The GATS, however, does not characterize the available flexibility. Consequently, while the SDT for developing countries is recognized in RTAs on services, its practical usage remains unspecific (Bilal 2002: 6).

Like the situation in the GATS, it is matter of argument as to the condition in Article XXIV to which flexibility applies.[38] Judging by the precedents, flexibility applies mostly in two spheres: in the transition period and in the product coverage. The former allows deviations under the "reasonable length of time" condition, while the latter allows deviations under the "substantially all the trade" condition. The view of the CRTA, however, is that the concept of flexibility applies only in the transition period and that the issue of product coverage is outside the scope of flexibility.[39] In accordance with this view, not a few cases of RTAs have persuaded longer time frame as a transitional period than ten years without a waiver. On the contrary, even though the flexibility in product coverage constitutes de facto acceptance of SDT, no legal guarantee is given in respect to the compliance of these provisions with WTO rules. There is much skepticism on flexibility in product coverage as neglect of an Article XXIV requirement.

Besides the ambiguity of the flexibility concept and lack of any mechanism to ensure effective implementation of SDT, what makes the legal framework on RTAs even more obscure is that both available rules for North-South RTAs—those on RTAs and those on SDT—are under review in the ongoing multilateral trade negotiations of

[38] Onguglo and Ito (2003: 49–63) divide the concept of flexibility into two categories: "existing flexibility" and "additional flexibility." They argue that SDT for developing countries falls under the latter type of flexibility. They also examine the modalities for granting additional flexibility in respect to each condition of Article XXIV.

[39] Interview with WTO officials, October 2003.

the so-called Doha Development Agenda (the New Round).[40] The form and content of RTAs currently under negotiation or consultation will be influenced by the outcome of this New Round. In reviewing RTA rules, "the negotiations shall take into account development aspects of regional trade agreement" (WTO 2001b: paragraph 29). This provision reflects a concern by certain developing countries that are eager to introduce more flexibility into rules relating to North-South RTAs (Bilal 2002: 6). Interestingly, the request to apply some SDT provisions to North-South RTAs was proposed at the Seattle Ministerial Meeting in 1999.[41] This proposal, however, was not adopted as part of the agenda at that conference. But developing countries have strongly demanded the enhancement of SDT regularly (WTO 2001a). Their requirement is based on the idea that SDT provisions "are to be looked at not as exceptions to the general rules but more importantly as an integral and inherent objective of the multilateral trading system" (WTO 2001a).[42] It is difficult to infer even the outline of a set of relevant rules from the current status of negotiations.

V-3. The Concern about Differentiation

The introduction of an SDT clause in Article XXIV would have a negative impact in one sense. It would lead to a segmentalization of preferential schemes which would result in dividing legal disciplines into pluralistic pieces. It could trigger exclusive trading blocs also involving developing countries. One of the most problematic issues is that it would provide an explicit legal base to the de facto differentiation among developing countries. Panagariya (2002) is concerned that "the preferences also became an instrument of breaking the united front presented by a group of developing countries."[43]

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[40] The ministers at the Doha Ministerial Conference in 2001 mandated the CTD to examine STD provisions with the phrase that "all special and differential treatment provisions shall be reviewed with a view to strengthening them and making them more precise, effective and operational" (WTO 2001b: paragraph 44). According to this declaration, the CTD has to consider measures or mechanisms to enhance SDT provisions. So far, the CTD has divided various proposals relating to SDT into three categories so that it can establish the priorities for strengthening the STD provisions.

[41] Interview with a WTO official, November 2003.

[42] In order to realize their goals, developing countries proposed the establishment of a concrete and binding SDT regime that would be responsive to their development needs. They also requested WTO members to elaborate a framework/umbrella agreement on SDT (WTO 2001a).

[43] Panagariya (2002) fears that inter alia such differentiation by preferences would be utilized by developed countries to break the generally unified position of a large majority of developing countries against Singapore on issues like the inclusion of labor standards into WTO agreements.

The traditional approach toward development issues in the GATT/WTO still emphasizes that developing countries need appropriate strategies as a package rather than strategies that focus on sectoral and divisive programs such as the Cotonou Agreement, the CBI and the AGOA. From a poverty-reduction point of view, there is alarm that "preferences should focus on the poor, wherever they are geographically located, and not on a limited set of countries. … Limiting preferences to LDCs or concentrating on a specific geographic region such as sub-Saharan Africa ignores the majority of the poor in the world today" (Hoekman et al 2003: 6). Even if differentiation between developing countries is necessary, the preferences for development are to be accorded not because of political, cultural or even geographical ties, but because of the difference in the levels of economic development (Yusuf 1980: 492).

