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Challenges to World Trade Organisation in Pursuit of Escalating Regional Trade Agreements

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ABSTRACT

Whether Regional Trade Agreements are strictly economic and political in nature? Whether Regional Trade Agreements (RTAs) does produce any legal challenges? Whether the sudden escalation of RTAs in past few decades brings challenges to the legitimacy of multilateral trade and the World Trade Organization (WTO)? Whether RTAs are trade creating or trade diverting in nature? This research article seeks to clarify the legal challenges posed by rising number of RTAs on multilateral trade, agreements and institutions related therewith. Legal challenges that RTAs have brought have not received the equivalent attention that political and economic challenges are receiving. RTAs can never be seen strictly through political and economic lens in isolation from international trade law. RTAs are an exception to the principle pillars of contemporary international trade law i.e principle of most-favoured nations (MFN) and the principle of non-discrimination (ARTICLE III:GATT) enriched under several agreements of WTO. A periodical legal scrutiny of RTAs is necessary in order to analyze challenges RTAs have posed to multilateral trade. Several legal scholars have criticized RTAs “as an escape route to WTO agreements and laws”. Primary objective of research article is to explore the jurisprudence of RTAs/custom unions (provided under ARTICLE XXIV:GATT, ARTICLE V:GATS) in order to navigate the loopholes in RTAs which can be a challenge to the legitimacy of contemporary international trade law. Furthermore, research article aims at concluding sincere suggestions and recommendations for bring about a balanced relationship between multilateral and regional trade in order to strengthen global cooperation and development.

I. INTRODUCTION

In past several decades Article XXIV: GATT, has unleashed a verve of proliferation in free trade areas/ regional economic groupings and regional trade agreements.² Basically, a regional

¹ Author is an Assistant Professor in India.

² AUTAR KRISHEN KOUL, GUIDE TO THE WTO AND GATT- ECONOMICS, LAW AND POLITCS 365 (2018), SPRINGER AND SATYAM LAW INTERNATIONAL (6th ed.).

trade agreement or custom union or a free trade area is permitted by ARTICLE XXIV: GATT, as an exception to the principle MFN treatment and non-discrimination (which are the primary pillars of modern multilateral trade law). A custom territory formed in accordance to ARTICLE XXIV, is to be treated as a contracting member having separate tariffs and other commercial negotiations maintained for a “*substantial part of trade*” for other contracting states/members of WTO. The primary objective of ARTICLE XXIV: GATT is “facilitation of trade” between constituent members instead of raising trade barriers for other countries.³ Whether increase in RTAs and custom unions is net trade creating or net trade diverting has become a serious issue before World Trade Organisation (WTO). There is a long persisting misconception that multilateral trade and negotiations are purely political and economic in nature, but law, economics and politics overlap in the sphere of multilateral or international trade. Analyzing legal challenges posed by RTAs are not less important than economic and legal challenges posed by them. A periodical and close examination of ARTICLE XXIV: GATT is necessary because RTAs have the capability of challenging the existence of WTO by offering alternative trade platform. Several countries view the regional trade platform as an insurance policy in case of collapse of multilateral trade platform (WTO).⁴ According to several critics’ multilateralism has been compromised due to the ‘*extremely elastic*’ and ‘*unusually complex*’ nature of Article XXIV (GATT).⁵ According to a World Bank report there were only fifty (50) Regional Trade Agreements in force in the year 1990, however the number of escalated to more than 280 in the year 2017.⁶ Furthermore, on February 1, 2021, 339 RTAs were officially recorded to be in force.⁷ Proliferation in RTAs demand proliferation in justifications too.

II. AN ANALYSIS OF SUDDEN PROLIFERATION IN REGIONAL TRADE AGREEMENTS OR CUSTOM UNIONS OR FREE TRADE AREAS

Escalation in number of RTAs has completely world trade scenario, which might result in trade diversion high welfare costs to WTO member countries. RTAs have started diversion of resources on regional level from multilateral level. Firstly, excessive number of participants

³ Article XXIV: 4; See also Understanding on the Interpretation of Article XXIV of GATT 1994, Preamble.

