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STRENGTHENING THE GLOBAL TRADE SYSTEM



Regional Trade Agreements and Plurilateral Approaches

Proposals and Analysis

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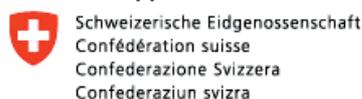
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For more information on the E15, please visit www.e15initiative.org

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INTRODUCTION

The E15 Initiative

A plethora of critical, impending issues mire the multilateral trading system of today. Ensuring food security in times of high and volatile prices, addressing concerns around natural resource scarcity, or scaling up sustainable energy production and diffusion, are just a few of many. The fragmentation of production through highly complex global value chains also poses critical challenges at the analytical and policy level.

In the meantime, preferential trade agreements continue to proliferate and have now become the de facto locus to deepen integration and further liberalization. In the face of the Doha deadlock, some have questioned the way in which negotiations are conducted, arguing that the World Trade Organization's (WTO) established practices of decision-making, such as the notion of a single undertaking, are ill suited to the fast-changing challenges of our times.

In the light of these pressing challenges, the E15 Initiative is a process aimed at exploring possible futures for the multilateral trade system. Launched in 2012 by the International Center for Trade and Sustainable Development (ICTSD), the initiative engages top global experts and institutions in thinking ahead on critical issues facing global trading bodies, primarily the WTO, bringing fresh ideas to the policy environment, and solutions and opportunities for governance reform.

In this Paper

This paper is a compilation of the material that has been produced by the Expert Group on Regional Trade Agreements and Plurilateral Approaches, jointly convened by the ICTSD and the Inter-American Development Bank (IDB) to examine the challenges that the expansion and consolidation of regional trade agreements (RTAs) poses for the WTO. The E15 Expert Group is exploring options for the WTO to deal with these challenges while preserving the integrity and efficiency of the multilateral trading system.

The overview paper that appears first in this compilation set the context for the launch of the Expert Group's dialogue. It raises the question of whether and how RTAs can be additive to the world trade system. As many new agreements have advanced beyond the multilateral system and have proven to create trade benefits to members, the paper suggests ideas the E15 Expert Group could discuss on integrating RTAs into the multilateral trading system.

From of the first group meetings, several major ideas took root. Experts from the group were asked to expand on these concepts

in think pieces that delve into the rationale behind specific ideas for managing the proliferation of sophisticated RTAs.

In a think piece entitled "RTA Exchange: Organizing the World's Information on Regional Trade Agreements" Kati Suominen discards the arguments for trying to regulate or standardize RTAs and instead presents an approach to coordinate and improve information and exchange of ideas on RTAs to realize efficiency gains across RTAs; multilateralize RTA best practices; and deepen the trade integration created by RTAs.

Next comes a think piece by Peter Draper and Memory Dube, "Plurilaterals and the Multilateral Trade System," that analyses the "cost-benefit" equation in pursuing plurilateral approaches. The authors examine the complexities and risks of the use of plurilateral agreements along with the benefits associated with retaining centrality for the global trade system, especially for the Doha Development Round. For medium-term success, the authors recommend adopting a Code of Conduct to govern plurilateral negotiations at the WTO.

Robert Lawrence's "When the Immovable Object Meets the Unstoppable Force: Multilateralism, Regionalism and Deeper Integration" analyzes the arguments on whether RTAs lead to discriminatory treatment or whether they make the markets of participants more contestable as a whole. Overall, he raises the question whether RTAs serve as stumbling blocks or building blocks to multilateral integration.

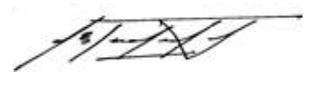
The final paper in the compilation is a think piece by Andrew L. Stoler titled "Will the WTO have Functional Value in the Mega-regional World of FTAs?" that explores whether the WTO can be expected to retain a meaningful functional value for its Members in the soon-to-be-realized world of WTO-plus mega-regionals.

The work of the E15 Expert Group on Regional Trade Agreements and Plurilateral Approaches offers a strong, innovative set of ideas for reforming and improving RTAs in the multilateral trading system. The pieces in this compilation are initial concepts that offer insights into the thoughts and discussions of the leading experts in the working group. While the ideas presented here reflect the views of their authors, they together form a better picture of the possible direction in which the multilateral trading system could evolve to manage trends in the current and future global marketplace.

Further information about the Expert Group on Regional Trade Agreements and Plurilateral Approaches, the experts, and the latest developments in the E15 Initiative can be found at www.e15initiative.org.



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REGIONAL TRADE AGREEMENTS: DEVELOPMENT CHALLENGES AND POLICY OPTIONS

Antoni Esteveordal, Kati Suominen and Christian Volpe-Martinić

INTRODUCTION

As multilateral trade talks have stagnated, regional trade agreements (RTAs) have moved to the forefront (including free trade agreements [FTAs], customs unions, and common markets). Overall, more than 200 RTAs have been notified to the World Trade Organization (WTO), and the total number of agreements hovers around 300 (Figure 1). In addition, there are numerous agreements that cover only trade in services. Almost all countries are member of at least one RTA, and most countries belong to two or more agreements at once (Figure 2).

The implications of RTAs on the multilateral trading system have been subject to policy debate for decades. The 1948 General Agreement on Tariffs and Trade (GATT) allows member countries to grant each other preferential treatment under FTAs or customs unions as long as certain conditions

are met. These conditions are defined mainly in GATT Article XXIV. The proliferation of RTAs in the past three decades has created a sense of urgency among GATT/WTO Members to assess RTAs' compliance with these provisions and address them in a more rigorous fashion--after all, while each member is party to numerous agreements, each is now also an outsider to an ever-growing number of RTAs. In the Doha Round, WTO members elevated RTAs to a "systemic issue," or one that affects the entire world trading system and requires to be addressed as such. However, efforts to deal with RTAs have been narrowly focused on market access provisions (like Article XXIV). They have over time proven to be rather toothless, as WTO members tend to be jealous of their own RTAs and their prerogative to negotiate RTAs.

The WTO has made good progress in this direction. In December 2006, Members issued a "Transparency Mechanism for Regional Trade Agreements," which requires them to provide an "early announcement" of their involvement in RTA negotiations and promptly notify a newly concluded RTA. This, in turn, puts forth a schedule for the RTA's examination by the WTO Secretariat (WTO 2011). Parties to a new RTA are required to submit certain data to the WTO, such as on the RTA's tariff concessions and rules of origin, and their MFN duties and import statistics. After this, the Committee on Regional Trade Agreements (CRTA) is supposed to prepare a detailed survey of the contents of the RTAs.¹ The CRTA is also to perform legal analyses of WTO provisions pertinent to RTAs; draw comparisons across RTAs; and examine the economic aspects of RTAs. The resources for the WTO to perform such analyses are, however, limited, and there are also political sensitivities that curb the ambition of these studies.

This may not matter. The longstanding concern that RTAs might balkanize the global trading system into exclusive

1 See <http://docsonline.wto.org/DDFDocuments/t/WT/L/671.doc>.

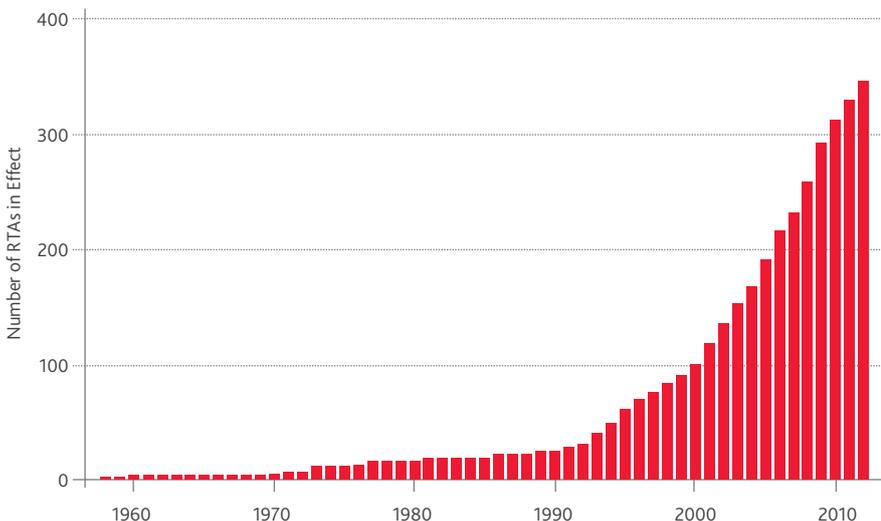


FIGURE 1:

Regional Trade Agreements in Effect Over Time

Source: Authors' calculations based on WTO.

blocs are moot--RTAs have proven to be more trade-creating than trade-diverting. The question today should not be whether RTAs undermine the multilateral trading system, but whether and how they can be additive to the WTO system. RTAs have emerged as incubators of new trade and trade-related rules in such areas as services trade, investment regulations, customs procedures and trade facilitation, environment, intellectual property rights, and e-commerce. RTAs have also been found to impart benefits that go well beyond traditional analyses on gains from trade, such as propelling export-oriented, efficiency-seeking investment flows among the members; encouraging cooperation among the members on customs and infrastructure integration; and helping relax the political economy constraints to multilateral trade talks in member nations.

It is not practical or even desirable to force RTAs into a certain mold. Rather, trade policymakers should focus on whether and how RTAs can be additive to the global trading system, and help deepen and enhance multilateral commitments. The purpose of this paper is to seek answers. One answer revolves around multilateralizing RTA disciplines and best practices. However, it may require changes in the World Trade Organization's (WTO) negotiation modalities for that to occur--a shift from unanimity and single undertaking rules to plurilateral agreements among coalitions of the willing. More generally, as a multilateral organization, the WTO is uniquely placed to act as a dedicated clearing house and forum where all matters related to RTAs and their rules and their practices could be discussed among all WTO Members. Such a forum alone would also help transfer best RTA practices from one RTA to another. It can readily draw on the countless datasets and analyses that have been produced around the world for years in row.

Section 2 reviews the economic and political drivers of trade regionalism, and examines RTAs' compatibility with the GATT and WTO Agreements related to them. Section 3 discusses the various multilateral efforts to deal with RTAs. Section 4 examines RTAs' benefits beyond market access in goods in

areas such as services, customs procedures, and investment. Section 5 discusses the evolution of the RTA "ecosystem," while Section 6 puts forth policy proposals for building a new relationship between RTAs and the multilateral trading system.

REGIONALISM VS. MULTILATERALISM: A FALSE CHOICE?

RTAs have been forged for centuries. The first modern-day RTAs were launched in the late 1950s. But it is since the 1990s that RTAs have spread like wildfire around the world. The wave started with the formation of sub-regional pacts, such as the Southern Common Market (MERCOSUR) forged in 1991 between Argentina, Brazil, Paraguay, and Uruguay; the consolidation of the European Union (EU), including the launch of the single market in 1993; the deepening of the Association of Southeast Asian Nations (ASEAN) throughout the 1990s; and, perhaps most notably, the formation of the North American Free Trade Agreement (NAFTA) between the United States (US), Canada, and Mexico in 1994.

Bloc formation was followed by prolific bilateralism. The EU forged numerous FTAs with Eastern European countries on the verge of becoming its members, while the US negotiated FTAs with Chile and Central America, and Latin American countries signed agreements with each other. The RTA wave subsequently engulfed Asia. The latest RTAs are transcontinental, with such partners as the US and Morocco, Mexico and Japan, and Chile and the EU recently forming bilateral agreements, among numerous others.

After being reticent until the 1990s to form preferential agreements, the US has become one of the most prolific integrators, signing 14 agreements in little over a decade with partners in the Americas, Asia, and the Middle East, and currently pursuing the rather ambitious TPP agreement

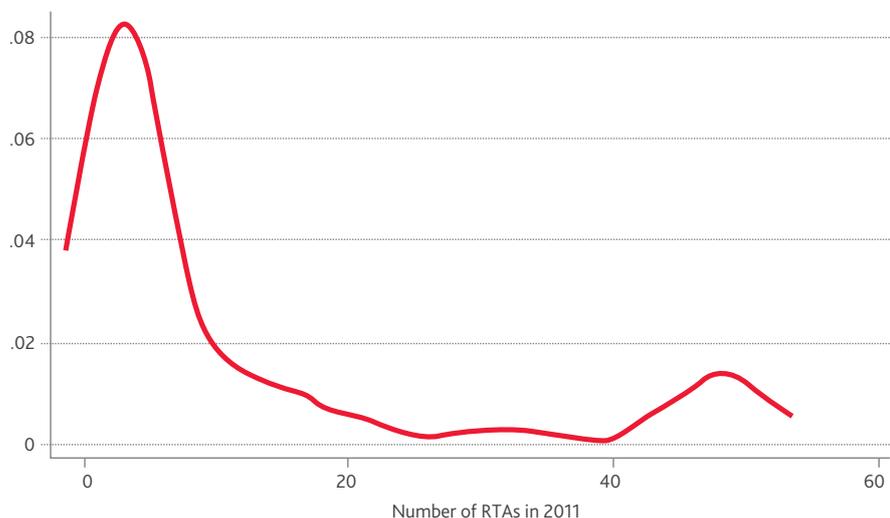


FIGURE 2:

Distribution of Number of RTAs in which Countries Participate in 2011

Source: Authors' calculations based on WTO.

with several Pacific Rim nations. Other particularly keen integrators include Mexico, Chile, Peru, Singapore, Canada, and the EU.

Integration schemes have mushroomed, and their content has become more complex and encompassing. Most agreements go beyond market access in goods to address trade in services and so-called behind-the-border issues, such as investment, intellectual property rights, competition policy, government procurement, and e-commerce. RTAs come in many flavors, but they also have clustered into distinct "families," particularly around key trading nations such as the US, EU, and Singapore. US agreements and the many agreements tailored after them in the Americas are particularly encompassing, as are the EU's agreements. Some sub-regional pacts have taken collaboration even further to issues ranging from macroeconomic cooperation to labor mobility and coordination of members' positions in multilateral trade negotiations.

Remarkably, GATT and WTO Members have been forming RTAs all the while, concluding seven multilateral trade rounds, establishing the WTO in 1994, and, since 2001, negotiating the Doha Round agreement. There are countless theories on why practically all the 154 WTO Members pursued regional integration alongside multilateral liberalization processes. Some focus on interest group pressure by exporter, importer, and investor lobbies, others on political leadership, and still others on strategic considerations in the world economy and politics and the dynamics of the multilateral trading system.² For example, RTAs can offer their members international bargaining power; insurance against external shocks or trade wars; and cooperation beyond trade in such areas as investment and infrastructures. For several WTO members and prolific trading nations such as Chile, Peru, and Mexico in Latin America, or India and the ASEAN countries, regional and bilateral agreements are now the preferred and most important means to conduct economic exchange with their trading partners. The world's largest traders--the US, China, the EU, and Japan--are on the same path.

Do RTAs "Comply" with Multilateral Trade Rules? The Building Bloc-Stumbling Bloc Debate

Whether trade regionalism is driven by politics or the expansion of intra-regional economic ties, RTAs are a very prominent part of the world trading system and the global economy, and they cover nearly half of global trade flows. RTAs have essentially proliferated alongside, yet uncoordinated by, the GATT/WTO system. Two parallel systems, global and regional, are now in place.

The conventional policy question surrounding RTAs has been whether they help or hamper the global trading system and MFN treatment. This is an important question both from a legal, formal point of view and from an actual, economic point of view -- incompatibilities between RTAs and the multilateral trading system could be associated

with violations of international trade law and could seriously distort global trade flows, production patterns, and economic growth. It is also a big question that has troubled GATT and WTO Members for decades.

From the beginning, the GATT system allowed member countries to grant each other preferential treatment under free trade areas or customs unions, as long as certain conditions were met. These conditions were defined mainly in GATT Article XXIV, but also in the General Agreement on Trade in Services (GATS), other WTO Agreements, and the so-called Enabling Clause, which exempts developing countries from MFN obligation for RTAs they form with each other. GATT Article XXIV stipulates that Members notify their RTAs to what is now the WTO, and that RTAs liberalize "substantially all trade" among Members "in reasonable length of time" and not introduce new "restrictive rules on commerce."³ The article also demands open regionalism--that RTA members do not raise barriers to third parties.

Concerns that RTAs are protectionist instruments have, since the early 1980s, prompted three major efforts in the GATT/WTO system to somehow regulate them.⁴ However, WTO Members have practically never debated or agreed whether any one RTA breaches multilateral trade rules, let alone the revised Article XXIV--multilateral, top-down regulation of RTAs has not worked. This is hardly surprising. WTO Members are jealous of their agreements, and unlikely to agree to any multilateral rules that would curb their ability to negotiate bi- and plurilateral agreements or force them to modify their existing agreements. Moreover, since all WTO Members with the exception of Mongolia belong to at least one RTA, all Members are reluctant to challenge the RTAs of other Members as discriminatory, let alone take another Member to the dispute settlement body, as the challenger could be next called out. As such, the dispute settlement body has dealt with RTAs on only a handful of occasions.⁵

Yet WTO Members have been concerned about the systemic implications of RTAs. In 1996, the WTO General Council established the CRTA as a means to examine individual RTAs and consider their systemic, cross-cutting implications for

2 | The literature is huge, so only some representative studies are highlighted here. For more exhaustive literature reviews, see, Winters 1996; Baldwin 2008; Bhagwati 2008; Mansfield 1998; World Bank 2000; Schiff and Winters 2003; Estevadeordal and Suominen 2009.

3 | For the purposes of Article XXIV, a customs union is understood as "the substitution of a single customs territory for two or more customs territories, so that (i) duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and, (ii) ... substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union." A free trade area is "a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories."

the multilateral trading system. Members that were eager to engage in the debate included Australia, Hong Kong China, India, Japan, Korea, New Zealand, and Pakistan, while the EU and the US, both of which were increasingly engaged in negotiating RTAs, were reluctant. The committee remained dormant, not issuing any examinations in 1996-2001.⁶

Have WTO Members complied with Article XXIV? The answer is negative in the sense that numerous RTAs among developing countries are exempted. But it also depends on how exactly the multilateral disciplines governing RTAs are interpreted.⁷ WTO Members' interpretations of the Article vary widely (see Estevadeordal and Suominen 2009). For example, "substantially all trade" has at least four interpretations--a quantitative approach geared to a statistical benchmark, such as a percentage of trade between RTA parties, most commonly suggested as 90, 85, and 80 percent; and a qualitative approach stipulating that no sector (or at least no major sector) should be kept from liberalization, with definitions of "sector" varying widely.