By contrast, others point out the positive effect of differentiation between developing countries. Many of the preference-receiving developing countries have benefited substantially from gaining preferential access for their exports. These trade preferences were originally conceived as a means to increase production and exports of developing countries so that they would eventually become more competitive internationally (FAO 2003).[44] As the distinct qualities of WTO members, such as economic strength and human resource skills, become diversified, the capacity to implement WTO disciplines will vary from country to country. Advocates regard these circumstances as a rationale for differentiation between developing countries in determining the reach of resource-intensive WTO rules (Hoekman et al 2003: 16).[45] The issue of differentiation is not peculiar to South-North RTAs. It is difficult to find the necessary unity to resolve intertwined and implicated agendas among countries with conflicting interests as found in the WTO.

[44] Preferences are effective, especially in the field of agriculture. An FAO report pointed out that trade preferences have benefited many countries in developing their agricultural exports as a major source of foreign exchange.

[45] Hoekman et al (2003: 16) further proclaims that "some WTO disciplines may not be appropriate for very small countries in that the regulatory institutions that are required may be unduly costly." They lay out the basic rationale for differentiation, which is that "certain agreements may simply not be development priorities or they may require many other preconditions to be satisfied before implementation will be beneficial." These predictions can be required in proportion to per capita income, institutional capacity and economic scale, instead of being applied across the board.

IV. Concluding Remarks

Recently, there has been a surge in bilateral and regional trade arrangements between developed and developing countries. These arrangements are known as North-South RTAs. In connection with these RTAs, a question arises as to what kinds of rules are applicable to such arrangements. Under the current WTO legal system, RTAs involving trade in goods are largely governed by Article XXIV of the General Agreement, while RTAs in services are governed by Article V of the GATS. RTAs are by definition discriminatory. This means they inevitably violate the MFN obligation, which is the fundamental principle of the WTO. However, many WTO members regard RTAs as necessary to develop or reconstruct their economies. In order to justify such MFN violations, therefore, each set of rules on RTAs has been incorporated into the General Agreement and the GATS.

Besides these provisions, another provision applying to RTAs among developing countries is the Enabling Clause. The Enabling Clause stemmed from the ambitious quest of developing countries during the 1960s to gain SDT within the multilateral trading system. These countries firstly materialized the GSP schemes among their overall demands, under which the developed countries could grant preferential market access across all developing countries by unilaterally reducing tariffs despite the conflict between these schemes and the MFN clause. With the intention to introduce GSP schemes into the GATT legal framework, the GATT member-states approved GSPs as an exception to MFN treatment through a ten-year waiver in 1971 and, in effect, provided a permanent waiver in 1979 through the Enabling Clause. This clause also covers SDT in those RTAs that consist of only developing countries.

Article XXIV of the General Agreement and Article V of the GATS set out several criteria for forming RTAs. These are: a “substantially all the trade” condition, a “reasonable length of time” condition, and the condition that there should be reciprocal liberalization among constituents. On the other hand, the Enabling Clause provides legal status only for *generalized* and *non-reciprocal* schemes, not for schemes that select only some developing countries. According to current WTO rules, North-South RTAs, unlike GSP schemes, must be reciprocal and must cover substantially all the trade. Special preferential schemes of the past were mainly implemented by the EC and the United

States. The EU's arrangement, which only applies to ACP countries, began with the Lomé Convention (now the Cotonou Agreement), while the United States established the CBI and the AGOA (legislated as national law), which benefits Caribbean or sub-Saharan countries through a discriminatory tariff measure. None of these specific trade preferences, which are aimed at limited groups of developing countries, meet the criteria stipulated in Article XXIV, and hence all preferences need a waiver from WTO rules.

The usual practice has been for the countries concerned to maintain their special trade preferences by obtaining a waiver. However, in recent years, obtaining waivers from the WTO has become more difficult, and, as a consequence, the countries involved have replaced trade preferences by concluding FTAs. However, such FTAs are also problematic. Firstly, the concept of flexibility is less than obvious. Member countries could exploit this concept and end up neglecting the WTO legal framework. Moreover, available disciplines on North-South trade arrangements—rules on RTAs and SDT—are on the negotiating table at the New Round, and so the outcome of this Round will impact upon the content of North-South RTAs. However, there is no way of knowing the kind of agreement that might be reached at the New Round; therefore, it is unclear what rules will apply to North-South RTAs in the future.

Another problem is that the approval of SDT for the provision of special preferences to some developing countries could provide a legal foundation for differentiation between developing countries. If SDT provisions are incorporated into the North-South RTA rules, preferences for development could be provided not on the basis of MFN treatment, but on the basis of geographical or other arbitrary criteria. However, the provision of preferences to a limited number of countries makes deviation from SDT an issue fundamental to the debate of how preferences should be provided to developing countries. So far, SDT has been seen as a way to improve the competitive position of developing countries. Instead, the position of developing countries might be weakened if some developing countries get special preferences. As such, there needs to be a deep and comprehensive discussion on how to fulfill the lack of SDT in North-South RTAs.

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