⁴ Kerry Chase, *Multilateralism compromised: the mysterious origins of GATT Article XXIV* (Department of Political Science and Fletcher School of Law and Diplomacy, Tufts University), World Trade Review (2006).

⁵ Kerry Chase, *Multilateralism compromised: the mysterious origins of GATT Article XXIV* (Department of Political Science and Fletcher School of Law and Diplomacy, Tufts University), World Trade Review (2006).

⁶ Mattoo, A., A. Mulabdic, and M. Ruta, *Trade Creation and Trade Diversion in Deep Agreements*, Policy Research Working Paper Series 8206, World Bank (August 07, 2021), <https://www.worldbank.org/en/topic/regional-integration/brief/regional-trade-agreements>.

⁷ RTA Database, *Regional Trade Agreements*, World Trade Organization (August 07, 2021), https://www.wto.org/english/tratop_e/region_e/region_e.htm.

make it hard to reach a consensus due to their differences in national or domestic interests.⁸ Currently there are 164 members and 25 observer governments in WTO.⁹ Secondly, decision making becomes really very complex due to the economic differences between member countries to WTO.¹⁰ Thirdly, member countries find conclusion of negotiations easier at “mini-lateral level” in comparison to “multilateral level”.¹¹ Countries with same legal, economic and political status find it easier to carry trade and trade related negotiations with among them. The primary objective of international trade law is to promote global economic cooperation and development. However, the analysis and scrutiny of RTAs or custom unions or free trade areas has never led to a unanimous specific endorsement or conclusion by contracting parties.¹² “Arguing that the severely uneven distribution of wealth among members make it difficult to reach decisions on controversial trade issues in the WTO, unlike the case where countries negotiate with economically compatible”.¹³ Hardships faced by WTO member countries during Uruguay round and Doha Round of multilateral trade negotiations has further encouraged WTO member countries to form their own trade markets in form of RTAs or custom unions or free trade areas.¹⁴ Countries have started using RTAs as protectionist efforts in international trade.¹⁵ For instance, Asian- Pacific Economic Cooperation (APEC) could be an effort to counter European Union (EU) and NAFTA’s effects. Similarly, South Asian Free Trade Agreement (SAFTA) has also influenced the trade in goods and services in South Asia. These bilateral and plurilateral legal trade ties can be very adverse to the multilateral trade platform (WTO). There are several other miscellaneous reasons for the proliferation in RTAs, like, environmental issues, illegal immigration etc. Countries may also join RTAs for their political benefits, as the countries which trade with each other are less likely to go for war.¹⁶ RTAs are continuously paving the path of bilateral and plurilateral trade. However, several scholars suggest RTAs as trade creating factors. However, the actual impact of RTAs on international trade flow remains controversial.

⁸ Paul Krugman, *Regionalism Versus Multilateralism: Analytical Notes*, in NEW DIMENSIONS IN REGIONAL INTEGRATION 74-75 (Center for Economic Policy Research 1993).

⁹ Members and observers, UNDERSTANDING THE WTO: THE ORGANIZATION (August 7, 2021), https://www.wto.org/english/thewto_e/tif_e/org6_e.html.

¹⁰ Id.

¹¹ Id.

¹² Krishen, *supra* note at 1, at 371.

¹³ JAMES H. MATHIS, REGIONAL TRADE AGREEMENTS IN THE GATT/WTO, ARTICLE XXIV AND THE INTERNAL TRADE REQUIREMENT 140 (2002).

¹⁴ Mohammad F. Nsour, Regional Trade Agreements in the Era of Globalization: A Legal Analysis, 33 N.C. J. INT’L L. 359 (2007).

¹⁵ Bob Switky, *The Importance of Trading Blocks: Theoretical Foundations*, THE POLITICAL IMPORTANCE OF REGIONAL TRADING BLOCS 13, 18 (Bart Kerremans & Bob Switky eds., 2000).