Empirically, most agreements do attain some of these most common interpretations of "substantially all trade" and "reasonable length of time"--liberalization of 90 percent of tariff lines and about the same amount of trade by year ten into the agreement (Estevadeordal and Suominen 2009). However, there are also a number of outlier RTA parties (in general developing countries) that are too many, and do not want to single out product categories (particularly sensitive sectors such as agriculture, textile and apparel, and footwear) that have prolonged tariff phase-outs and/or non-tariff barriers.

There also is no clear agreement as to what constitutes "other restrictive regulations of commerce." RTAs carry several rules that can qualify the extent of market access that tariff liberalization provides, such as tariff rate quotas; special safeguards; anti-dumping regulations; non-tariff measures; and rules of origin (RoO). Such disciplines are often put in place due to political reasons--governments may be more willing to engage in deep tariff liberalization in RTAs when defensive instruments are also available. However, the distortionary impact of these instruments can be significant and accentuate over time, as such rules tend to remain in place even after preferential tariffs have been phased out. For example, by tying final goods producers to using intra-RTA sourcing even if it is inefficient, stringent RoO can at the extreme augment intra-RTA final goods producers' production costs to the point where compliance costs exceed the benefits that RTA tariff preferences confer.⁸

RTA members' compliance with the prohibition against raising barriers to third parties is also disputed. Indeed, economists have long engaged in a contentious debate on whether RTAs are "building blocs" or "stumbling blocs" to multilateral trade liberalization. The building bloc camp argues that RTAs fuel the liberalizing logic of the multilateral system; help advance global trade talks; and serve as laboratories for new trade rules that could eventually

be multilateralized. The stumbling bloc camp maintains that RTAs are discriminatory instruments that lead to trade diversion and deviate governments' attention from multilateral trade talks.

4 As early as 1983, the GATT Director-General created an independent group of seven eminent persons to study and report on the problems facing the international trading system. The Leutwiler Report issued in March 1985 concluded that multilateral "rules permitting customs unions and free-trade areas have been distorted and abused" and that "the exceptions and ambiguities which have thus been permitted have seriously weakened the trade rules, and make it very difficult to resolve dispute to which Article XXIV is relevant."

During the 1986-1994 Uruguay Round, a group of countries that included Australia, India, Japan, New Zealand, and Korea--nations that at the time had not set out to form numerous RTAs but did worry about the discriminatory impact of emerging agreements--called for toughening the language of Article XXIV (WTO 2011). India proposed reviewing the requirement that duties and other restrictive regulations be eliminated on "substantially all trade" between the RTA partners (Croome 1995). Japan called for improving the consultations before and after preferential agreements were reached, and for improved procedures for examination of such agreements, proposing for the establishment of special procedures separate from the GATT dispute settlement system aimed at discussing compensation for damages to outsiders to RTAs (Croome 1995). The Members that opposed Japan's proposal suggested that RTAs be analyzed under the newly-created Trade Policy Review Mechanism, which assesses WTO members compliance with their multilateral trade commitments.

The grievances did result in the Understanding on Interpretation of Article XXIV, which helped clarify "reasonable length of time" as 10 years into an RTA's lifespan and fine-tuned paragraph 5 to call for multilateral assessments of "the general incidence of the duties and other regulations of commerce applicable before and after the formation of a customs union." The Understanding also establishes procedures in cases where non-members to a customs union be compensated if the common external tariff applied by the customs union is above the level of the tariff applied by any of the members prior to its forming. It also posits that concerns related to Article XXIV could be submitted to dispute settlement (Croome 1995). Despite initial opposition by the EU, India, and Yugoslavia, the Understanding was adopted and became part of the Uruguay Round agreements (WTO 2011). A further important outcome of the Uruguay Round was the inclusion of a provision on the regulation of regional and bilateral agreements on trade in services in GATS.

5 The main one is *Turkey-Textiles*, the WTO Appellate Body held that the burden of establishing that an RTA meets the requirements of Article XXIV falls on the respondent WTO Member if it invokes the RTA to justify a discriminatory measure.

6 One of the reasons was that WTO Members were reluctant to provide information or agree to conclusions that could later be used or interpreted by the WTO's dispute settlement panel. The process was also stifled by the disagreements over the terminology of Article XXIV, and the lack of specific multilateral language on such provisions as preferential rules of origin. Also views on whether the CRTA or the dispute settlement body should deal with RTAs remain divided. Others hold that the examination of the consistency of RTAs ought to be reserved solely to the CRTA. One notion is that GATT and WTO rules applying to RTAs are of less relevance today in the light of the fact that trade diversion is reduced as a result of multilateral tariff reductions. The empirical evidence on RTAs' positive welfare effects, and that they are different from WTO agreements lie in that they cover more trade-related disciplines (Mavroidis 2010). As such, the Transparency Mechanism should become the de jure new forum to discuss RTAs within the multilateral trading system.

7 Indeed, the very design of Article XXIV was not immune to politics. It was sponsored in the 1940s by the US, a staunch advocate of multilateralism and non-discrimination, as a means to address customs unions, but it was extended to allow for the formation of FTAs to accommodate the imminent US-Canada FTA that was under secret negotiations but failed to materialize (Chase 2006).

While a priori both views find support in the empirical literature, overall available evidence can be considered to favor the building bloc thesis. Limao (2006) and Karacaovali and Limao (2008) analyze the impact of preferential trade liberalization on multilateral trade liberalization at the Uruguay Round in the US and EU, respectively, and find that liberalization was less in products where preferences were granted. More specifically, Limao (2006) concludes that the US cuts in MFN tariffs were small for products imported under preferential trade agreements (PTAs) relative to similar products imported only from non-members. The subsequent study by Karacaovali and Limao (2008) shows that the EU reduced its MFN tariffs on goods not imported under PTAs by almost twice as much as it did on PTA goods. The implication of such a negative relationship between multilateral and preferential trade liberalization is that these large countries offer preferences on a unilateral basis to extract concessions from the recipients in non-trade areas. So they tend to resist liberalization to prevent erosion of preferences. Limão and Olarreaga (2006) make a similar finding in the case of import subsidies provided to RTA partners by the US, EU, and Japan.

The studies referred to above concentrate on large and developed countries. Related papers considering developing countries include Baldwin and Seghezza (2007), Estevadeordal et al. (2008), and Calvo-Pardo et al. (2009). Baldwin and Seghezza (2007) find that these tariffs are complements, not substitutes, since margins of preferences tend to be low or zero for products where nations apply high MFN tariffs. They argue that the positive correlation between MFN and preferential tariffs might be caused by sectoral vested interests that (co-) determine both types of tariffs. Estevadeordal et al. (2008) conclude that regional trade liberalization has had a complementary effect on general trade liberalization in Latin America, particularly in countries that are not members of customs unions.⁹ On the same lines, Calvo-Pardo et al. (2009) find that preferential tariff liberalization caused external tariff liberalization in ASEAN countries. Agreements in Latin America and Asia can therefore be seen as forces that operated in favor of broader liberalization.

More generally, the divergence in results for developed and mostly developing countries might be traced back to prevailing preferential tariffs. Thus, preliminary evidence in Ludema et al. (2012) for Latin American countries suggests that when preferential tariffs are above zero, external and internal liberalization are complementary, but they become substitutes after those tariffs reach zero. The rationale would be that in the absence of flexibility in preferential tariffs when they hit zero, only external tariffs remain to accommodate political economy forces.

WTO vs. RTAs as Trade-Creating Institutional Arrangements

Even if they are not free from political economy constraints, RTAs can, on the whole, be considered good cholesterol for world trade (though most studies have glazed over the complexity of RTAs, operationalizing them as a dummy

variable). Frankel et al. (1997) analyze the EU, MERCOSUR, the ASEAN, and East Asia, concluding that regionalism has over the past decades been trade-creating. Soloaga and Winters (1999) find that except for Latin America, RTAs of the 1990s did not boost intra-bloc trade significantly, and also that there was trade diversion only in the EU and the European Free Trade Association (EFTA). However, Adams et al. (2003) estimate that 12 of 16 trade agreements, including the EU, ASEAN, and NAFTA, have diverted more trade than they have created among members. The World Bank (2004) unsurprisingly finds that RTAs whose members have high external barriers, especially RTAs in Africa, are trade-diverting, while RTAs where members have reduced external barriers are trade-creating. Based on the experience of seven RTAs (EU, CAN [Comunidad Andina, or Andean Community] NAFTA, CACM [Central American Common Market], MERCOSUR, ASEAN, and LAIA [Latin American Integration Association]), Carrere (2006) concludes that these agreements have generated a significant increase in trade between members, often at the expense of the rest of the world. DeRosa (2007) shows that some of the world's major RTAs, such as the EU, NAFTA, ASEAN, MERCOSUR and EFTA, are trade-creating—even though there is trade diversion in agriculture, an unsurprising finding given the pervasive barriers in the sector around the world. Using different empirical approaches, Baier and Bergstrand (2007, 2009), Egger and Larch (2011), and Egger et al. (2011) find that trade agreements have increased members' bilateral international trade flows. Egger et al. (2008) show that in the case of developed countries, such trade volume effects are primarily associated with growing intra-industry trade as opposed to inter-industry trade. Suominen (2004) finds that while RTAs are trade-creating, restrictive RoO can cause trade diversion in inputs. Also tariff rate quotas (TRQs) in RTAs can be discriminatory. TRQs in RTAs are usually additional to TRQ entitlements under the WTO Agreement on Agriculture.¹⁰ That the expansion of the quota of one supplying RTA partner can cause some erosion in the quota rents to other quota holders has raised suspicions that TRQs in RTAs are inconsistent with GATT and WTO rules.

The latest findings attest to a distinction between the "closed regionalism" of the import substitution policies in the 1960s and 1970s and the RTA wave of the 1990s and

⁹ Estevadeordal et al. 2009 observe that this pattern does not hold across sectors. More precisely, while in some industries, complementary effects between both kinds of trade liberalization are observed, in others no significant links are detected and—in a few cases—even substitutability seems to prevail. Variation across sectors appears to be systematically related to both import demand elasticities and countries' sectoral comparative advantages. In particular, countries are more likely to cut external tariffs once they have lowered regional tariffs in those sectors with larger import demand elasticities and where they have an overall comparative advantage.

¹⁰ The Appellate Body in the dispute *Turkey—Restrictions on Imports of Textile and Clothing Products* found that a dispensation could be available in cases where it could be shown that the proposed measure is essential to the formation of the RTA, but did not set the criteria by which this condition could be fulfilled in practice.

2000s, which was embedded in a context of multilateral liberalization. However, the conventional notion has remained--that RTAs are second-best to global trade liberalization. In theory, they are--multilateral liberalization and the MFN principle are economists' panaceas. There is evidence of the benefits of multilateral liberalization. For example, Subramanian and Wei (2007) argue that the WTO system has had a massive positive impact, more than doubling world trade from their counterfactual alternative. According to their estimates, additional imports by industrialized countries were USD 8 trillion more than they would have been in the absence of the WTO. This trade-promoting role of the WTO has been, however, uneven across countries and sectors.¹¹

At the same time, RTAs have attained far greater depth and breadth than multilateral talks. They have also had impact. Rose (2004a) contends that countries joining or belonging to the GATT/WTO do not significantly trade more with each other than outsiders.¹² In contrast, the Generalized System of Preferences (GSP) and RTAs appear to have played an important role in encouraging trade.¹³ Eicher and Henn (2008) explicitly combine the various approaches to trade opening--WTO accession, reduction in tariffs abroad, and RTA formation--finding that once previously omitted variables are stacked alongside the WTO variable, the positive WTO effects vanish altogether. RTAs emerge as stars in their analysis, on an average resulting in trade creation amounting to 123 percent of pre-PTA bilateral commerce (see also Hufbauer and Schott 2008). The positive news from these dueling analysts seems to be that pulling the liberalization lever does generate greater trade flows--the debate is just what policy lever yields the biggest flow.¹⁴

BEYOND BUILDING BLOC--STUMBLING BLOC DEBATE: RTAS AS WTO+

Efforts at the WTO to assess, let alone regulate, RTAs have been rather narrow in focus and had scant impact. Granted, while GATT/WTO may have influenced RTA negotiations, it has never been employed to "tame" or discipline supposedly discriminatory reciprocal trade agreements (Davey 2011; Low 2008). Multilateral measures on RTAs have arguably also become less relevant--although the number of RTAs has skyrocketed, the odds of trade diversion have decreased with unilateral, preferential, and multilateral tariff cuts around the world. The WTO's ineffectiveness in regulating RTAs is also likely more positive than negative--it gives RTA negotiators elbow room to continue creating and experimenting with new trade rules that would be all but impossible to agree on across the WTO membership. Indeed, RTAs have become WTO+ laboratories of trade rules and also often entail deep, mutually beneficial integration for the parties. The following reviews RTA disciplines in investment, services, competition policy, and customs procedures.

Investment

International investor protection and investment liberalization issues are regulated by a multilayered set of bilateral, regional, sectoral, plurilateral, and multilateral agreements.¹⁵ The main multilateral instruments governing investment issues include the Agreement on Trade-Related Investment Measures (TRIMs) and the Agreement on Subsidies and Countervailing Measures (ASCM), which limit WTO Members' abilities to apply certain kinds of measures to attract investment or influence the operations of foreign investors. Also the GATS, the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), and the plurilateral Agreement on Government Procurement include provisions pertaining to investments, particularly to the entry and treatment of foreign enterprises and the protection of certain property rights. The Understanding on Rules and Procedures Governing the Settlement of Disputes contains rules for addressing conflicts that arise under these agreements.

TRIMs applies to measures affecting trade in goods. It exhorts the national treatment principles of the GATT, and bars investment measures that lead to quantitative restrictions. TRIMs also requires members to inform each other of any rules that do not conform to it. There are further TRIMs provisions that are viewed as inconsistent with GATT articles, including local content and trade balancing requirements. As compared to the extensive, in-depth coverage of investment rules in bilateral investment treaties and RTAs, TRIMs is much thinner. After a failure at the WTO's Cancun Ministerial in September 2003, the General Council in July 2004 dropped investment along with two other so-called "Singapore issues"--competition policy and transparency in government procurement. By and large, the innovation in investment rules continues to be accomplished in bilateral investment treaties (BITs) and RTAs.

From any one country's perspective, the multilayered approach to investment rules can help signal credibility to investors. Yet, at the global level, it has forged a highly

- 11 Industrial countries that participated more actively than developing countries in reciprocal trade negotiations witnessed a large increase in trade. In addition, bilateral trade was greater when both partners undertook liberalization than when only one partner did. Finally, sectors that did not witness liberalization did not see an increase in trade.
- 12 Rose 2004b argues that GATT/WTO member do not have more liberal trade policies. Trade liberalization, when it occurred, usually lagged behind the GATT entry by many years, and the GATT/WTO often admitted new members that remained closed for years.
- 13 According to Rose 2005, there is little evidence that membership in the GATT/WTO has had a significant dampening effect on trade volatility.
- 14 Anderson and van Wincoop 2001 contend that the volume of trade between two countries depends on the height of the bilateral barriers between them relative to the average trade barriers each country faces with all its trading partners. Following this logic, a country can increase its trade volume both by preferential and multilateral liberalization.
- 15 Bilateral investment treaties (BITs) have been found to have a significant positive impact on FDI flows (for example, Egger and Merlo 2007).

complex web of agreements. However, there is already a de facto harmonization process in place, as most RTAs feature similar main principles, such as non-discrimination, and also because the many agreements the US and EU have entered into are very similar with each other.

Services

The GATS covers all services except those provided in the exercise of governmental authority and, in the air transport sector, air traffic rights and all services directly related to the exercise of traffic rights. The GATS has governed multilateral services rules since the Uruguay Round. It contains a number of general obligations applicable to all services, including an MFN rule and a transparency rule, but in market access each member defines its own obligations through its own schedule.

Services chapters in RTAs usually only cover Modes 1 and 2 (cross-border supply and consumption abroad), and are thus separate from RTA chapters on other forms of trade in services--investment and temporary entry of business persons. The coverage of services in these two sectors has intensified in recent US agreements with Chile, Peru, Colombia, and Panama.

How do RTAs' rules in services interact with the GATS? Roy et al. (2007) assess 28 RTAs, arguing that they have tended to provide important advances when compared to GATS schedules in three ways--RTAs are often very substantive and have helped propel liberalization in sectors that have only thin commitments in the GATS, such as financial services, and in more traditionally contentious areas such as audiovisual or education services. Countries that have used negative-list approaches in RTAs have bound at least the existing level of openness for a large majority of sectors, a measure that arguably instills predictability in a bilateral relationship and is key to attracting investment and spurring cross-border trade. Countries have submitted a high number of sub-sectors to liberalization in the GATS schedules as well as their GATS offers in the Doha Round, which they have freed in RTAs. As such, either the GATS commitments did not reflect their applied regime or, as is more likely, the improved commitments in RTAs induced actual liberalization and new commercial opportunities.

In general, RTAs in the Americas are particularly comprehensive in services and often go well beyond GATS provisions. In particular, NAFTA-inspired agreements feature a much wider schedule of commitments than is made in the GATS (see Houde et al. 2007).¹⁶ The commitments of developing countries are in general shallower than those made by the developed countries. Paradoxically, far-reaching liberalization in RTAs could particularly lower developing countries' incentives to negotiate further at the multilateral level, particularly if multilateral talks provide for limited reciprocity. Indeed, the way in which developed countries have induced developing countries to open services sectors is by offering, through RTAs, preferential treatment in trade in goods as a quid pro quo.¹⁷

The issue linkage is not as easy to make at the global level. The Doha Round services negotiations have proven less far-reaching and ambitious than many developed countries would have hoped. Industrial countries are looking for developing country commitments to reform "infrastructure services," such as banking, insurance, telecommunications, and air transport, while developing countries expect new opportunities to provide labor-intensive services, such as healthcare, construction, and basic information technology services (Scott 2007).

Competition Policy

The GATT and WTO Agreements do not contain a standalone set of competition policy rules. However, there are a number of multilateral provisions that do address competition policy issues (see Anderson and Evenett 2006). For instance, GATT Articles VIII and IX on monopolies and exclusive suppliers, and anti-competitive practices restricting trade in services, respectively, as well as the Agreements on Safeguards bar signatories from endorsing or encouraging non-governmental measures akin to voluntary export restraints, orderly marketing arrangements, or other governmental arrangements.