¹⁶ Krishen, *supra* note 1, at 375.

III. IMPACT OF REGIONAL TRADE AGREEMENTS ON INTERNATIONAL TRADE LAW AND WORLD TRADE ORGANIZATION

Currently, RTAs or custom unions cover more than half of international trade parallel to global multilateral trade agreements in operation.¹⁷ This research article highlights the adverse effects of RTAs on multilateral trade law and policy. When two or more countries form a custom union they can derive huge economic gains but at the expense other member countries to WTO.¹⁸ The reason behind inception of ARTICLE XXIV: GATT came into existence in order to motivate countries across the globe having regional ties to turn the character to of trade from regional or bilateral to international/global or multilateral. However, regional trade and custom unions have a very long history which could have prevented the countries having regional ties from signing a multilateral agreement prohibiting regional trade or custom unions. There, ARTICLE XXIV: GATT was drafted as an exception to the principles of MFN¹⁹ and non-discrimination²⁰, which are cornerstone to the contemporary international trade law. However, the hardships in reaching consensus among WTO members, especially during Uruguay and Doha Round of multilateral trade negotiations made WTO members to navigate an alternative trade platform(s). Today, almost every member country of WTO is a participant regional trade agreements.²¹ Due to the proliferation in RTAs and their advantages countries have started drifting away multilateral trade agreements, treaties, conventions and institutions. Impact of RTAs could be very severe, they have the capability of dividing global trade into several regional trade blocs. Multilateral liberalization has started to slow down due to increasing regional arrangements and free trade areas. Regionalism is continuously evolving as it much easy to pursue negotiations at “mini- lateral level” in comparison to “multilateral level”, which could prove extremely adverse to World Trade Organization (WTO). Trade diversion due to surge in RTAs or custom unions could prove very dangerous to the world economy.²² Currently, there are mixed views and opinions on the issue of “surge in RTAs”, however the sudden escalation in RTAs can influence the benefits of multilateral trade if differences in resource allocation and diversion in trade and investment are not minimized.²³

¹⁷ Regional trade agreements - OECD, , <https://www.oecd.org/trade/topics/regional-trade-agreements/> (last visited Aug 7, 2021).

¹⁸ MATHIS, *supra* note 12, at 137.

¹⁹ ARTICLE I, GATT 1994: General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, 1867, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 187, 33 I.L.M. 1153 (1994).

²⁰ *Id.*, ARTICLE III.

²¹ RTA Database, *supra* note 6.

²² Shujiro Urata, *Globalization and the Growth in Free Trade Agreements*, Asia- Pacific Review, Vol. 9, No. 1, 28 (2009).

²³ WTO | Regional Trade Agreements - scope of rtas, https://www.wto.org/english/tratop_e/region_e/scope_

IV. WORLD TRADE ORGANIZATION EFFORTS TO COUNTER THE ADVERSE EFFECTS OF REGIONAL TRADE AGREEMENTS

WTO is continuously making serious efforts to ensure balance and inclusiveness on the issues of “sudden surge in RTAs” and “trade diversion”.²⁴ In February, 1996 WTO established a Committee on Regional Trade Agreements (CRTA) to navigate and record information on RTAs and provide a platform for discussion on the impact of RTAs on multilateral trade.²⁵ In December, 2006 the WTO introduced a provisional transparency mechanism for RTAs which was given permanent status at Nairobi Ministerial Conference, 2015.²⁶ The WTO incorporated the provisions of RTAs in its agreements to complement multilateral trade flow, not to threaten it. Let’s scrutinize the WTO efforts to counter challenges raised by RTAs to the multilateral trade-