TRIPS empowers signatories to act against anti-competitive practices in the licensing of intellectual property rights.¹⁸ Attempts to fashion a more comprehensive multilateral framework of competition policy provisions have thus far been unsuccessful. The WTO Ministerial Conference in Singapore in 1996 created the Working Group on the Interaction between Trade and Competition Policy to study the issue; the Doha Ministerial Declaration of 2001 sharpened the group's focus to clarifying core principles, including transparency, non-discrimination and procedural fairness, provisions on cartels, modalities for voluntary cooperation, and capacity building, to support fostering competition policy institutions in developing countries. However, in July 2004, the WTO General Council dropped competition policy from the negotiation agenda. Some of the reasons cited included a rejection of the proposed negotiation framework by developing countries as excessively intrusive, and a perceived lack of capacity to negotiate this area.

¹⁶ Mexico, Morocco, and Singapore make complete commitments with very few reservations in their agreements with the US in sectors where they have no commitments at the multilateral level. Also the US, Australia and Japan have more commitments in their bilateral agreements than in their GATS schedules.

¹⁷ Egger et al. 2012 find that, for developed countries, the responsiveness to the respective preferences is much bigger for trade in services than for trade in goods.

¹⁸ In the meantime, the United Nations 1980 Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices, while voluntary and of limited practical relevance, iterates the importance of complementing tariff and non-tariff liberalization with non-restrictive business practices.

As is the case in investment, the deepest and most comprehensive set of competition policy rules appear to be forged in the context of RTAs (for a review of the specific competition provisions in RTAs, see Brusick et al. 2005). Perhaps encouragingly for future multilateral talks, there are broad similarities between the two most dominant competition policy models in RTAs, those of the EU and US RTAs, respectively (Baldwin et al. 2007). Moreover, RTA provisions on competition policy have tended to have solid non-discrimination clauses that “multilateralize” the RTA obligations to non-members. For instance, a US firm in Turkey has the same rights before Turkish competition authorities as a EU firm because the EU-Turkey agreement gave rise to Turkey’s competition policy framework. In other words, in some instances, RTAs have helped open up an area where prior national rules, if in place, may have been too stringent. It is in countries without explicit competition policy rules where nationality concerns, rather than non-discrimination, may arbitrate access.

Customs Procedures

RTAs’ customs procedures and trade facilitation provisions are in general compatible with three main international instruments in these areas.¹⁹ They are the Arusha Declaration and the UN/EDIFACT Initiative that address the use of technology and data processing issues; the World Customs Organization’s (WCO) Revised Kyoto Convention, which addresses such areas as review and appeal, customs clearance, and uses of new technologies; and GATT/WTO trade facilitation provisions, including Article V (Freedom of Transit), Article VIII (Fees and Formalities connected with Importation and Exportation), and Article X (Publication and Administration of Trade Regulations). Indeed, trade facilitation and customs procedure measures in RTAs seem to have paralleled the development of international instruments. For instance, RTAs that entered into force after 2000 tend to include such provisions as the release of goods, automation, risk assessment, or express shipments—issues also included in the 1999 Revised Kyoto Convention.

The Doha Round negotiations on trade facilitation are relatively narrow in scope, aimed at clarifying and improving GATT Articles V, VIII, and X. The negotiations also contemplate technical assistance and capacity building for developing countries to implement future commitments. Some private sector observers think that limiting the scope of trade facilitation within the scope of these articles alone can be dangerous, as it might divert attention away from the manifold challenges surrounding the movement of goods. RTAs provide an opportunity to mitigate such outcomes in three ways. First, unlike WCO provisions, RTA provisions are binding and enforceable via dispute settlement mechanisms. Second, given that customs procedure and trade facilitation disciplines are relatively similar across RTAs, they can facilitate and accelerate convergence in these disciplines around the world. Third, to the extent that RTAs streamline customs procedures and facilitate trade, they are inherently good for

the multilateral trading system--the resulting lowered trade costs boost trade with all trade partners.²⁰

Beyond Static Gains from Trade: Dynamic Benefits from the Expanding Scope of RTAs

Some newer RTAs are going much beyond these provisions that are more standard in RTAs. The foremost example is the TPP. The draft agreement includes various groundbreaking commitments that go much above and beyond tariff opening, such as renunciation of current manipulation and mercantilist practices; intellectual property rights protection; deep liberalized trade in services; removal of barriers to foreign direct investment/ownership; elimination of a host of other non-tariff barriers such as manipulation of standards; transparency and openness in government procurement practices; and restrictions on preferential treatment toward state-owned enterprises.

Such growing scope of RTAs means that judging them by their static trade gains is outdated. RTAs are recognized to impart significant dynamic and non-traditional gains:²¹

Credibility: As the Washington Consensus was taking hold in the 1990s, reformist interests in emerging nations pursued RTAs with major developed countries to signal their resolve not to renege on economic reforms to international investors. For example, Mexico joining the US and Canada in a legally binding, complex agreement with commitment from competition policy law to investment rules reduced its policymakers’ room for maneuver and ability to backtrack from legislative and regulatory changes related to the agreement.

Dynamic effects on trade: RTAs can also have dynamic effects on member countries’ trade.²² Estevadeordal et al. (2012) show that RTAs in Latin America appear to have served as an export platform. More precisely, by reducing tariffs and thereby allowing for increased intra-regional exports, these

19 Time associated with customs procedures can be an important barrier to trade (for example, Djankov et al. 2010; and Volpe and Graziano 2012).

20 For a review of the specific trade facilitation provisions in RTAs see, for example, UNCTAD 2011.

21 Trade policy in general and RTAs in particular can also affect countries’ specialization patterns and the spatial distribution of economic activities. Combes and Overman 2004 and Brühlhart provide useful reviews of the relevant empirical literature. For evidence on Latin American see, Hanson 1998; Sanguinetti and Volpe Martincus 2009; Volpe Martincus 2010; Sanguinetti et al. 2010.

22 In particular, RTAs also produce similar dynamic gains as any trade liberalization, such as sifting and sorting. However, studies in general do not take into account the dynamic effects that trade liberalization might induce, such as the sift-and-sort features of Schumpeter’s “creative destruction.” The dynamic effects that trade liberalization might induce are difficult to quantify but are probably large. Differences between countries also make a difference--the most protected countries can reap much greater gains from new liberalization than relatively open ones.

agreements seem to have fostered exports of differentiated products to Organization for Economic Co-operation and Development (OECD) markets.²³

Effects on investment: RTAs that are particularly comprehensive help propel trade in goods and services as well as investment flows. Thus, Levy Yeyati et al. (2003) find that, on an average, regional integration contributes to attract foreign direct investment (FDI), although this is likely to be unevenly distributed across member countries. Baltagi et al. (2008) report significant positive effects of Europe agreements between Western and Central and Eastern European countries on bilateral FDI. Developing nations forge RTAs mostly to attract investment, which in turn can be channeled into building export platforms—not unlike the outcome of the NAFTA on Mexico's northern border.

Shaping participation in global value chains: RTAs can specifically affect countries' involvement in global value chains. For instance, Blyde and Volpe Martincus (2012) show that these agreements have had a significant positive effect on the number of foreign affiliates located in partners' territories.

Synergies among provisions: RTAs that yield synergies among their various provisions can accentuate positive effects. For example, simultaneous liberalization of tariffs, services, and investment can spur trade well beyond what a simple tariff lowering could. For example, Egger et al. (2012) find that the joint inception of goods and services preferences is associated with a welfare gain that is larger than the sum of those derived from an independent inception of goods and services preferences alone.

Synergies among multiple policy interventions: Improvements in infrastructure—regional road networks; energy transmission lines; transparent customs operations; fluid cross-border communications; services trade integration; and deep capital markets and financial integration—are key to tariff liberalization rendering the expected benefits. Thus, in 2000, 12 South American countries launched the Initiative for the Integration of Regional Infrastructure (IIRSA), which has developed 524 infrastructure projects across the region—covering transportation, energy, and communications. Beyond building physical infrastructure, the IIRSA also supports the harmonization of regulation across the region and improvements in cross-border traffic. Similarly, the Meso-American Integration and Development Project, which stretches from Mexico to Colombia, includes regional infrastructure and trade facilitation reforms. The importance of such initiatives that reduce non-tariff trade costs in general and transport costs in particular has been underscored in several studies (for example, Mesquita Moreira et al., 2008). More specifically, simultaneously acting on both the software (policy and regulation) and the hardware (physical integration) of integration help regions make more of it—such coordinated interventions facilitate trade, drive down the costs of business, and ensure a more equitable distribution of the gains from trade, thereby increasing stability.²⁴

Learning by negotiating and implementing: RTAs can also serve as training grounds for countries to negotiate and implement multilateral trade rules. For example, many Mexican officials became world-class trade negotiators after their “apprenticeship” with the US team in NAFTA talks in the early 1990s.

Bargaining power: RTAs can also help aggregate governments' preferences at regional levels, reducing collective action problems at the multilateral level, and leverage their bargaining power. Caribbean Community members have banded together to collectively negotiate at the WTO.

Cross-border cooperation: Trade agreements can serve as a focal point with real economic incentives to pursue further cross-border integration—increasingly important as regional and global cross-border externalities, such as migration, financial shocks, and environmental hazards, place an added premium on international coordination and pooling of resources for common policy responses (Devlin and Estevadeordal 2002).

Liberalizing logic of RTA system: RTAs have an internal liberalizing logic—their spread gives outsiders incentives to form new RTAs or to join existing ones, lest they see their market access erode (Baldwin 2006). This built-in logic of the RTA system will eventually culminate in a system ever closer to global free trade. In addition, RTAs are also an antidote to “free-riding,” the unhealthy flip-side of the MFN principle (Ludeman and Mayda 2009). While MFN wards off discrimination, it also enables slower liberalizers to enjoy the benefits of market opening by others and do less on their own. Countries that choose to free ride on the WTO system are increasingly left out when it comes to writing trade rules and enjoying access to foreign markets.

23 In related studies, Borchert 2010 finds that exporting a given product to the US had a positive effect on Mexican exports to third countries and that tariffs cuts associated with NAFTA had a direct positive effect on the probability to export to additional markets and a negative impact on the volume shipped, whereas Molina 2010 shows that previous export experience in a given product to an RTA has a positive effect on the probability that the same product is subsequently exported to a non-member country. Also related to this research, there are some recent papers that present theoretical mechanisms that generate systematic spatial patterns in exporting, and empirical evidence on these patterns. For instance, in Albornoz et al. 2012, firms learn about their export profitability only after engaging in exporting. Assuming that profitability is correlated over time and across destinations, their model predicts that firms that have successfully entered some market are more likely to access countries that are similar to it. In Chaney's 2010 model, firms can break into a market only if they have a contact. The probability of a given exporter acquiring such a contact in a new country is assumed to be increasing in the aggregate trade between the potential destination country and other countries that the firm was serving before. Finally, according to Morales et al. 2010, firms are more likely to enter countries that are similar to other destinations to which they have previously exported (extended gravity) because they have already completed part of the costly adaptation process (for example, identification of a distributor, product customization to adapt it to local tastes or to make it fulfill legal requirements imposed by national consumer protection laws, and so on).

24 See the Inter-American Development Bank's (IDB) Sector Strategy to Support Competitive Global and Regional Integration (2011).

PENDING CHALLENGES AND OPPORTUNITIES: CONVERGENCE, MULTILATERALIZATION, AND OTHER INNOVATIONS

RTAs address standard market access issues, but also several trade-related issues that are only partially addressed at the WTO, and an array of behind-the-border regulations, most of which have yet to be addressed at the multilateral level. As such, RTAs conceptually pose three distinct potential challenges to the global trading system—discrimination, transactions costs, and inefficiency.

Discrimination

Thus far, much of multilateral discussion has been on the potential discrimination that can result to non-members from RTAs' market access rules. This debate is increasingly found to be moot—most RTAs are found to be trade-creating. The very proliferation of RTAs, or new agreements between current insiders and outsiders, attenuates the discriminatory edge—Mexico's preferences in the US market are at least somewhat diluted by US FTAs with Chile, Colombia, and Peru.

To be sure, this does not mean that assessing and measuring discrimination is misguided—more can be understood about the trade effects of rules in different sensitive sectors and about more opaque rules such as RoO. RTAs' tariff preferences would also become a more prominent issue if the preferential margins suddenly became higher—if emerging markets and developing nations with substantial “water” between their applied and bound tariffs were to raise their applied tariffs. Moreover, there can be discriminatory effects beyond market access provisions, such as from regulatory harmonization among RTA members that locks them into a certain regime and complicates accessions to further RTAs with different rules (WTO 2011).

The point is that RTAs are about much more than market access, and the discriminatory effects of market access rules should not be the sole or even the primary focus of policy discussions. Besides, if history is a guide, policy recommendations flowing from such exercises are likely to go unaddressed by the WTO membership.

Transaction Costs: Toward Convergence?

The debate on RTAs needs to focus increasingly on transaction costs and coherence. Take transaction costs first. The end game of the current RTA frenzy could be competitive liberalization, whereby all countries have an RTA with each other. Without this, the RTA system remains an internal paradox. RTAs can and are designed to lower the costs of cross-border business, and they can provide for more efficient supply, production, and distribution networks. Yet, the spaghetti bowl of multiple overlapping RTAs can

also contain internal frictions that create transactions costs to companies operating across various RTA “theaters” simultaneously. These costs could be above and beyond what they would be if operating under a single set of trade rules.

This is critical in today's world economy. Unlike integrated production activities that were internalized in a company and centered in a few locations, today's production is segmented and spread over an international network of production sites. As a result, a growing share of global trade consists of intermediate goods shipped from one country to another, and many household items from cars to computers contain parts hailing from multiple countries. The explosion of intermediate trade has been particularly striking in Asia, where parts and accessories constitute about a quarter of all trade.

The RTA spaghetti raises transactions costs for companies that operate global supply chains. RoO protocols are a case in point. Studies by the Inter-American Development Bank (IDB) and Asian Development Bank (ADB) indicate that some 60 percent to 80 percent of large companies in diverse countries, such as Peru, Singapore, Thailand, and Mexico, would much prefer a world with a single agreement with a common set of rules of origin, or at least with regional mega-agreements, rather than today's world where they have to comply with multiple and overlapping RTAs (see Estevadeordal et al. 2009). The complexity is also troublesome to customs officials for verifying RoO in countries with multiple agreements, such as Chile, Mexico, Singapore, Thailand, the US, and Vietnam.

Erasing some of the transactions costs through forging larger integration zones can yield major economic gains, particularly for smaller countries. In a study of the Paneuro system, a vast system of cumulation implemented in 1999 across all bilateral FTAs the EU had with various Eastern European nations, cumulation increased trade between Eastern European spokes by between 7 percent and 22 percent, and the increase was between 14 percent and 72 percent for the benefiting sectors (see Augier et al. 2005, 2007). Harris and Suominen (2008) take the idea further to examine the effects of cumulation zones over the past 50 years, finding that adding partners representing 10 percent of world output to a “cumulation zone” was associated with a 3 percent increase in the bilateral trade of small countries. Importantly, this is a net effect, including any reduction in trade due to trade diversion.

Some groups of countries are making concrete efforts to converge their bilateral and plurilateral RTAs with each other into broader integration blocs—to use a gastronomic analogy, to build “lasagna plates” from the “RTA spaghetti bowl” (Figure 3). Such convergence processes are independent of the WTO, but complementary to the aim of building larger economies of scale and reducing the transactions costs that are by and large inherent to the spaghetti bowl.

The most prominent example of convergence was accomplished in Europe in 1999, when the EU created the Paneuro system. The system essentially substituted all the bilateral FTA commitments between the EU and the Eastern European nations for a single agreement, and in particular created a uniform RoO protocol covering all agreements. This was rather easy—the various bilateral FTAs were very similar in design. The Paneuro RoO have subsequently been transposed to the EU's extra-regional FTAs.

There are various examples of cumulation that do not fully reach the Paneuro-type diagonal cumulation in the Asia-Pacific, Latin America, and among US agreements.²⁵ Still another and more current prominent examples of

convergence-like process is somewhat distinct, they include the TPP in the Asia-Pacific, which currently encompasses 11 nations, which in turn have more than two dozen pre-existing RTAs with each other. Once formed, the agreement would essentially form a single agreement among these various nations; however, most likely the various bilateral FTAs would remain in force—essentially enabling the TPP member to choose among two distinct channels. In the Americas, Chile, Colombia, Peru, and Mexico, which have trade agreements with each other, are pursuing the Pacific Alliance that has freed 92 percent of products and harmonized rules of origin, among other measures. Costa Rica and Panama are observer members.