- **The Committee on Regional Trade Agreements**

CRTA has replace the parties working on analyzing the RTAs under GATT, and GATS. The primary work entrusted to CRTA is to conduct systematic studies on RTAs related legal issues and concerns.²⁷ Articles and provisions of GATT are generic in nature which can give rise to several interpretations. However, CRTA at several occasions has made serious attempts to discuss and clarify some controversial phrases under ARTICLE XXIV: GATT. For instance, in its meetings CRTA has made a thorough revision and discussion on several phrases like “substantially all trade areas” under ARTICLE XXIV: 8, “general incidents of duties and other restrictive regulations of commerce” under ARTICLE XXIV: 5. CRTA has also clarified critical legal questions about how to calculate general incidents of duties before and after before and after formation of a free trade area or custom union, and other impact of non- tariff measures like environmental issues, anti- dumping, preferential rules of origin etc. however, it becomes extremely difficult for CRTS to provide timely and accurate report on RTAs due to continuously changing quantity and quality of RTAs.²⁸ Further, the participant countries of WTO never take recommendations and decisions of CRTA seriously. If the participants to an RTA or custom union don’t provide sufficient and accurate information about RTA to the CRTA, CRTA cannot conduct an thorough examination about the RTA in question. The

rt_a_e.htm (last visited Aug 7, 2021).

²⁴ Id.

²⁵ Id.

²⁶ Id.

²⁷ Work of the Committee on Regional Trade Agreements, <http://www.wto.org/english/tratop-e/region-e/regcome.html> (last visited Aug 07, 2021).

²⁸ World Trade Organization, Comm. on Reg'l Trade Agreements, *Report (2005) of the Committee on Regional Trade Agreements to the General Council*, WTO Doc. WT/REG/15 (Nov. 3, 2005).

inefficient nature of CRTA has served as a major blow to the legitimacy of World Trade Organization.²⁹

- The Transparency mechanisms

The transparency mechanism launched during Doha Round of negotiations was meant to ensure that RTAs become “*building blocs, not stumbling blocs to world*”.³⁰ Transparency mechanism requires contracting parties to RTA to notify as early as possible to the WTO about relevant agreement information. Contracting parties to RTA must notify the CRTA and the WTO before ratification of the concerned RTA. Further, any changes or modifications in RTAs shall also be notified to the working parties on RTAs of WTO. WTO decisions on RTAs shall be adopted by member parties to the WTO, in order make an RTA in compliance with the procedure laid down by agreements of the WTO (ARTICLE XXIV: GATT, ARTICLE V: GATS). Transparency mechanism to certain level has succeeded to bring about a balanced relationship between multilateralism and regionalism.

- Judicial intervention in Regional Trade Agreements

Several disputes before WTO Dispute Settlement Understanding has also served a important factor in clarifying vague terms in ARTICLE XXIV: GATT and ARTICLE V: GATS. Pre-Uruguay Round of multilateral negotiations panels constituted under GATT could not make binding decisions and interpretations regarding provisions of RTAs as evident from Banana I and Banana II case laws.³¹ However, the conclusion of multilateral trade negotiations of Uruguay Round brought appreciable reforms in dispute settlement mechanism in dealing with legal issues and challenges raised by RTAs.³² The “*Turkey- textile case*” clearly demonstrated the authority of the WTO and its panels to adjudicate on disputes relating to RTAs.³³ The Dispute Settlement Understanding (DSU) panel of WTO has periodically emphasized about its

²⁹ General Agreement on Trade in Services, Apr. 15, 1994, Marrakech Agreement Establishing the World Trade Organization, Annex 1B, Legal Instruments-- Results of the Uruguay Round, 33 ILM 1144 (1994) [GATS].

³⁰ Lamy Welcomes WTO Agreement on Regional Trade Agreements, http://www.wto.org/english/newse/news06_e/rta-july06_e.htm (last visited on Aug 07, 2021) (WTO 2006 News Item from July 10, 2006).

³¹ Report of Panel, *European Community -- Tariff Treatment on Imports of Citrus Products from Certain Countries in the Mediterranean Region*, 4.15, L/5776 (Feb. 7, 1985) (unadopted) (the Panel held that the examination - or re-examination - of Article XXIV agreements was the responsibility of the CONTRACTING PARTIES. In the absence of a decision by the CONTRACTING PARTIES and without prejudice to any decision CONTRACTING PARTIES might take in the future on such a matter, the Panel was of the view that it would not be appropriate to determine the conformity of an agreement with the requirements of Article XXIV on the basis of a complaint by a contracting party under Article XXIII: 1 (a)).

³² Ministerial Declaration: Adopted on 14 November 2001, WTO Doc. WT/MIN(01)/DEC/1, T 29 (Nov. 20, 2001), available at http://www.wto.org/english/thewto-e/ministe/min01e/mindecl_e.htm.

³³ *Turkey—Textiles AB Report*, The Panel noted that “the issue regarding the GATT/WTO compatibility of a customs union, as such, is generally a matter for the CRTA since ... it involves a broad multilateral assessment of any such custom union, i.e. a matter which concerns the WTO membership as a whole.”

jurisdiction to adjudicate in legal issues involved in RTAs. For instance, “*Mexico- Tax measures on Soft Drinks and other beverages*”, where DSU clarified that it had legal right to adjudicate the dispute between U.S. (complainant) and Mexico (defendant) pursuant to articles 3.2. and 19.2 of Dispute Settlement Understanding.³⁴ However, contracting parties to RTAs give preference to quasi- judicial mechanisms (like, negotiations, mediation or arbitration) for settlement of their disputes relating to RTAs. Thereby, DSU doesn’t exercise a complete authority over resolution of RTAs- related disputes. RTAs are consistently forming an alternative trade platform parallel to the multilateral trade platform introduced by GATT/World Trade Organization.

V. SUGGESTIONS AND RECOMMENDATIONS

Apart from CRTA and transparency mechanism, WTO shall form a separate working group to evaluate the impact and trade diversion created by sudden surge in RTAs. WTO shall periodically evaluate the controversies generated by RTAs and remind its member countries importance of global trade and economy. For, sustainable development of all countries across the globe, global cooperation is necessary. Therefore, WTO at its ministerial conferences shall repeatedly emphasize on the issue of preserving integrity and dignity of international trade. Member countries of WTO shall also make serious efforts to give more priority to global development instead of domestic development. It is high time for every country to realize the importance global integrity, cooperation and development for the prosperity future generation and sustainable development. The WTO shall also organize conferences to encourage member countries to find optimal solutions about the adverse impact of proliferation in RTAs instead of exploiting the world trade under the umbrella of the regional deals. WTO shall also by consensus among its member countries draft a safeguard agreement on RTAs to international trade in order to bring about optimal solutions for the controversies created by RTAs.

VI. CONCLUSION

The research article has made serious attempt to evaluate the threats to the legitimacy of WTO due to proliferation in RTAs or custom unions or free trade areas. An legal analysis of ARTICLE XXIV: GATT and ARTICLE V: GATS, is necessary although they more economic and political in nature. There is an immediate need to strike a balance between multilateralism and regionalism for preserving the global trade and legal order associated with it. A healthy understanding among WTO member countries about interaction between regionalism and

³⁴ Panel Report, *Mexico-Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/R (Oct. 7, 2005).

multilateralism can ensure the dignity and integrity international trade (law). Such understanding could enable RTAs to form building blocs of global trade in goods and services. In January, 2007 Director General of WTO also said “*RTAs should not replace the multilateral system.*”³⁵ WTO shall repeatedly remind its member countries about the importance of multilateral trade and to foster international relations and cooperation. Further, it has become very important for WTO to introduce optimal reforms in the area of RTAs or custom unions or free trade areas, in order to counter challenges posed to its legitimacy by regional trade. The “family of nations” shall also give due respect to multilateral treaties, agreements and institutions to foster international peace, cooperation and development.

³⁵ Pascal Lamy, Speech at Confederation of Indian Industries Partnership Summit 2007, Multilateral or bilateral trade agreements: which way to go? (Jan. 17, 2007) (transcript *available at* <http://www.wto.org/english/news-e/sppl-e/sppl53-e.htm>).