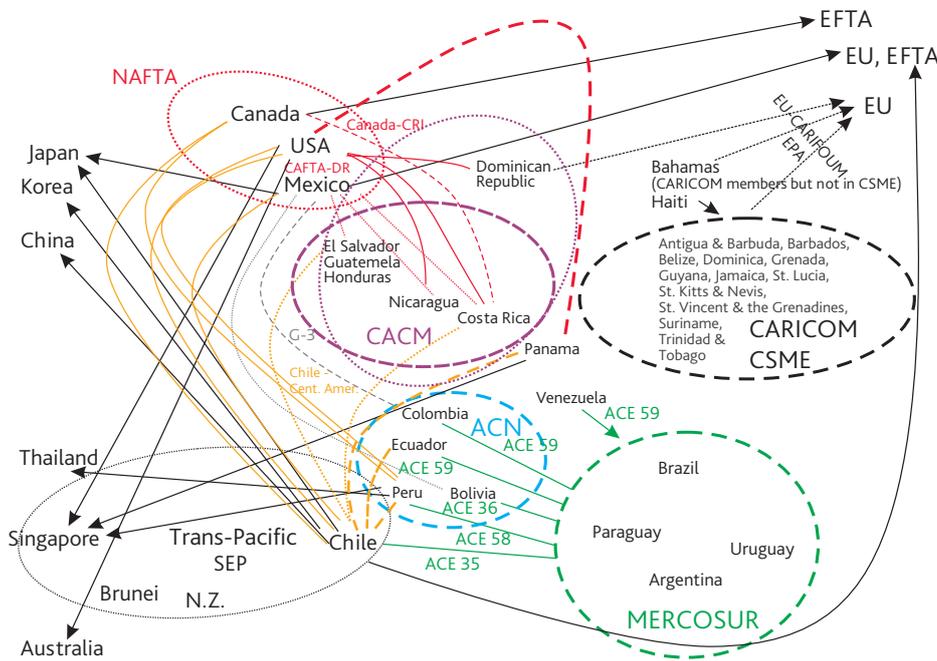


FIGURE 3:
The Spaghetti Bowl and Lasagna Plates
Spaghetti Bowl

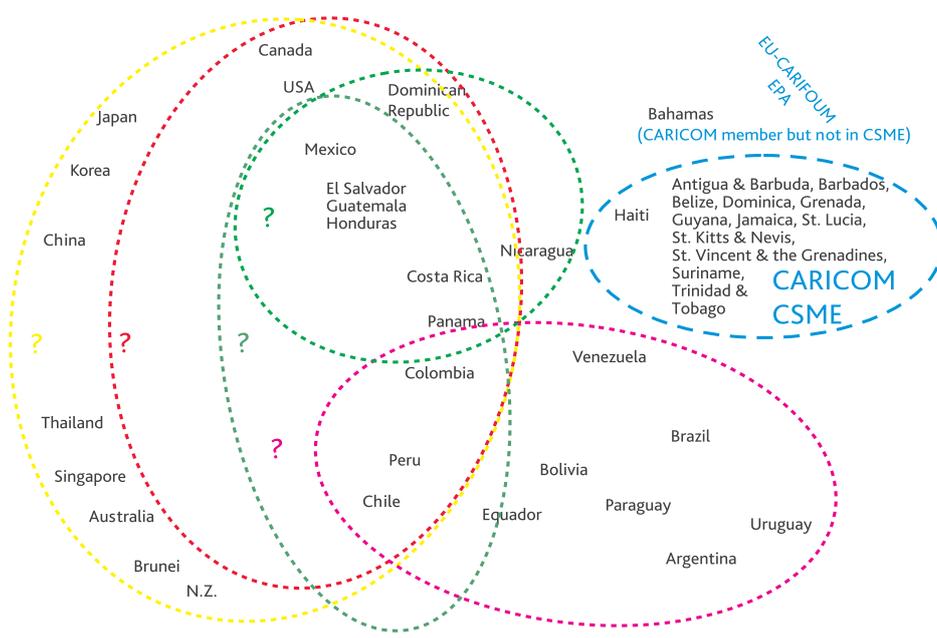


FIGURE 3:
The Spaghetti Bowl and Lasagna Plates
Lasagna Plates

For the multilateral system, convergence processes can be positive as long as they are based on open regionalism and do not introduce stringent RoO. They may also help aggregate their member countries' disparate preferences for multilateral bargaining. Convergence is also at least conceptually a feasible process--the target and the end result are clear (such as region-wide cumulation of production); trade and foreign policy benefits ought to be greater than in any one bilateral FTA; and a single large regional hegemonic actor, such as the EU or the US, may be able to propel the process unlike so far accomplished at the global level. To the extent that differences across pre-existing RTAs produce transactions costs to firms operating on two or more RTA fronts simultaneously, such convergence areas can also help member country firms diversify their export markets and lower the potential for distortive hub-and-spoke patterns.

A further advantage of convergence zones is that they almost inherently entice their members to go beyond the provisions in bilateral agreements. For example, the TPP would not only knit together several nations and agreements; but also stand out for holding the potential for a transformative "gold standard" trade agreement that charts the path for future trade agreements that are more comprehensive than current WTO-based ones and have stronger enforcement mechanisms.

However, there are several major considerations that would have to be addressed in any convergence process. First and foremost is the co-existence between a new set of converged rules and the rules of the other RTAs, and the actual contents of the resulting rules--which would ideally be more liberalizing than those of any of the component agreements. The most likely scenario is one of overlapping agreements (bilateral and plurilateral) rather than plurilateral agreements that automatically swallow the pre-existing agreements among members.

Inefficiency: Multilateralizing Regionalism?

Recent RTAs have addressed behind-the-border issues from intellectual property to competition policy and product norms in a very robust fashion. This is where the innovation in RTAs is occurring, and it is an area where the multilateral trading system lags well behind. Indeed, RTAs have gone so far beyond multilateral disciplines and mere tariff liberalization that they should be viewed as a distinct from the WTO system, not as a parallel, let alone a competing or conflicting system. The typically cited tension is one between the principle of subsidiarity, whereby common rules should be addressed at their lowest level of governance to be well-tailored for the needs of the parties, and efficiency, whereby other jurisdictions should also accede to the rules, especially if and when such rules have spillover effects on them and yield public goods.

More concretely, it is perfectly reasonable for two or more RTA members to forge rules that are tailored to their idiosyncratic circumstances and purposes. The more

complex question is what such rules do--whether they are discriminatory effects against outsiders; whether they lock in the insiders into a certain regime; and, as above, whether they increase transactions costs for the parties that need to deal with multiple RTA fronts at once. Evidence thus far seems to indicate that trade effects of various RTA rules to third parties are positive. For example, the EU's single market appears to have increased access at least as much for firms from third parties (Mayer and Zignago 2005).

Moreover, given that regulations in RTAs are tailored to the parties' needs and political economy circumstances, expanding them to third parties is not necessarily easy. Also broad-based or quick multilateralization can be complicated--RTAs are inherently motivated by their members' interests to deepen their multilateral commitments, and negotiating similar rules at the multilateral level is practically impossible. There thus seems to be an inherent division of labor between RTAs and the WTO. However, it is entirely plausible that there would be efficiency gains for the global trading system from expanding the scope of parties with common regulations or even mutual recognition--that is, from multilateralizing certain RTA disciplines.

Multilateralization has been discussed quite intensely over the past five years, and the most often cited examples of the mechanics by which it might work is the Information Technology Agreement (ITA), which in 1996 brought tariffs of IT goods to zero among the original 14 WTO members (the then 15-member EU counted as one member). Only interested WTO Members that were genuinely committed to signing the ITA took part in the negotiations; however, further parties joined, and the agreement now has 46 of the largest WTO Members, such as the US, the EU, Japan, and China. ITA-type plurilateral deals are now advocated as a potential future negotiation modality in the WTO (see Hufbauer and Suominen 2010). The post-Uruguay Round agreements on basic telecommunications and financial services are two cases in point. RTAs can play a powerful role in this process. Asia-Pacific Economic Cooperation (APEC) has made an attempt to encourage commonalities among the

25 In the South Pacific Regional Trade and Economic Co-operation Agreement (SPARTECA), Australia and New Zealand allow members of the South Pacific Forum islands to cumulate among themselves and still receive preferential treatment. The Canada-Israel PTA permits cumulation with the two countries' common PTA partners a set of countries which includes the US and no other. This extension of cumulation most likely accommodates existing integration of Canadian industry with US suppliers. US agreements with Israel and Jordan also have some cumulation. Singapore has pursued innovative mechanisms in its PTAs that, while not extending cumulation in the conventional sense of the term, do allow for greater participation of non-members in the production of originating goods. The main mechanism is outward processing (OP), which is recognized in all of Singapore's PTAs. OP enables Singapore to outsource part of the manufacturing process, usually the lower value-added or labor-intensive activities, to neighboring countries, yet to count the value of Singaporean production done prior to the outsourcing activity toward local, Singaporean content when meeting the RoO required by the export market. There are as yet only limited efforts to carve cumulation areas within the Americas. The Dominican Republic-Central America-United States Free Trade Agreement (CAFTA-DR) between the US, Central America, and the Dominican Republic contains provisions for cumulation of inputs from Canada and Mexico in the production of garments of woven fabric (HS Chapter 62).

various RTAs among its members through its Best Practices for PTAs.

Gradual, bottom-up multilateralization will be likelier than top-down WTO-mandated multilateralization. Indeed, in some disciplines, multilateralization may be occurring by default—for example, RTA provisions on competition policy tend to be multilateralized through non-discrimination clauses. Similar de facto multilateralization may be occurring in services, as RTAs' RoO for services trade are generally quite loose. In most cases, third-country service providers can free-ride on the preferences provided by an RTA by establishing an investment presence in one of the partner countries.²⁶ More generally, while there is marked variation across RTAs in terms of their coverage and content of the various disciplines, there are also important RTA clusters of main world regions and traders, such as the US and the EU. There is also clear “borrowing” of RTA models from one region to another. For example, the Chile-Korea FTA's market access provisions are a striking copy of the disciplines in the US-Chile FTA—which in turn is modeled quite extensively on the NAFTA.

However, for WTO Members to promptly multilateralize RTA disciplines in the multilateral system would require a return to plurilateral agreements, which were a permitted modality in global trade talks before the consensus and single undertaking rules were adopted. In a plurilateral agreement, only a coalition of the willing would accede to an agreement, receiving all the rights and accepting all the obligations. The benefit of plurilateralism over multilateralism is speed, as those who do not want to accede are left out and do not constrain the talks. Moreover, since Members self-select into agreements, compliance will be easier. Further, it is far from certain that plurilaterals would be narrow-based. The incentives are substantial—accession to any one deal, while requiring policy adjustments, would also mean more hospitable practices by as many as 153 trading partners abroad.

POLICY RECOMMENDATIONS

RTAs have transformed global commerce, and mostly for the better. There is by now an important body of literature that attests to the value added of RTAs to the global trading system. At their best, trade agreements can serve as engines of liberalization; focal points of inter-state cooperation; incubators of new global trade rules; and testing grounds for mechanisms to adjust to an open trading environment. They enable countries to craft provisions to suit their idiosyncratic circumstances; help aggregate national and global pro-trade forces to lobby for further liberalization; and can deepen trade disciplines. It may also be the case that a critical mass of trade agreements can create the dynamics conducive to global trade liberalization, perhaps well beyond what could be accomplished through multilateral negotiations alone.

There have been several proposals and attempts to ensure that RTAs are non-discriminatory, including strengthening the WTO's legal framework applicable to RTAs and accelerating unilateral and multilateral trade opening. There have also been ideas to address, both at the regional and multilateral levels, potential transactions costs and inefficiencies entailed by RTAs. These include a norms-based, “soft law” approach to regulating RTAs; converging RTAs into broader integration zones; and multilateralizing RTA disciplines, such as can be done by transposing their “WTO+” features to the GATT and WTO agreements (Davey 2011; Low 2010; Sutherland Report 2005; Warwick Commission Report 2007; WTO 2003).

The key policy question addressed in each of these areas is whether and how the WTO system and RTAs can be and be made most synergistic and help deepen and improve each other. The focus is shifting in the right direction, away from a narrow focus on RTAs' coverage and trade effects and futile, top-down efforts to standardize or harmonize RTAs. These approaches will now need to be deepened, with the end consumer in mind—companies engaged in global commerce. Three approaches should in particular be considered.

RTA Exchange to Share Best Regional Practices

The WTO is uniquely placed to act as a dedicated clearing house and forum where all matters related to RTAs, their rules, and their practices can be discussed among all WTO Members. This type of an “RTA Exchange” could feature an annual forum where the Members regularly share practices and challenges from building RTAs, as well as an informative and interactive website on RTAs, their rules, the various research findings on them, the practical experiences in negotiating and implementing them, and the various ways in which regional governments have sought to complement them through further regional cooperation. For example, many nations could learn from the efforts made in the NAFTA to harmonize standards after regional tariff liberalization was complete. Asian and Latin American nations have much to learn from the experiences and failures of the EU nations in deepening their regional arrangement. To prevent the RTA Exchange from being diluted to long-winded political statements, both the annual forum and the website should include independent outside analysts.

This type of forum would raise the level of debate on RTAs, systematize it, and make it more applied than earlier policy discussions on RTAs. It would automatically enhance RTAs' transparency, and it could help bring together analytical work that is already being generated around the world. The Exchange should be complemented by an interactive

26 See, for example, Fink and Jansen 2007. Baldwin et al. 2007 cite the NAFTA-style telecommunications provision as an agent of multilateralization due to the sheer number of countries adhering to it, and because harmonization to a single regulatory regime for telecommunications frees trade in the same way that adoption of an international standard liberalizes technical barriers to trade—a common set of rules that governments apply to private firms in many nations tends to foster competition and trade.

website filled with data, information, and fresh ideas for policymakers, companies, and analysts.

New Negotiation Modality for Multilateralizing Regionalism

Unlike the 1940s, multilateral trade talks now tackle multiple issues among a record 154 Members. For multilateralization of RTA regulations to occur effortlessly, changes would be required in the WTO's negotiation modalities—a shift from the unanimity rule and single undertaking principle to enable faster deals among a critical mass of members. Such a critical mass can, for the sake of simplicity, be defined as coalitions of the willing; though such a coalition would need to encompass at least some of the large trading nations to have a meaningful impact. The multilateralization process could start out much as the ITA did, as a plurilateral agreement, whereby a subset of WTO Members commit to a set of rules that is binding among them and can be enforced in the WTO dispute settlement system. The Members left outside would not access the benefits or need to adhere by the obligations until acceding to the agreement. The process is fully voluntary, but discussion on multilateralization can be encouraged, both through the RTA Exchange and in specific, topical forums, such as on e-commerce or competition policy.

Trade Facilitation with Rule Convergence

Convergence of RTA provisions such as complex RoO can be desirable, but they cannot be forced. For convergence to occur and be meaningful, a larger actor, such as the US or the EU, would need to press for it with its several FTA partners. None of the larger players has much to lose from seeking convergence (apart from resistance from protectionist interests against any further trade concessions), and could have something to gain. However, since these "hub" nations also have relatively similar rules with all their various FTA partners, it is the "spoke" nations that would likely gain most from harmonized trade rules, as showcased by the Paneuro system.

However, it is not always clear that the perceived benefits of convergence would so significantly outweigh the costs that various nations would be prepared to seek it. There are attempts in the Americas and APEC region that speak to the difficulties of such an enterprise. And convergence of rules is not everything. Indeed, assessing how and whether to somehow converge or multilateralize RTAs should avoid leading to "RTA myopia"—excessive focus on RTA rules, when there are several other ways in which members could expand their trade and trade with outside parties. For example, trade facilitation, customs modernization, and improvements in infrastructures are also likely to generate trade gains, and potentially larger than those from convergence, and they would benefit all countries, not just RTA members. Such further measures are highly complementary and synergistic to efforts to converge or multilateralize RTA, and should be prioritized. They are also

politically easier to accomplish than renegotiating existing agreements or negotiating new ones.

The RTA Exchange should be complemented by a dedicated forum that includes independent analysts, leaders of global companies, trade and economic development officials of the various member nations, and multilateral development bank officials to define measures complementary to RTAs that provide the greatest "bang for the buck." The forum's discussions should include sophisticated, technical analyses on the benefits and costs of various plausible complementary measures that facilitate and expand trade with partners in different regions.

CONCLUSION

The WTO is at a defining moment. It faces questions about its legitimacy and effectiveness, and is surrounded by increasingly vibrant system of RTAs. RTAs have long been seen as competing with and undermining the world trading system when they should be viewed as buttressing the multilateral trading system, which is struggling to adjust to an increasingly complex global economy and constituency. RTAs have deepened trade relationships, increased trade, and created the grounds for broader cooperation conducive to trade among their members, well beyond what can be accomplished at the multilateral level alone.

Yet RTAs are not enough—multilateralism is also critical, and global, system manager institutions plays a central role in ensuring non-discrimination and settling disputes. Even as RTAs advance the cause of open markets and provide insurance against the breakdown of multilateral talks, they are not a substitute for multilateral liberalization. The two fronts must move in parallel. The WTO is uniquely placed to provide a venue for its Members to discuss best practices in RTAs and ways to build on the RTA ecosystem for greater efficiencies in global trade.

BOX 1:

GATT Article XXIV: Territorial Application — Frontier Traffic — Customs Unions and Free-trade Areas

1 The provisions of this Agreement shall apply to the metropolitan customs territories of the contracting parties and to any other customs territories in respect of which this Agreement has been accepted under Article XXVI or is being applied under Article XXXIII or pursuant to the Protocol of Provisional Application. Each such customs territory shall, exclusively for the purposes of the territorial application of this Agreement, be treated as though it were a contracting party; Provided that the provisions of this paragraph shall not be construed to create any rights or obligations as between two or more customs territories in respect of which this Agreement has been accepted under Article XXVI or is being applied under Article XXXIII or pursuant to the Protocol of Provisional Application by a single contracting party.

2. For the purposes of this Agreement a customs territory shall be understood to mean any territory with respect to which separate tariffs or other regulations of commerce are maintained for a substantial part of the trade of such territory with other territories.

3. The provisions of this Agreement shall not be construed to prevent:

- (a) Advantages accorded by any contracting party to adjacent countries in order to facilitate frontier traffic;
- (b) Advantages accorded to the trade with the Free Territory of Trieste by countries contiguous to that territory, provided that such advantages are not in conflict with the Treaties of Peace arising out of the Second World War.

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

5. Accordingly, the provisions of this Agreement shall not prevent, as between the territories of contracting parties, the formation of a customs union or of a free-trade area or the adoption of an interim agreement necessary for the formation of a customs union or of a free-trade area; Provided that:

(a) with respect to a customs union, or an interim agreement leading to a formation of a customs union, the duties and other regulations of commerce imposed at the institution of any such union or interim agreement in respect of trade with contracting parties not parties to such union or agreement shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union or the adoption of such interim agreement, as the case may be;

(b) with respect to a free-trade area, or an interim agreement leading to the formation of a free-trade area, the duties and other regulations of commerce maintained in each of the constituent territories and applicable at the formation of such free-trade area or the adoption of such interim agreement to the trade of contracting parties not included in such area or not parties to such agreement shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the same constituent territories prior to the formation of the free-trade area, or interim agreement as the case may be; and

(c) any interim agreement referred to in subparagraphs (a) and (b) shall include a plan and schedule for the formation of such a customs union or of such a free-trade area within a reasonable length of time.

6. If, in fulfilling the requirements of subparagraph 5 (a), a contracting party proposes to increase any rate of duty inconsistently with the provisions of Article II, the procedure set forth in Article XXVIII shall apply. In providing for compensatory adjustment, due account shall be taken of the compensation already afforded by the reduction brought about in the corresponding duty of the other constituents of the union.

7. (a) Any contracting party deciding to enter into a customs union or free-trade area, or an interim agreement leading to the formation of such a union or area, shall promptly notify the CONTRACTING PARTIES and shall make available to them such information regarding the proposed union or area as will enable them to make such reports and recommendations to contracting parties as they may deem appropriate.

BOX 1 (CONTINUED):

GATT Article XXIV: Territorial Application — Frontier Traffic — Customs Unions and Free-trade Areas

(b) If, after having studied the plan and schedule included in an interim agreement referred to in paragraph 5 in consultation with the parties to that agreement and taking due account of the information made available in accordance with the provisions of subparagraph (a), the CONTRACTING PARTIES find that such agreement is not likely to result in the formation of a customs union or of a free-trade area within the period contemplated by the parties to the agreement or that such period is not a reasonable one, the CONTRACTING PARTIES shall make recommendations to the parties to the agreement. The parties shall not maintain or put into force, as the case may be, such agreement if they are not prepared to modify it in accordance with these recommendations.

(c) Any substantial change in the plan or schedule referred to in paragraph 5 (c) shall be communicated to the CONTRACTING PARTIES, which may request the contracting parties concerned to consult with them if the change seems likely to jeopardize or delay unduly the formation of the customs union or of the free-trade area.

8. For the purposes of this Agreement:

(a) A customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that

(i) duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and,

(ii) subject to the provisions of paragraph 9, substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union;

(b) A free-trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.

9. The preferences referred to in paragraph 2 of Article I shall not be affected by the formation of a customs union or of a free-trade area but may be eliminated or adjusted by means of negotiations with contracting parties affected. This procedure of negotiations with affected contracting parties shall, in particular, apply to the elimination of preferences required to conform with the provisions of paragraph 8 (a)(i) and paragraph 8 (b).

10. The CONTRACTING PARTIES may by a two-thirds majority approve proposals which do not fully comply with the requirements of paragraphs 5 to 9 inclusive, provided that such proposals lead to the formation of a customs union or a free-trade area in the sense of this Article.

11. Taking into account the exceptional circumstances arising out of the establishment of India and Pakistan as independent States and recognizing the fact that they have long constituted an economic unit, the contracting parties agree that the provisions of this Agreement shall not prevent the two countries from entering into special arrangements with respect to the trade between them, pending the establishment of their mutual trade relations on a definitive basis.

12. Each contracting party shall take such reasonable measures as may be available to it to ensure observance of the provisions of this Agreement by the regional and local governments and authorities within its territories.

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RTA EXCHANGE: ORGANIZING THE WORLD'S INFORMATION ON REGIONAL TRADE AGREEMENTS

Kati Suominen

INTRODUCTION

Regional trade agreements (RTAs) have proliferated around the world in the past two decades alongside and independent from the General Agreement on Tariffs and Trade (GATT)/World Trade Organization (WTO) system. By now, two parallel systems, multilateral and regional, are in place. The rise of RTAs has created a sense of urgency among WTO members to examine whether they are discriminatory toward outsiders, and also how exactly the various GATT regulations on preferential treatment should be interpreted, and whether their scope should be broadened. Such concerns have grown as each WTO Member has found itself an outsider to an ever-growing number of RTAs. In the Doha Round, WTO Members elevated RTAs to a “systemic issue,” or one that affects the entire world trading system and requires to be addressed as such.

In practice, multilateral efforts to regulate RTAs have been and will be toothless. After all, all WTO Members are jealous of their respective RTAs, and are unlikely to call for rules that could force them to modify their own agreements. Besides, RTAs are not the problem they have been worried with. Research shows that most RTAs adhere to open regionalism—they create, not divert, trade with outsiders—and also help aggregate pro-trade forces to lobby for further liberalization. RTAs have in many ways been saviours of the global trading system, opening paths to trade liberalization for WTO Members even as the Doha Round has stagnated. RTAs have numerous further benefits—they are found to serve as focal points of interstate cooperation; incubators of new global trade rules; and as testing grounds for mechanisms to adjust to an open trading environment.

It is not possible, practical, or desirable to seek to regulate or standardize RTAs. Rather than worrying about the

potential discriminatory effect of RTAs, WTO Members need a new approach, one that aims to mitigate the real challenge posed by RTAs, and harnesses the many opportunities created by them to deepen and broaden global economic integration for expanded trade and development. Such an approach would consist of the following high-impact measures.

- **Creating efficiency gains across RTAs:** The “spaghetti bowl” of RTAs has been shown to raise transactions costs for companies that operate global supply chains, as well as smaller exporters seeking to export to many different markets, each with its own RTA. Erasing some of the transactions costs through converging RTAs into larger integration zones can yield major economic gains, particularly for smaller economies.
- **Multilateralization of RTAs' best practices:** Recent RTAs, in particular, have addressed behind-the-border issues from intellectual property to competition policy and product norms in a very robust fashion. This is where the innovation in RTAs is occurring, and also where the multilateral trading system lags well behind. RTAs offer a vast body of tested and tried rules that can help advance multilateral rulemaking in critical areas.
- **Deepening trade integration created by RTAs:** RTAs help generate goodwill and greater economic interaction among their members that can be conducive to deeper integration in other policy areas, such as standards harmonization or infrastructure development. There have been several efforts around the world that offer lessons for countries and regions that have yet to fully exploit the opportunities opened by RTAs.

There are several possible ways to reduce spaghetti bowl problems and take full advantage of RTAs for global trade and development. But how do we best realize them?

One key answer revolves around improved information and exchange of ideas on RTAs. The existing data, information, and discussion on RTAs is voluminous, but also ad hoc, uncoordinated, and dispersed across a variety of forums around the world. There is no one instance that would encourage broad-based global “mindshare” on RTAs, with a view to sharing experiences and building synergies among RTAs and between them and the WTO system. This is a lost opportunity.

This is also an opportunity for a consortium of like-minded institutions committed to advancing global trade integration to step up to the plate. Such as consortium—composed of development banks, other international organizations, and leading academic institutions—could establish and run an “RTA Exchange,” a first-in-class global clearing house of information on RTAs, and a virtual international discussion forum on ways to leverage RTAs for broader and deeper global trade integration. With a bottom-up approach that engages multiple different

stakeholders engaged in world trade, the RTA Exchange would enhance transparency, and facilitate the transfer of lessons learned and best practices across RTAs. This would lay the groundwork for multilateralizing RTAs' best practices, and generate fresh thinking on ways to complement RTAs for trade and development. It would doubtless also unearth policy innovations that have yet to see the light of day.

Is there a role for the WTO in the RTA Exchange? The WTO should have an interest in forming the exchange for two reasons. First, becoming a hub of information and ideas on RTAs, which are today's center of gravity of global trade integration and rule-making, the WTO would regain relevance rather than being sidelined. Second, geared to facilitating and encouraging information sharing and open dialogue on the ways in which RTAs can best be leveraged for global trade and development, the WTO will serve its mission to "open trade for the benefit of all," and likely get far more done than is possible through clogged multilateral trade negotiations. However, politicization of RTAs within the WTO system precludes the institution from running the RTA Exchange alone. The WTO can offer, as well as use, some of the elements of the Exchange—it can be an observer to the founding consortium.

PROBLEM

The rich debate over the past several years about the implications of RTAs to the world trading system has mostly centered around their discriminatory effects toward outsiders. The conventional analysis has reflected concerns that RTAs could be trade-diverting and antithetical to the multilateral trading system. The 1948 GATT allows member countries to grant each other preferential treatment under free trade areas or customs unions, as long as certain conditions are met. These conditions are defined mainly in GATT Article XXIV, which stipulates that members notify their RTAs to what is now the WTO, and that the RTAs liberalize "substantially all trade" among their members "in reasonable length of time" and not introduce new "restrictive rules on commerce." The Article also demands open regionalism—that RTA members do not raise barriers to third parties.

Since the early 1980s, there have been a number of efforts at the GATT/WTO system to somehow regulate RTAs to counteract the odds of trade diversion. The quest for transparency intensified in the wake of the Uruguay Round. In 1996, the WTO General Council established the Committee on Regional Trade Agreements (CRTA) as a means to examine individual RTAs and to consider their systemic, cross-cutting implications for the multilateral trading system. Parties to a new RTA are required to submit certain data to the WTO, such as on the RTA's tariff concessions and rules of origin, and the members' most favoured nation (MFN) duties and import statistics. The CRTA is subsequently to prepare a detailed survey of the contents of the RTAs, and to perform

legal analyses of WTO provisions pertinent to RTAs, draw comparisons across RTAs, and examine the economic aspects of RTAs.

In the Doha Round, WTO Members elevated RTAs to a "systemic issue," or one that affects the entire world trading system and requires to be addressed as such. In December 2006, the Members issued a "Transparency Mechanism for Regional Trade Agreements" that requires the Members to provide an "early announcement" of their involvement in RTA negotiations and promptly notify a newly concluded RTA, and that puts forth a schedule for the RTA's examination by the WTO Secretariat.

These approaches have in part been premised on the notion that RTAs may have discriminatory effects, or even that there could be trade-offs between the multilateral and regional system of trade governance, which make it incumbent on the WTO to monitor and somehow regulate RTAs. These approaches have also been rather narrowly focused, like Article XXIV mostly is, on market access provisions in RTAs. While useful for shedding light on RTAs, these approaches also promise limited benefits for three reasons.

- **Lack of political will:** Efforts to monitor and regulate RTAs have proven ineffective. WTO Members have practically never debated hard or agreed whether any one RTA breaches multilateral trade rules, let alone revised Article XXIV—multilateral, top-down efforts to address RTAs have gone practically nowhere. The reason is simple—WTO members are jealous of their respective RTAs and their prerogatives to form new ones, and unlikely to agree to any multilateral rules that would curb their ability to negotiate RTAs or force them to modify their existing agreements. Illustrative, the dispute settlement body has dealt with RTAs in only a handful of occasions.
- **Secretariat's resource constraints:** The resources for the WTO Secretariat to perform in-depth analyses on RTAs are limited; in addition, political sensitivities have curbed the ambition of these studies.
- **Addressing the wrong "problem":** Longstanding concerns that RTAs balkanize the global trading system are becoming moot—research indicates that most RTAs are more trade-creating than trade-diverting. Moreover, while RTAs have been blamed for sapping energy from the multilateral trading system, it is also the case that RTAs have helped save the global trading system in its time of crisis. They have fuelled the liberalizing momentum as multilateral talks have frozen, and when some protectionist practices emerged during the 2008–09 global financial crisis. In addition, RTAs have created a positive internal dynamic—the very proliferation of RTAs has reduced the preferential edge that any one RTA confers.

Besides advancing global trade liberalization, RTAs have emerged as incubators of new trade and trade-related rules

in such areas as services trade, investment regulations, customs procedures and trade facilitation, environment, intellectual property rights, and e-commerce. In some of these areas, RTAs are unquestionably more advanced and sophisticated than the multilateral trading system. RTAs have also been found to impart benefits that go well beyond traditional analyses on gains from trade, such as propelling export-oriented, efficiency-seeking investment flows among members; encouraging cooperation among members on customs and infrastructure integration; and helping relax the political economy constraints to multilateral trade talks in member nations.

In short, the WTO has scant power over RTAs, and WTO Members are unlikely to demand that existing RTAs be modified. Top-down efforts to monitor and constrain RTAs have proven futile. They are also misguided—research shows that RTAs have in the main had positive effects on the world trading system, and also adhered to the common interpretations of Article XXIV. It is thus neither practical nor desirable to standardize RTAs or devise new, elaborate rules to regulate RTAs. Why seek to fix what works?

Today's policy question should not be whether RTAs undermine the global trading system, but how RTAs and their many WTO+ features can be leveraged to deepen and broaden global trade integration. Positively, international debate is shifting in the right direction, away from a narrow focus on RTAs' coverage and trade effects and to measures to forge efficiencies and synergies across the many RTAs. There are efforts to converge multiple RTAs into broader integration zones (for example, the Pacific Alliance in Latin America); form mega-regional agreements encompassing several large trading nations (for example, the Trans-Pacific Partnership, or TPP); and start negotiating plurilateral agreements on key trade disciplines among members of several different RTAs (for example, the International Services Agreement negotiations).

These types of approaches will now need to be deepened. A key step in this direction is an enhanced understanding of the contents, dynamics, and lessons learned from various RTAs. Indeed, although the RTA spree of the past two decades has created a vast reservoir of agreements, rules, and practical experiences, it is also the case that data, information, and discussion on RTAs remains ad hoc, uncoordinated, and dispersed across a variety of forums around the world, whether university centers, multilateral development banks, or regional organizations.

Granted, policy entrepreneurs and intrepid analysts may bring some of this dispersed data and collective wisdom together, but such efforts, unless large scale and sustained, are of limited impact. There is no one instance that would systematically and on a consistent basis bring together all relevant information on RTAs around the world, let alone encourage dialogue and sharing of experiences among the various stakeholders in global trade on RTAs. There decidedly is no one instance that would encourage global "mindshare" on RTAs with a view to building synergies among RTAs and

between RTAs and the WTO system, and in general helping unearth fresh ideas and lessons learned on best ways to broaden and deepen trade integration on the back of existing RTAs.

A failure to tap the wealth of information and experience on negotiating, implementing, and complementing RTAs is a giant lost opportunity. This is also a gap that needs to be bridged. A new institution is needed—an RTA Exchange.

LAUNCHING THE RTA EXCHANGE

The RTA Exchange is to be a cutting-edge forum where all matters related to RTAs and their rules and practices could be shared and discussed in an open environment. Its founders have an opportunity to make the RTA Exchange the leading venue of actionable data, insight, idea generation, and information sharing on RTAs.

A clearing house of information and a genuinely global discussion forum, the RTA Exchange would promote debate and generate ideas bottom-up among trade and economic policymakers, private sector representatives, multilateral development bank officials, and analysts around the world. Bringing diverse stakeholders together into a free-ranging, apolitical forum, the consortium would leverage the substantial global "wisdom of crowds" on RTAs, thereby curating actionable intelligence from those closest to the problems and opportunities in the global trading system. Hosting a broad-based forum, the consortium would also reach a large set of players, maximizing the informational benefits of the RTA Exchange.

Modes of engagement: The RTA Exchange would be "lean and mean"—run by one or two professionals and two or three support staff. It would have five distinct ways to engage with the various stakeholders.

- **Clearing house of information:** A highly interactive website with a comprehensive, existing, ever-growing body of information, data, and analysis on RTAs, curated from sources around the world.
- **Forum for engagement among stakeholders:** Regularly updated site with videos, blogs, and announcements, as well as other easy-to-digest, real-time ideas and analyses on RTAs. The RTA Exchange staff would also actively create and curate such pieces, engaging experts, and having an "open door policy" for potential contributors. Among other things, one can imagine a Wikipedia on RTAs developing as a result.
- **Discussion space:** A Facebook-like, user-driven application linking the various stakeholders, with discussions lightly moderated by the Exchange management team.

- **Webinars for education:** Frequent e-learning, such as online seminars engaging diverse speakers and experts on various aspects related to RTAs. Registered members can suggest topics for such seminars.
- **Annual conference.** An annual international meeting on RTAs.

Contents: The contents of these various windows for engagement could be organized into five main areas, each with its specific purpose.

- **Gaining fresh information, data, and analytics on RTAs:** A cornerstone of the RTA Exchange should be an interactive and easily searchable repository of RTA agreements; descriptive comparisons of RTAs and RTA disciplines; and the countless web-based technical studies, forums, news articles, and videos on RTAs that have been published over the past several years. Updated on a daily basis, this repository would also bring together the websites and resources of the great many organizations that house data and information on RTAs, such as universities, the World Bank, regional development banks, and various regional organizations. It would also include the WTO's Database on Preferential Trade Arrangements, and could build on the WTO's new interactive market access database, incorporating data on preferential tariff liberalization schedules and preferential margins.
- **Negotiating and implementing RTAs:** The RTA Exchange should include information, blogs, and interviews with public and private sector actors and analysts on lessons learned and practical experiences in negotiating and implementing RTAs. Such issues as the design of rules of origin regimes, best practices in including the private sector in RTA negotiations/implementation, and trade enforcement are perennial concerns for trade negotiators and implementers of RTAs. Among other things, the RTA Exchange can include web-based seminars and interviews with seasoned negotiators and analysts on best practices in designing and implementing RTAs.
- **Deepening regional integration:** Many RTA partners have leveraged the goodwill and greater economic interaction resulting from trade liberalization to deepen bilateral or regional integration in other policy areas. Such experiences need to be shared. For example, many countries in Africa and Asia could learn from the efforts made in the North American Free Trade Agreement (NAFTA) context to harmonize standards among the parties after tariff liberalization was complete. Similarly, Asians and Latin Americans should have much to learn from the experiences and challenges of the European Union (EU) nations in deepening their regional integration.
- **Converging and multilateralizing RTAs:** Converging RTAs and multilateralizing RTAs could have significant efficiency gains, facilitate trade, and promote the creation of scale economies among across different RTAs. This

could overcome the potential problems of hub-and-spoke formations that tend to disadvantage smaller countries and balkanize the global trading system. It would also bring the world ever closer to the full-fledged trade integration that multilateral negotiators have aspired to deliver. Indeed, perhaps the main objective of the RTA Exchange would be to actively inform and promote dialogue on experiences and strategic ideas on ways in which WTO Members can build synergies across RTAs and between RTAs and the WTO system.

For example, African and Asian nations could have much to learn from the Pacific Alliance convergence effort in Latin America and from the creation of the Paneuro system of cumulation in Europe in 1999. Similarly, outsiders to the TPP and the Transatlantic Trade and Investment Partnership (TTIP) could gain analytics and knowledge via the Exchange on the benefits of joining these mega-regionals. The RTA Exchange team can take the lead in curating ideas and inputs from around the world on these major strategic issues, as well as enable a user-driven discussion on best practice elements in RTAs.

- **Developing complementary policies.** Efforts to enhance efficiencies in the global trading system, such as converging RTAs, risks "RTA myopia"—excessive focus on RTA rules, when there are several other ways in which RTA members could expand their trade and trade with outside parties. For example, trade facilitation, customs modernization, and improvements in infrastructures are likely to produce gains that are at least as significant as rule convergence could be. Such complementary policies should be prioritized. They are consistent with the Doha Round's development agenda and the Aid for Trade agenda, and politically easier to accomplish than renegotiating existing agreements or negotiating new ones. The RTA Exchange should bring together the various stakeholders to define complementary policies that provide the greatest "bang for the buck." Upon demand, the consortium and outside analysts could also prepare technical analyses on the costs and benefits of various plausible complementary policies.

Benefits of the RTA Exchange

The RTA Exchange would be the world's leading venue on issues related to RTAs. It would raise the level of debate on RTAs, systematize it, and help make it more actionable than is possible through academic exercises. It would automatically enhance RTAs' transparency, and help harness the global wisdom of crowds on best ways to leverage RTAs for global trade integration and development. For emerging and developing nations with limited capacities to gather and analyze information on RTAs and their related best practices, the RTA Exchange would offer a shortcut and putting them in touch with relevant information and analysis on RTAs, and providing ready access to peers and experts in other regions as well as in leading global institutions and academic centers.

Granted, for the RTA Exchange to impact WTO negotiations and rule making, its work would ideally have to be woven into the fabric of the WTO's work. For example, existing WTO Committees and Councils should have responsibility for taking up and reviewing RTA elements within the purview of their committee (that is, the TBT committee would look at TBT-related matters), and the consortium members of the RTA Exchange should provide all technical input and the latest ideas related to RTAs for this.

CONCLUSION

The WTO is at a defining moment. It faces questions about its legitimacy and effectiveness, is struggling to adjust to an increasingly complex global economy and constituency, and is surrounded by an increasingly vibrant system of RTAs, which had long been thought of as detrimental to the world trading system. There have been several proposals and attempts to ensure that RTAs are non-discriminatory, including strengthening the WTO's legal framework applicable to them, and to shed light on RTA disciplines and depth of liberalization.

PLURILATERALS AND THE MULTILATERAL TRADING SYSTEM

Peter Draper and Memory Dube

INTRODUCTION

The multilateral trading system was shaped by plurilateral agreements. Historically, a number of plurilateral codes evolved in parallel with the tariff agreements negotiated under the General Agreement on Tariffs and Trade (GATT), with nine being concluded in the Tokyo Round (Kennedy 2012). These were folded into the Uruguay Round under the single undertaking, whereby nothing is agreed until everything is agreed. That process took place under unique historical conditions, notably the end of the Cold War and the consequent peaking of the power and influence of the United States (US) in the multilateral trading system, thus enabling a unique deal tailored to American designs. Consequently it is the Uruguay Round that can be considered *sui generis*, rather than the current potential reversion to plurilateral codes.

Given the size of the World Trade Organization's (WTO) membership and the diversity of interests in play, it is possible that the single undertaking has run its course. The ongoing Doha Round impasse means that key WTO rules are not being updated, while trade liberalization has moved to other forums, principally regional. While preferential trade agreements (PTAs) are compatible with the WTO (WTO 2011a), increasing recourse to them in the context of stagnation in the multilateral rule-making mechanism constitutes a growing existential crisis for the WTO. Therefore, proponents of plurilaterals argue that those countries with core interests in updating the rules and in pursuing liberalization under the aegis of the WTO should be allowed to proceed, provided the correct conditions pertain. Opponents, principally developing countries, worry that their interests will be neglected as the major trading powers steam ahead without them, in the worst case potentially "imposing" plurilateral outcomes on them at some future date, but at the least forging new standards that developing countries will find difficult to implement, which could lead to loss of market access. This fear stems primarily from the multilateralization of some Tokyo Round codes under the single undertaking approach adopted for the Uruguay Round. Nonetheless, WTO members have agreed to explore new approaches to advancing negotiations under the aegis of the

multilateral trading system (WTO 2011b). Plurilaterals, in principle, offer one option. This could introduce complexities and risks, but retaining the centrality of the multilateral trading system, even if its integrity may be called into question, could outweigh such potential costs. Accordingly, this brief constitutes a high-level consideration of the "cost-benefit" equation involved in pursuing plurilateral approaches, with brief application to key subjects on the Doha Round agenda.

CHALLENGE AND OPPORTUNITY: CAN PLURILATERALS REVIVE THE MULTILATERAL TRADING SYSTEM?

The short answer to this question is "yes, but..." The "yes" part of the answer pertains to the fact that plurilaterals could, in principle, be used to pioneer new rules or market openings in an otherwise clogged system, thus keeping the WTO at the centre of the global trading system. Since the WTO is a global public good, the benefits of which are widely acknowledged and evidenced in particular through Member state recourse to its dispute settlement mechanism, it is clear that progress beyond the Doha impasse would be substantially beneficial. For this reason, many countries, mostly developed, support the adoption of new approaches to concluding the Doha Round, through plurilateral negotiations in particular. There is precedent for this, since plurilateral agreements were resorted to in order to break the impasse in the Tokyo Round negotiations, resulting in the aforementioned "codes" system (Saner 2012).

The single undertaking principle does not legally prevent the addition or adoption of new agreements to the WTO, be they multilateral or plurilateral, even if a multilateral trade negotiation round has failed. Rather, it is a negotiating device adopted by choice, and can be done away with (Kennedy 2012). For instance, even though the single undertaking was adopted for the Doha Round, paragraph 47 of the Doha Ministerial Declaration provides that "...the conduct, conclusion and entry into force of the outcome of the negotiations shall be treated as parts of a single undertaking. *However, agreements reached at an early stage may be implemented on a provisional or definitive basis*" (authors' emphasis).

An important question is whether paragraph 47 obviates the need to obtain consensus, thereby allowing members to proceed with negotiation of plurilaterals, or if the paragraph allows for negotiation of plurilaterals but consensus is still required for the provision to become actionable. The challenge in carving out a package for the least developed countries (LDCs) from the Doha Round would suggest that such unbundling still requires, *de facto* if not *de jure*, consent from all members. Similarly, the Hong Kong Ministerial Declaration, with specific reference to the services negotiations in Annex C, provides for a request-offer

approach to be pursued on a plurilateral basis to facilitate the participation of all Members, focusing particularly on developing countries whose negotiation capacity is limited. However, progress has been painfully slow, not least because the services negotiations are formally and politically linked to progress in other negotiating areas, principally agriculture and Non-Agricultural Market Access (NAMA).

Yet the absence of the single undertaking could fundamentally alter the balance of issues and interests under negotiation. Plurilaterals could conceivably revolve around the export interests of the major trading powers. Once those interests are satisfied, they would effectively be removed from the equation of broader, cross-issue trade-offs. This could make it difficult, if not impossible, to launch major trade rounds in the future. In addition, it could leave untouched the key sectors that still enjoy substantial protection in the major trading powers, notably agriculture and labour-intensive manufacturing, such as clothing. Therefore, developing countries especially could find that their export interests are substantially hit, and they have no recourse beyond asymmetrical PTAs. In such a scenario, while the multilateral trading system could have advanced, potentially innovating new rules too, it could end up being more skewed towards the interests of the major trading powers. And those countries that do not have much influence in the multilateral trading system, especially LDCs, could find that new standards and market access conditions are forged without taking their interests into account, for example, development concerns in the Doha Round (IDEAS Centre 2013). There is also apprehension about the negotiation of non-Doha issues and the impact of this on the multilateral trading system. That raises the question of whether these plurilaterals should be limited to negotiating the issues currently under deadlock in the Doha Round, or if the negotiation of plurilaterals should henceforth be the default position for progress in rulemaking in the WTO. The latter approach would make developing countries more nervous as they could see it as the erosion of the multilateral system. For these reasons and more, many developing countries, including some large trading powers such as BRICS (Brazil, Russia, India, China, and South Africa), in principle, seem to be opposed to plurilaterals.

In the end, developing countries may not have much choice. The emergence of "mega-regionals" raises the possibility that developing countries will be excluded from market share in the signatory regions.¹ Also, since these mega-regionals are being negotiated outside the scope of the multilateral trading system, developing countries are prevented from negotiating the rules that may set standards for the trading system as a whole. In this light, plurilaterals have more scope to strengthen the multilateral trading system than PTAs, especially mega-regionals. Plurilaterals also offer "insurance" to countries seeking to advance their trade interests through PTAs, particularly through mega-regionals. Since those processes are large, complex, politically sensitive, and therefore vulnerable to failure, Member states negotiating them are likely to want to keep open their options for

advancing trade rules through the WTO. As the Doha Round has failed, plurilaterals could constitute that insurance.

There is an implicit understanding regarding the uniquely vulnerable position of LDCs in the global trading system, and the consequent need to shield them from reciprocal commitments. It can, therefore, be reasonably expected that any plurilateral concluded would have special provisions for LDCs that confer rights and exempt them from any commitments. This is discussed further below within the context of creating a code of conduct for the negotiation of plurilaterals.

So while the window for exploring new approaches—particularly plurilaterals—to concluding the Doha Round has opened a crack, many obstacles remain. At the heart of this impasse is distrust and mismatched ambitions. Therefore, it is important to shed light on what exactly plurilaterals could entail legally, their limitations, and how the trust deficit could be sensitively and constructively handled.

RESPONSES

First, it is critical to understand what exactly plurilaterals are and how they relate to existing WTO rules. This frames the political economy possibilities and constraints, and provides context to a concrete proposal to negotiate, upfront, a code of conduct to govern subsequent negotiation of plurilaterals. Such a code could allay the worst fears and build sufficient consensus to proceed. The next issue then is which plurilaterals should be attempted, in what combinations and sequence. This is a challenging set of speculations since it encompasses many Member states with widely diverging interests, so it is briefly attempted in the penultimate section.

Towards a Taxonomy of Plurilaterals

Broadly speaking, plurilaterals can be characterized as either "inclusive" or "exclusive."

Inclusive plurilaterals essentially entail conditional, unilateral, sectoral liberalization. They are market access instruments, and almost certainly would not apply to rules. The key point is that liberalization arising under their rubric is conducted on a most favoured nation (MFN) basis, and is conditioned on other main trading powers also conducting such MFN liberalization. The only way around this would be to ensure that both countries that have an interest, and those that should ideally have an interest, are part of the "critical mass" necessary for the initiation of the plurilateral negotiation. In that sense, inclusive plurilaterals are challenging to achieve, but once agreed upon they obviate the need for consent by

¹ The ongoing Trans-Pacific Partnership Agreement (TPP), and the proposed Transatlantic Trade and Investment Partnership Agreement (TTIPA). At the centre of both is the US, incorporating the third largest economy in the world in the form of Japan in the case of the TPP; and the entire European Union (EU) in the case of the TTIPA.

all WTO Members via the Ministerial Conference; this consent would be required for exclusive plurilaterals. The foremost example of this approach is the Information Technology Agreement (ITA),² whereas sectorals under the NAMA negotiations could be considered potential candidates.

Since the ensuing liberalization is unilateral, it does not depend on WTO rules or broader negotiations per se. It could also be locked in through revisions to Member state tariff or services schedules as submitted to the WTO. This approach has the advantage of achieving liberalization breakthroughs where broader negotiations are stalled, such as under the Doha Round. However, it carries the longer-term danger that major exporting interests could be removed from the equation of subsequent, broader liberalization efforts.

As with inclusive plurilaterals, exclusive plurilaterals involve liberalization only for those Members participating and signing up to the subsequent agreement. The key difference is that the benefits of such liberalization are only available to parties to the agreement. Exclusive plurilaterals take several forms—goods PTAs, covered by GATT Article XXIV; services PTAs, covered by GATS Article V; and those residing under the Marrakesh Treaty, Annex 4. PTAs have their own sets of rules, and consequently are not considered here since Member states are free to pursue them. Our concern, therefore, is with agreements that fall under Annex 4, such as the Agreement on Government Procurement (GPA).

The GPA essentially opens up government procurement markets only to firms from signatory countries. This agreement, and two others covering bovine meat and dairy (both terminated in September 1997), do not apply on an MFN basis. The biggest legal hurdle to the adoption of any new Annex 4 plurilateral agreement is the consensus requirement. Article X:9 of the WTO agreement provides that “The Ministerial Conference, ... may decide exclusively by consensus to add that agreement to Annex 4.” For such consent to be granted, the interests of non-participating countries become an important consideration, particularly in the current political economy of the WTO, and could possibly influence the content of the agreements. The meaning of “consent” in this context is most probably that no Member objects. Any new agreements of this kind, therefore, would require the “consent” of all WTO Members through the Ministerial Conference or General Council—a tall order indeed. The multilateralization of any current Annex 4 agreements would also need to be adopted by the Ministerial Conference, as this would entail an amendment to the provisions of the WTO Agreement.³

With some developing countries such as Brazil, China, India, and South Africa having openly expressed their rejection of the idea of a plurilateral alternative to the Doha impasse, preferring instead a multilateral approach, it is likely that these countries would veto any attempt to adopt a new plurilateral agreement under Annex 4.⁴ This raises the probability of an impasse. The issue of exclusive plurilaterals should then possibly be considered alongside questions

of whether the consensus rule needs a review, otherwise the system could be held hostage through the exercise of effective veto power. Against this, the consensus rule works as a safeguard against a possible repeat of the Uruguay Round precedent regarding the incorporation of Tokyo Round plurilateral agreements into the single undertaking.

Some analysts point to the possible use of waivers from existing rules, as covered under the Marrakesh Treaty Article IX, as allowing for plurilateral outcomes. However, a waiver applies only to existing rules, and cannot be used to negotiate new rules. It could conceivably be granted for new market access arrangements, such as for generalized system of preferences market access for poor countries. But such arrangements would not constitute plurilateral arrangements per se. At best, a waiver could potentially be sought with regard to an inclusive plurilateral that does not fall within Annex 4, but only with the intention of exempting the application of the MFN obligation to non-participants to the negotiation. An example would be the ITA where the participants could theoretically seek a waiver from the MFN obligation, and thus only apply the benefits among themselves, even though the agreement is not an Annex 4 one. Furthermore, waivers are granted for limited periods only and can be withdrawn. Therefore, this avenue would be cumbersome at best, and most likely very partial relative to what proponents of plurilaterals are looking for.

Each plurilateral arrangement would specify its own dispute settlement arrangements with recourse to the WTO's dispute settlement mechanism (DSM) being an attractive option

2 The Information Technology Agreement (Ministerial Declaration on Trade in Information Technology Products) was signed at the Singapore Ministerial Conference in December 1996 by 29 countries, but because of its 90 percent trade coverage criteria, only came into effect in April 1997 when other countries signed up to it. The ITA is basically about tariff reduction in all products listed in the Declaration, and such tariff reduction is on an MFN basis. There is a provision in the agreement for the periodic review of product coverage, but despite the participants having been consulting on this since 1997, agreement has yet to be reached on additional product coverage and consultation continues (WTO), http://www.wto.org/english/tratop_e/inftec_e/itaintro_e.htm.

3 Article X: 1 of the WTO Agreement provides, in short, that a proposal to amend the provisions of the WTO agreement must be submitted to the Ministerial Council whose decision to submit such proposal to the WTO Members for acceptance shall be taken by consensus. For the proposal to be adopted, two-thirds of the Members must agree to it, and the amendment is effective for all members, but only if it does not modify Members' substantive rights and obligations. All Members whose rights such amendment infringes and who have not accepted the amendment may be asked, by a three-quarter majority of the Ministerial Conference, to withdraw from the WTO or, they may be allowed to remain Members upon consent by the Ministerial Conference. Hence, the Article X: 1 process is a very onerous one and, with the political activation of developing countries within the WTO, it is highly unlikely that any proposal to multilateralize Annex 4 agreements would ever see the light of day unless such developing countries were sufficiently reassured.

4 Note that China has been negotiating to accede to the GPA since it formally joined the WTO in 2001. But this process predates the Doha Round.

and a major motivation for negotiating plurilaterals. WTO dispute settlement can be built in two ways—for exclusive arrangements residing under Marrakesh Annex 4, the rules of the agreement could specify this; and for inclusive arrangements if the liberalization schedules are lodged with the WTO, then dispute settlement would apply. Appendix 1 of the Dispute Settlement Understanding (DSU) provides that application of the DSM to plurilateral trade agreements “shall be subject to the adoption of a decision by the parties to each agreement setting out the terms for the application of the Understanding to the individual agreement, including any special or additional rules or procedures.” In order to be able to apply the DSU procedures, the members of the plurilateral agreement would have to include, in the agreement, a provision for the application of the DSU, as well as adopt a decision that sets out the dispute settlement provisions of the agreement, and notify it to the Dispute Settlement Body (DSB). However, the decision to amend the list of covered agreements under Appendix 1 of the DSU has to be adopted through a consensus decision by the Ministerial Conference. Any special or additional rules and procedures regarding the adjudication of any matters related to the plurilateral agreements can vary on a case by case basis depending on the particular agreement.

Acceptance of Plurilaterals: Political Economy Considerations

Inclusive plurilaterals are clearly not as problematic as exclusive ones, since the full consent of the entire membership of the WTO is not required. Launching inclusive plurilaterals is where the real political economy lies, since they are subject to the free-rider problem. Therefore, the real challenge is in securing “critical mass”, that is, a sufficient body of major current or potential exporters such that those outside the arrangement do not constitute an export threat while keeping their own markets closed. Critical mass is, therefore, a flexible concept, and will be defined according to the industry subject to the plurilateral and who the main actors in that industry are.

Exclusive plurilaterals of the GPA Annex 4-type are much more challenging to initiate and conclude. As WTO law currently stands, Members wishing to initiate such negotiations need to be assured that no WTO Member would object to the arrangement. These plurilaterals also face the “critical mass” problem. Since intra-Member trust in the WTO context is extremely low, initiating new exclusive plurilaterals currently seems to be a challenging proposition. By contrast, if trust in the negotiating process grows, the “critical mass” requirement would diminish, and vice versa.

Therefore, the central question is how to rebuild trust in favour of plurilateral negotiations in the wake of the Doha Round's failure.

The Case for a “Code of Conduct” to Govern Plurilateral Negotiations

There is a case for taking a step back and initiating a formal

process of negotiating a “code of conduct” to govern plurilaterals in advance of formally initiating any, as proposed a few years ago by the World Economic Forum's global agenda council on the global trade system (World Economic Forum 2010). Such a code could reassure the many developing countries that are nervous of having plurilateral agreements foisted on them, and could include, among other things, the underlying principles that:

1. membership is voluntary;
2. the subject of the plurilateral is a core trade-related issue;
3. those participating in plurilateral negotiations should have the means, or be provided with the means, as part of the agreement, to implement the outcomes;⁵
4. the issue under negotiation should enjoy substantial support from the WTO's membership; and
5. the “subsidiarity” principle should apply in order to minimize the intrusion of “club rules” on national autonomy.

Flowing from these principles, plurilateral codes should also be governed by a set of rules. These could include, among others, the following:

- only parties to the agreement can participate in WTO dispute settlement and, consequently, cross-agreement retaliation should not be allowed, since it would reduce the incentives to join the agreement;
- Any WTO Member can participate in the negotiations voluntarily, subject to demonstrating sufficient capacity to implement the outcomes; and
- the provision of benefits to non-members should not be required, since that would reduce the incentives to negotiate the plurilateral, but could be allowed.

Further, transparency mechanisms should be built into plurilateral negotiations so that exclusiveness could be minimized in order to build trust and interest in it.

Nonetheless, negotiating such a code is likely to be a fraught undertaking given the ongoing impasse in the Doha Round and would require, at a minimum, upfront good-faith gestures on the part of major trading powers such as committing to a real “LDC outcome” from the rump of the Doha Round. Even then success is not guaranteed since there are quite a few

5 | Article X: 8 of the WTO Agreement.

6 | At the inaugural ICTSD Expert Group meeting on the multilateral trading system and PTAs participants agreed that these should include technical assistance and special and differential treatment. The revised GPA agreement provisions may be of some guidance in this regard.

developing countries that remain implacably opposed to the notion of plurilaterals. Consequently, it would take time and patience to build the case.

Which Plurilaterals?

The first question requiring an answer is whether to focus on “carve-outs” from the current Doha Round, or rather select new subjects not contained in the Doha mandate. In its favour, the “Doha carve-out” option means the potential plurilateral agreements would be drawn from the negotiation subjects as agreed in the negotiation mandate. This would ensure that the plurilateral agreements remain within the ambit of the membership’s expectations, since they would be based on subjects agreed to by the broad membership of the WTO. Nonetheless, non-Doha plurilaterals should also be on the table since they could incorporate key areas not adequately covered under current rules, such as investment (World Economic Forum 2013).

Providing a focus to the selection of subjects is the real challenge. Two coherent attempts are worthy of closer analysis, which unfortunately is beyond the scope of this paper—the idea of negotiating a “green” or “sustainable” plurilateral as advocated by the International Centre for Trade and Sustainable Development (ICTSD) and other organizations; and the idea of negotiating a global value chains (GVCs) friendly plurilateral as advocated by the World Bank and the World Economic Forum. The “sustainable” plurilateral is driven by the imperative of addressing climate change and would tackle the underlying competitiveness problem in the climate talks head on, potentially dealing with a major blocking dynamic in the United Nations Framework Convention on Climate Change (UNFCCC) process. Of course it would also confront the politics of that process. The latter would cluster several negotiating areas critical to the operation of GVCs, notably trade facilitation and network services, both of which are critical to LDCs, and developing countries more generally. However, support among the membership for this initiative would depend on a sufficient number of Member states buying into its unilateral liberalization policy logic (World Economic Forum 2012). Currently that seems like a tall order, to judge by the ill-fated LDC package—within which trade facilitation features centrally.

In addition there is the putative International Services Agreement (ISA), and the various NAMA sectorals proposed to date. The ISA seems almost certain to end up being a PTA, which would not require the broader membership’s consensus to implement. The NAMA sectorals, if conceived as inclusive plurilaterals, would “merely” require critical mass to initiate negotiations. However, the political economy dynamics around the free-rider problem are such that inclusive NAMA sectorals are unlikely to get off the ground unless BRICS and other significant emerging markets come on board. As things currently stand, in the post-financial crisis world of creeping protectionism, that seems like a distant prospect.

Furthermore, the underlying dynamic of the “Doha carve-out” option is fraught with difficulties. This essentially comes

down to the fact that the progress of the single undertaking up to this point would have to be unpicked, which could yield a cascade of objections. In principle, a balance could be struck between the multiplicity of interests in play, but the logic of constructing it could lead inexorably back to the single undertaking. In short, if all interests are to be catered for, then we would end up where we started—with a comprehensive negotiating round.

If the “Doha carve-out” is so challenging, what about starting new negotiations on issues not covered under the Doha mandate? The main, probably fatal, obstacle is the fact that the major developing country trading powers that would be needed to secure both critical mass and the broader membership’s consensus, notably BRICS, have so far insisted on maintaining the integrity of the Doha architecture. So while a subject like investment is interesting and necessary to consider in its own right, the prospects of actually launching plurilateral negotiations on it and other non-Doha subjects seem vanishingly small for as long as the Doha impasse endures.

CONCLUSIONS

Getting beyond the Doha impasse is a challenge. Plurilaterals could ultimately be the right way to proceed, but the main challenge is to kick-start the process. From the preceding analysis, we propose a two-pronged strategy, recognizing that the timeframe for success is medium term, and that success is by no means guaranteed. First, the notion of negotiating a code of conduct to govern subsequent negotiation of plurilaterals should be introduced into formal WTO processes. If successfully pursued, this could substantially enhance levels of trust among the membership and, thereby, contribute to building sufficient consensus to launch a serious attempt to negotiate plurilaterals. Second, and in parallel, efforts to launch the “sustainable” and GVC plurilaterals should be accelerated, and accompanied by including as many Member states and relevant stakeholders in transparent discussions about the putative merits of these two potential plurilaterals. In the process, consideration should be explicitly given to whether launching negotiations in these two areas might establish a sufficient “critical mass” of interest among the whole WTO membership and, if not, what other subjects could be added, bearing in mind the need not to overwhelm the negotiating agenda.

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WHEN THE IMMOVABLE OBJECT MEETS THE UNSTOPPABLE FORCE: MULTILATERALISM, REGIONALISM AND DEEPER INTEGRATION

Robert Z. Lawrence

INTRODUCTION

The debate about whether or not regional trade agreements (RTAs) are building or stumbling blocks has raged for more than two decades, and it is not surprising that it has now been joined again. It has always been the case, however, that the answer to the question depends not simply on whether RTAs proliferate but rather on what precisely they entail. "The devil," as the saying goes, "lies in the details." In particular, what is crucial is whether these agreements lead to discriminatory treatment and build in constraints on additional liberalization or whether they actually make the markets of the participants more contestable, not only for themselves but also for non-members. There is evidence of both tendencies at work, although officials generally emphasize the latter. By subjecting each agreement to a "multilateral impact statement," an independent assessment body could encourage agreements that are building blocks.

An observer of the trading system could reasonably draw two contrasting implications from the experience of trade negotiations of the past decade. The first is that the multilateral system is at an impasse. The combination of decision-making by consensus and a highly diverse and heterogeneous membership with powerful and large emerging economies makes it very difficult to include all members in a single undertaking. Not only has it been difficult to get agreement on traditional issues such as meaningful reductions in tariffs and subsidies, but it also has been impossible to obtain agreements that require developing countries as a group to implement rules that constrain their domestic economic and social policies in new areas. At Cancun, for example, it proved impossible to obtain the required consensus to launch negotiations on three of the Singapore issues—competition policy, investment, and transparency in government procurement. The World Trade

Organization (WTO) has also repeatedly passed resolutions rejecting the expansion of its remit to include commitments on labour and environmental standards.

Yet, another powerful force is in motion. Many developed and developing countries are seeking to pursue zero for zero tariff reductions together with deeper integration through regional and mega-regional agreements in precisely the areas that have been roundly rejected by the WTO as a whole. The European Union (EU) and Japan have been actively negotiating deeper agreements with each other and with numerous other partners. Despite a lack of enthusiasm for trade agreements for much of its first term, the Obama administration has now embraced free trade agreements (FTAs) with considerable energy. The comprehensive United States (US) FTAs with Colombia, Panama, and South Korea were passed in 2012, and President Barak Obama has agreed to launch negotiations for the Transatlantic Trade and Investment Partnership (TTIP). Japan has now joined Canada and Mexico as recent additions to the 11 nations that are negotiating the Trans-Pacific Partnership (TPP). The scope and depth sought in the TPP and the TTIP are considerable and far beyond anything contemplated at the WTO. Their agendas call for agreements that not simply eliminate tariffs, but accomplish extensive liberalization in investment and services, place new rules and disciplines on subsidies and state-owned enterprises, and aim to achieve greater regulatory convergence and coherence.

The forces propelling both these trends are strong. On the one hand, as large emerging economies become increasingly important, it has become more difficult to either ignore them or to coerce them into signing agreements they deem against their interests. Prior to the Uruguay Round it was relatively easy for the developed countries to simply exempt developing countries from obligations when these countries were unwilling to sign. In the Uruguay Round, by buying off some countries with concessions (such as the elimination of the Multi-Fibre Arrangement quotas that protected textiles) and putting pressure on others to go along, it was possible to induce developing countries to sign an agreement that contained intellectual property rules to which many were opposed. But that time has now passed, and since Cancun it has become clear that the emerging economies not only can say no, but when they do, achieving agreement with a single undertaking becomes impossible because they are too important to exclude.

On the other hand, the forces driving deeper integration have also become stronger. The combination of liberalization, improvements in technology, logistics, and telecommunications has increased the possibilities of reaping additional economic gains from economic integration through establishing and improving the operation of global value chains. Multinational corporations are thus leading the way to help take full advantage of these opportunities by agreeing to new rules and more effective governance, and many countries seeking the growth and employment these companies can provide are willing to oblige. In addition,

in many advanced countries, representatives of the major political forces (labour, environmentalists, and enterprises) all seek “a level playing field” in which their foreign competitors are subject to similar rules. Hence the pressures for agreements to include rules for labour, environment, and competition policies.

So what happens when (the immovable object of) resistance to the erosion of domestic policy space by emerging economies meets the (unstoppable) force driving deeper regional integration? Thus far the clash has left the WTO at an impasse. But could the regional initiatives be a way in which they could be reconciled?

A TEMPLATE

Probably the least likely outcome is the claim, commonly offered by official proponents of regional negotiations that, once concluded, the new RTAs can be rubber-stamped in broader agreements at the mega-regional and multilateral levels. The TPP in particular is seen as “the most promising platform for development of an eventual Free Trade Area of the Asia-Pacific,” and as the basis for agreements on 21st century issues in order “to raise the overall bar for the multilateral trading system.”¹ While such claims may provide officials with some cover from accusations that they are undermining the multilateral system, they are not very convincing.

Given the problems with ending the Doha Round with its emphasis on conventional issues such as agricultural subsidies and market access for industrial products, and the positions taken on issues of deeper integration described above, it is not immediately apparent that the central problem of the multilateral system will be solved by “raising the bar” through deeper RTAs that emphasize regulatory convergence, investment liberalization, and generally higher standards. Indeed, these are precisely the kinds of issues the multilateral system has the greatest problems dealing with. On the basis of the experiences of the ill-fated Multilateral Agreement on Investment in the 1990s and the debacle at the Cancun Ministerial, it is especially hard to understand why the excluded developing countries should be expected at the Asia-Pacific Economic Cooperation (APEC) or the WTO to embrace an agreement they were not even party to negotiating.

Will the centripetal attraction of the specific rules that are crafted really be so great that once the TPP and/or the TTIP are signed, China, Brazil, India, and other major emerging economies will have no choice but to follow the lead of those that have signed? If Vietnam agrees in the TPP, for example, to accept restrictive rules for the operation of its state-owned enterprises, will China then sign meekly on the dotted line? If the participants in the TPP and/or the TTIP agree to the inclusion of labour standards (or the preservation of intellectual property protection that inhibits the introduction of generic pharmaceuticals), will India feel it has no choice but

to go along? It is very unlikely that in their precise negotiated form these agreements will soon become blueprints for the WTO.

If they were crafted in a manner that really allowed them to command universal acceptance—simply and without reservations—their wider adoption, while still unlikely, might be easier. But in reality these agreements are the outcomes that result from a host of politically driven pressures that depend critically on the power and specific needs of those who are at the table. And this is likely to create obstacles for their broader application, especially as complete packages. The inclusion of environmental and labour standards in these trade agreements, for example, may make it easier to obtain political support for the TTIP and the TPP in the US Congress, but at the same time could make it impossible to broaden the agreement to include other major partners if these are a precondition for joining.

The TPP is indeed ambitious, but there are numerous inconsistencies between the rhetoric on the one hand, and the concessions to political realities on the other. High standards, like beauty, are in the eyes of the beholder. On pharmaceuticals, the US position is that the stronger the intellectual property protection for pharmaceuticals the better. With respect to state owned enterprises, hard budget constraints are to be the order of the day. And when it comes to regulatory practices, high standards are likely to involve US-like procedures such as transparency, and judicial and public review. But when it comes to sector exclusions, rules of origin (RoO), and the phasing in of benefits, streamlining is expected to take a back seat. One might have hoped, for example, that in a 21st century agreement, the central vision would be akin to that in the EU92 initiative with the exception of the free movement of labour, that is, the aim would be to achieve, as soon as possible, a single integrated internal market with the free movement of goods, services, and investment capital. In this case, all 11 participants in the TPP would be governed by a single set of rules. But the US and some others have insisted on negotiating with participants bilaterally in what is really a hybrid mega-regional in which the concessions that were made in their bilateral agreements will remain in effect. Thus, since sugar was excluded from the US-Australia agreement, for example, it will not be included in US TPP concessions to Australia. Similarly, a 21st century agreement might have been expected to allow the diagonal cumulation of content across all members to meet RoO. Thus fabric from Malaysia could be combined with sewing in Vietnam in order to sell in the US or Japan. But this is unlikely to happen.

1 “The TPP has been central to this rebalancing toward Asia and it’s, as you know, a high-standard agreement. It’s an agreement that seeks to set high standards for 21st century issues as a way of raising the overall bar for the multilateral trading system” (transcript of on-the-record conference call by then Deputy National Security Advisor for International Economic Affairs, Michael Froman), [http:// www.ustr.gov/about-us/press-office/speeches/transcripts/2013/april/dep-nsa-froman-amb-marantis-cc-tp](http://www.ustr.gov/about-us/press-office/speeches/transcripts/2013/april/dep-nsa-froman-amb-marantis-cc-tp).

These problems in creating the TPP are a microcosm and a test case for the problems of welding RTAs into a more comprehensive arrangement at the multilateral level. Generally what is being sought is a politically realistic compromise between achieving greater integration, and preserving the political benefits that were achieved when the earlier agreements were negotiated. This does not make progress impossible, but it does make it difficult. And it certainly suggests that the rhetoric, which talks about high 21st century standards, deserves to be taken with a grain of salt. The key question that only time will resolve will be whether the RTAs will indeed serve as a foundation upon which more comprehensive agreements can be built, or whether they will actually make these far more difficult to achieve.

UNEASY COEXISTENCE

An outcome, that is more likely than the wholesale adoption of the TPP or TTIP templates, therefore, is that the current uneasy coexistence of the WTO and RTAs will continue. The WTO will hopefully remain effective in enforcing its existing rules and acting as a forum for discussion and review of trade policies. It might also achieve progress in areas such as trade facilitation, preferences for least developed countries, and the enlargement of product coverage and additional membership in sector agreements and new plurilaterals. But the prospects for a new, mega multi-issue agreement, especially one based on a single undertaking, will be dim. Increasingly, therefore, the attention of many members will be concentrated on their bilateral and mega-regional initiatives. And, with varying degrees of success, these agreements will make some progress.

While clearly not the best of all worlds, this coexistence scenario has both costs and benefits. The costs could be largest if the mega-regionals that are crafted serve to fragment the world economy into haves and have-nots, that is, into a world divided between those countries that are willing to accept a US and/or EU template for trade agreements and those that are not. These costs could also be felt through lost opportunities for non-discriminatory multilateral liberalization by some of the most dynamic and significant emerging economies. The BRIC countries, for example, are unlikely to sign up to regional or multilateral trade agreement templates that do not reflect their priorities. Yet they are also too large to be ignored, and are more likely to concentrate on concluding their own regional initiatives based on different principles and rules. Some countries may find it possible to coexist in both camps, but others may be excluded, and all of this would come at the expense of achieving a more integrated global trading system under the effective aegis of the WTO.

“The devil,” as they say, “lies in the details.” Depending on how they are crafted, there could, however, be benefits from RTAs, even in this “uneasy coexistence” scenario. Some of the deeper aspects of these agreements could automatically

provide benefits to outsiders even if they do not participate directly in the agreement or adopt its rules, by making these markets more contestable. For example:

- More effective measures to control subsidies in a US-EU agreement would not only assist non-subsidized US and European firms and farmers who compete with each other, but also help all foreigners to compete in the US and the EU.
- The achievement of regulatory transparency and reforms would similarly reduce transactions costs not only for insiders but also for all who sell in these markets.
- Measures that facilitate trade, by making customs and regulatory practices more efficient, will likewise benefit all firms, including outsiders that are involved in trade.
- Higher labor and environmental standards might help create an internal level playing field among participants in a regional agreement; but if they raise costs, they could also improve the competitiveness of outsiders.
- Proponents of establishing a single US-European standard sometimes present it as something that will enhance these economies to compete with outsiders. And indeed having a single standard would create efficiencies and lower internal costs. But having to meet only one standard in the US and Europe would also reduce the costs of those who wish to export to it. If the US-EU agreement achieves enhanced approvals of genetically modified products, for example, the benefits would similarly accrue to all producers of these products. Similarly, if mutual recognition of standards were to be agreed between the US and the EU, and outsiders required to meet either the US or the European standard in order to sell in the whole transatlantic market, outsiders would gain.

NETWORK EXTERNALITIES

The multilateral system and other RTAs are likely to be influenced by these agreements, not because other countries formally sign up to its provisions, but rather because they are more likely to voluntarily adhere to their standards and rules because it reduces transactions costs. Conventional wisdom has it that higher standards will lead to a race to the bottom, but there are mechanisms by which standards can lead to a race to conform. Exporters may have no choice but to configure their products to meet the particular standards of one very large market, but once they do, they are more likely to retain the same configuration in other markets. (This point was made, for example, by those who pointed out that the North American Free Trade Agreement [NAFTA] could improve environmental outcomes by inducing Mexican auto firms to produce cars that meet US standards.)

The influence of these large mega-regional agreements will thus be felt indirectly through the power of what are known

as network externalities, that is, the benefits that accrue to existing participants when more members join a network. If no one already had learnt how to type using QWERTY typewriter keyboards, perhaps a better arrangement would work on today's electronic keyboards. But today keyboard manufacturers have no choice but to use it, since that is the arrangement most people expect. Similarly, Esperanto may be a fairer option for the global language, but once a critical mass of people started using English as their first or second language, the rest had to learn and use it in order to be understood. By this logic, if the economies that sign the TPP and the TTIP—which together make up more than half of world trade and gross domestic product (GDP)—agree on a standard, the rest of the world will have incentives to follow. This again suggests a mixed verdict. From a global standpoint, these may not be the best possible standards, but the power of network externalities will tend to induce adherence anyway. On the other hand, common standards could reduce transactions costs and facilitate competition.

A second major indirect influence will occur through setting precedents that will enable additional liberalization. If the participants in a deep regional agreement are prepared to grant one another concessions, they are more likely to be willing to grant other countries similar benefits, both in RTAs and multilaterally. If Vietnam, for example, agrees in the TPP to allow multinational firms from the US, Japan, and other TPP nations the freedom to invest, or the ability to be subject to investor-state dispute settlement, it is far more likely to be willing to allow investment from other nations. This enhances the possibility that it would sign other plurilateral or multilateral investment treaties. Many European countries, for example, have become accustomed to granting other European countries mutual recognition in the context of the EU. Their experience makes it easier for them to conclude mutual recognition agreements with the US. For the US, however, the approach presents challenges. But if the US adopts forms of mutual recognition in the TTIP, others seeking deeper integration with the US may find the going easier.

These potential integrative benefits need not only be indirect. They could (and should) also be consciously cultivated by those concluding the agreements. Especially in the case of the US-EU, for example, there are opportunities to make important contributions towards helping unravel the spaghetti bowl of RoO that currently lead regional arrangements to fragment the global economy. The line of least resistance in the TTIP would be to negotiate another unique set of rules that cover only the agreement and would be overlaid on the RoO that govern the US and EU agreements with others. Imagine the possibilities if the TTIP RoO were constructed to serve as the basis for all the RTAs signed by both partners. Implementing the same RoO (and allowing for diagonal cumulation) in all RTAs in which either the US or the EU participate would achieve far more conformity than anything the WTO could feasibly achieve. However, the existing rules have been carefully crafted to

meet particular protectionist pressures, and it will take great political will to resist them.

Proposal: Multilateral Impact Statements

In the US, federal policymakers are encouraged to take account of the environmental impacts of their actions, by requiring all qualifying measures to be subject to an environmental impact statement.² The purpose of these exercises is not necessarily to prevent the measures from being implemented, but rather to raise awareness and to encourage policies that minimize environmental impact. Similar awareness should be raised in an effort to encourage the negotiators of regional arrangements to put their money where their mouths are and design agreements that would (a) create contestable markets that provide benefits to outsiders as well as participants, and (b) serve as the modular components of a more integrated global trading system. One mechanism for doing this would be for an independent authoritative body—either a think tank or distinguished panel of trade authorities—first to lay out a set of relevant criteria and then to apply these to an analysis of RTAs. Ideally, suitable methodologies and criteria would be widely available, and it should become standard practice for drafts of agreements to be analysed prior to being finalized so that negotiators would be given opportunities to correct major deficiencies.

CONCLUSION

Some would like to see the WTO eliminate RTAs or subject them to stringent disciplines. But this will not happen. Countries have already proceeded too far with their commitments. Moreover, RTAs should not be eliminated. Some functions are, in principle, better carried out at a sub-global level. Viewed simply as tariff reducing exercises, preferential arrangements are said to be “second best” because they can divert trade. But the WTO also does not eliminate all barriers, and its partial multilateral trade liberalization, the realistic alternative to preferential arrangements, is also “second best” in the same way. So the choice is between two second-best approaches, and it is an empirical matter as to which is superior. Indeed both can promote trade.

Regional agreements can be discriminatory and can introduce unwarranted complexity to the trading rules. However, by creating markets that are more easily contested; by

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As noted, “Contrary to a widespread misconception, NEPA does not prohibit the federal government or its licensees/permittees from harming the environment, but merely requires that the prospective impacts be understood and disclosed in advance. The intent of NEPA is to help key decision makers and stakeholders balance the need to implement an action with its impacts on the surrounding human and natural environment, and provide opportunities for mitigating those impacts while keeping the cost and schedule for implementing the action under control” (http://en.wikipedia.org/wiki/Environmental_impact_statement).

implementing standards that others voluntarily adopt; and by setting precedents that make countries more accustomed to signing deeper agreements, RTAs could make deeper agreements at the WTO easier to negotiate. At the end of the day, therefore, the old question still arises—will these agreements serve as stumbling blocks that prevent multilateral integration or can they actually be building blocks? Trade policies should be focused on trying to ensure that they are building blocks.

WILL THE WTO HAVE FUNCTIONAL VALUE IN THE MEGA-REGIONAL WORLD OF FTAS?

Andrew L. Stoler

INTRODUCTION

The negotiation of a Trans-Atlantic Trade and Investment Partnership (TTIP) agreement between the United States (US) and the European Union (EU) would create an integrated market accounting for 40 percent of global gross domestic product (GDP). The bilateral trading relationship is the world's largest, with the US annually exporting USD 458 billion in goods and services to the EU and buying 17 percent of EU goods exports and 25 percent of EU services exports. The stock of foreign direct investment (FDI) that the US and EU have in each other's markets amounts to USD 3.7 trillion.

The Regional Comprehensive Economic Partnership (RCEP) negotiations aimed at producing a regional trade agreement (RTA) grouping Association of Southeast Asian Nations (ASEAN) members with China, Japan, Korea, India, Australia, and New Zealand would cover 50 percent of the world's population, 30 percent of global GDP, and 25 percent of global exports.

The Trans-Pacific Partnership (TPP) negotiations, assuming they one day reach the goal of an Asia-Pacific Economic Cooperation (APEC)-wide RTA, would cover 40 percent of global trade, including 60 percent of US merchandise exports, and 39 percent of the country's services exports. The decision by Japan to join in the negotiations and recent expressions of interest by China in the project greatly increase the potential economic value of the TPP as well as its potential to attract additional participants in the near future.

In addition to these projects, the EU and Japan have launched comprehensive trade and investment negotiations and the leading countries of Latin America's Pacific rim have initiated regional talks aimed at consolidating an Alliance of the Pacific—a market integration effort that would amount to the ninth economy of the world.

These are all mega-regional trade and economic integration projects, which, if successfully completed, would see the most important international goods, services, and investment transactions of the participants comprehensively covered by preferential free trade agreements (FTAs). Even more significantly, while the agreements promise to eliminate tariffs, all are focused on dealing with the behind-the-border regulatory and other issues that are of greater concern to business in the 21st century. Most of these behind-the-border questions would be addressed through so-called "WTO-plus" commitments, meaning that they either deal with issues beyond the scope of today's WTO coverage or take a WTO-covered subject and employ a different approach that produces a superior result in a regional agreement.

The WTO system is generally considered to have three principal functions—liberalizing international trade in goods and services through multilateral trade negotiations; overseeing the implementation of the system of multilateral trade agreements; and settling disputes among WTO Members where those disputes relate to "covered agreements." The central question explored in this paper is whether the WTO could be expected to retain a meaningful functional value for its members in the soon-to-be-realized world of WTO-plus mega-RTAs.

An important caveat is in order at this point. The proponents of the mega-regionals have promised much in their characterization of the new trade pacts as 21st century trade agreements. To qualify as such, the new agreements will need to go beyond what has been negotiated regionally in the past. For now, we will assume that the ambitious objectives of the TPP, TTIP, and others will be met, and that agreements with these characteristics will be the comparator with what is on offer in the WTO. Obviously, if the mega-regionals fail to attain the objectives set for them, we will be looking at a different (and less satisfactory) international reality.

THE MEGA-REGIONAL PROBLEM FOR WTO

What do business people and policymakers in economies where international trade and investment are important want from trade agreements in the 21st century? Naturally enough, they want to participate in agreements that deliver real additional access to key markets, remove discrimination from regulatory environments, and improve and guarantee the legal safety of their valuable commercial rights and investments.

Against this background, does the WTO system deliver—particularly when judged against the mega-regionals?

Liberalization and Access to Markets

The failed Doha Round of multilateral trade negotiations certainly calls into question whether the WTO can any longer deliver on liberalization and market access. But even if the Round had not failed, would it really have produced new access to markets? Probably not. There is so much “water” in most WTO Members’ bound tariff rates that even huge cuts would not affect real market access. The bound Australian tariff for automobiles is 40 percent ad valorem, compared to a currently applied rate of 5 percent. The December 2008 modalities for the Non-Agricultural Market Access (NAMA) negotiations suggest the use of a “Swiss formula” with a coefficient of 8 for developed countries—which would cut Australia’s bound rate for automobiles to 6.7 percent—with no improvement in access. For a developed country with average MFN tariffs around 4.5 percent, post-Round tariff averages would still be 2.9 percent—scant improvement to access.

In the case of market access for agricultural products, the last version of the Doha Round modalities was so riddled with exceptions, exemptions, special product and sensitive product designations and safeguards that it is a sure bet that the result of the negotiations would not have produced increased access for any agricultural products other than those which countries had to import because they did not produce them at home.

In the agriculture negotiations, there are roughly 620 six-digit HS tariff lines from Chapters 1 to 24 that are subject to market access modalities. Under these modalities, developed countries would be able to completely exempt 37 lines from liberalization and developing countries could exempt up to 162 tariff lines from cuts. Worse still, there would be multilateral acquiescence that the exempted items are justifiably “sensitive” or “special”—seriously compromising future efforts to liberalize trade in these products.

The situation is no better for services trade, where it is generally recognized that WTO Members’ scheduled services commitments reflected the status quo at the end of negotiations 20 years ago in 1993 and where the offers tabled in the Doha Round rarely came close to matching the commitments the same countries were prepared to make in regional negotiations.

Modern 21st century mega-regionals have a WTO-plus approach to liberalization and market access. Generally, the objective is tariff elimination—although this may be phased-in in some cases and occasionally subject to special transitional safeguards. For services trade, the mega-regionals tend to follow the “top-down” or “negative list” approach, which is both far more liberalizing and much more transparent than the “bottom-up” approach dictated by the WTO General Agreement on Trade in Services (GATS) agreement.

So, even if the Doha Round had not failed, there is no reason to believe that the WTO would have been perceived to have delivered on its liberalization/market access function. This is particularly true when those potential Round results are looked at in relation to the expected outcomes of the mega-regionals.

Implementation of System Agreements

It could be argued that the WTO Councils and Committees have done a reasonably good job of overseeing the implementation of the existing WTO agreements and arrangements—but that would be based essentially on a static view of the world and whether the disciplines agreed in 1993 should have been expected to evolve and improve over time.

Viewed from the standpoint of a trading enterprise, some of the most important agreements in the multilateral system are addressed to critical questions such as product standards, conformity assessment, quarantine regulations, customs procedures, and intellectual property protection. Unfortunately, in most cases, these existing agreements tend to reflect what could be agreed on as a “lowest common denominator” and, for a variety of reasons; they tend not to impact on real, specific border and behind-the-border problems and regulatory issues.

The difference between the WTO and the WTO-plus approach of mega-regionals can be illustrated by two of the objectives for the TTIP listed by the Acting US Trade Representative in his 20 March 2013 letter to Congress.

- Seek to build on key principles and disciplines of the WTO Agreement on Technical Barriers to Trade through strong cross-cutting disciplines and, as appropriate, through sectoral approaches, to achieve meaningful market access, and establish ongoing mechanisms for improved dialogue and cooperation on TBT issues.
- Seek greater compatibility of US and EU regulations and related standards development processes, with the objective of reducing costs associated with unnecessary regulatory differences and facilitating trade, inter alia by promoting transparency in the development and implementation of regulations and good regulatory practices, establishing mechanisms for future progress, and pursuing regulatory cooperation initiatives where appropriate.

Once the US and EU begin to use the TTIP to set the standards and cement an approach to regulatory coherence, that will be their template for their future relations with non-TTIP members in the rest of the WTO. With the template thus set, the influence of others will be minimized, no matter what is said in the general principles of the Technical Barriers to Trade (TBT) and other agreements.

And it is not just the TTIP. Similar “regulatory coherence” objectives characterize the TPP negotiations in the Pacific. Current Geneva-centered activity in the implementation of WTO agreements does not come close to matching such ambitious objectives in these areas of real practical concern to the people who actually engage in international trade. What the mega-regional negotiators have appreciated is that the world has moved on from 1993 and whether you are discussing TBT or customs procedures or other areas where WTO-plus has become a part of modern trade agreements, we need to see the possibility of concrete results on discrete problems affecting trade—not just a respect for the principles of multilateral agreements.

Dispute Settlement

It is often argued that notwithstanding the explosion of RTAs over the past two decades, the trading system will always need the WTO because it has shown itself to be very effective in the management of dispute settlement. It is certainly true that relative to other international tribunals, the WTO Dispute Settlement Understanding (DSU) system has been a great success story. But whether or not the WTO’s dispute settlement function and its attractiveness to its members can stand up to the challenge from the mega-regionals and their WTO-plus elements in the future depends on the answers to a few important questions.

First, will the mega-regionals be successful in terms of their hoped-for country coverage or will important WTO Members be left out of these new arrangements? Second, will the WTO system be able—in the reasonably near future—to expand its “covered agreements” to include the topics dealt with today only in RTAs and the mega-regionals? Third, will the dispute settlement mechanisms of the mega-regionals be seen as robust as the WTO DSU system we have benefitted from in the post-Uruguay Round period?

If all major trading countries—and bearing in mind that not all countries that are in positions of influence in the WTO today are major trading countries—are covered in the next few years by WTO-plus mega-regionals, then it is quite possible that the functionality of the WTO DSU would be called into question.

Why do major trading powers like the US and the EU abide by the outcome when they lose disputes to the likes of Costa Rica and Ecuador in the WTO? It is because they do not want their big trading partners to accuse them of bad faith if they do not, in which case the system will start to break down. But one needs to wonder whether the same incentive to live up to WTO dispute settlement rulings will be there if a WTO Member can depend on effective dispute settlement with its most important partners through a mega-regional agreement’s dispute settlement system.

The bigger problem is that the demise of the Doha Round has demonstrated that the functionality of the WTO’s DSU is certain to be compromised to a very important degree

by the shortcomings of the system in terms of its limited “covered agreements.” We already know that investment disputes must go to other bodies like the World Bank group’s International Centre for Settlement of Investment Disputes (ICSID). Other questions, like North American Free Trade Agreement (NAFTA) trade remedy disputes, have specific avenues of resolution expressly limited to the RTA’s own procedures.

Finally, the mega-regionals under negotiation are likely to bring on board some of the innovative developments in dispute settlement that have evolved since the end of the Uruguay Round. For example, some FTAs allow for the imposition of monetary fines on offending governments in place of trade retaliation. The WTO system needs to account for developments like this.

WHAT CAN WTO HOPE TO DO TO REMAIN RELEVANT?

We have so far looked at the principal functions of the WTO and how these functions might well be undermined by developments on the mega-regional front. The discussion shows that the problem for the WTO is not limited to the failed Doha Round’s inability to deliver on liberalization and market access but in fact is more generalized—likely affecting all three of the WTO system’s main functions. It is about much more than the Doha Round.

A great deal of effort has gone into the GATT/WTO system over the years and it would be a great pity if it were to become irrelevant due to its failure to address current challenges to its viability. We need to be conscious of the fact that the extra-WTO mega-regional environment is evolving at an accelerating pace and if we are not already out of time to save the WTO, we are rapidly approaching the point where it could be too late. So what can be done? There is no possibility of stopping the mega-regional juggernaut at this point in time, so developments on that front must be taken as a given, as well as assumptions for the future. This means that the change has to take place in the WTO if the institution is to survive. That said, the WTO of the future will almost certainly be a different WTO than we see today.

WTO-plus Elements of Mega-Regionals

A starting point in the discussion of potential responses is to understand what the challenges for the WTO are in terms of the WTO-plus elements of the new mega-regional trade agreements. Leaving aside for now the assumed impracticality of 159 WTO Members agreeing to follow the mega-regional approach to market access (that is, going to free trade in goods and services), and using the stated objectives of the TTIP as a basis for the discussion, WTO Members need to try to meet the challenges of mega-regionals in the following areas.

Investment: All the mega-regional projects will have an important focus on FDI, including the RCEP negotiations to which India is a party. WTO Members made a serious mistake in 2004 when as part of the so-called framework agreement they stopped work on investment in Geneva. In the TTIP, investment negotiations will seek to establish a national treatment regime that eliminates artificial or distorting barriers to investment and an agreement that provides meaningful procedures for resolving investment-related disputes.

Competition policy and consumer protection: The objectives of the TTIP include addressing matters of mutual interest on competition policy and process, and improving cooperation on competition policy, as well as in e-commerce-related consumer protection initiatives.

Regulatory coherence and convergence: This is about TBT and Sanitary and Phytosanitary (SPS) measures but also more. As already noted, the mega-regionals aim to eliminate barriers that exist just because partners have historically chosen different ways of achieving the same shared regulatory objectives. Mutual recognition arrangements and cooperation in the development of new standards and conformity assessment procedures can go a long way to achieving the objective of regulatory coherence.

Trade facilitation: Even if a new WTO agreement on trade facilitation was reached, it would not be the same as what we see in mega-regionals where the emphasis is on concrete measures to speed border crossings and reduce the red tape associated with international trade. Trade facilitation, of course, is perhaps the single most important thing governments can subscribe to if they want to make it possible for their producers to link to global value chains.

Electronic commerce: Agreements like the TPP and the TTIP will contain provisions designed to facilitate the use of electronic commerce, including through commitments not to impose customs duties on digital products; procedures for authentication of electronic transactions; electronic filing of customs documentation; and setting the rules for international data flows.

Government procurement: This is an area where the WTO commitments apply to only a very limited number of members. In most modern 21st century agreements (and certainly in all the mega-regionals), government procurement markets are recognized as major opportunities that need to have rules guaranteeing fair, transparent, and predictable conduct of purchases by participating governments. In the WTO, there are not even any GATS procedures for services procurement, but services are normally covered in RTAs.

Intellectual property rights protection: The TRIPS agreement dates from 1993. Developments in technology, particularly in copyright for digital products, have led to the need for new protections not afforded adequately by TRIPS.

Existing and future RTAs recognize this problem and deal with it through updated WTO-plus protections for intellectual property (IP).

State-owned enterprises: The negotiation of rules to set globally relevant disciplines on state trading enterprises, state-owned enterprises (SOEs) and designated monopolies appeared as an issue for the first time in the TPP negotiations and has been (wrongly) interpreted by some as being aimed at China and its multitude of SOEs. The issue is broader than China and the TPP and features as an objective of the TTIP as well.

Other areas: Provisions addressed to labor standards and environmental protection are also likely to feature in the mega-regionals under negotiation. Since there is no “root” to these questions in existing WTO agreements, we will leave them aside for the moment—but without prejudice to the reader’s consideration whether their treatment in the WTO materially affects the WTO’s ability to function effectively in the future.

Potential Responses

In some respects, it is probably already too late to save the functionality of the WTO from the impact of mega-regional trade agreements. This is almost certainly the case when one looks at trade liberalization and real improvements to market access, especially when one looks at the backward-moving proposals contained in the Doha Round draft modalities for market access in agricultural trade. That said, there are probably some things that WTO Members could consider doing if they want to preserve some credibility in the system, post-mega-regionals.

In the next—and final—section of this contribution, I will try to explain why I think we must accept that the nature of the WTO in the future must change in some fundamental respects, compared to the 20th century institution created in 1995. Before coming to that discussion, I would like to revisit a couple of points made in an earlier paper on a related topic. These points relate to the need to at least initiate a dialogue in the multilateral system on the WTO-plus elements now so prevalent in RTAs and foreseen for the mega-regional projects.

Kati Suominen has proposed the creation in the WTO of an “RTA Exchange” that could help make the best out of RTAs in the interest of the global trading system. She has suggested that such an exchange could serve as a clearing house and forum where all matters related to RTAs and their practices could be discussed among all WTO Members. The exchange could also help to transfer best RTA practices from one RTA to another. In an era of mega-regionalism, this could be particularly important for new RTAs among smaller groupings to ensure that their practices align with those of the major trading powers.

I have previously backed a very similar idea and drawing on that earlier contribution I believe that participation in the

exchange should also be open to both global and regional organizations and groupings with experience in dealing with WTO-plus issues. The discussion would be enriched by the participation of the Organisation for Economic Co-operation and Development (OECD), regional development banks, regional UN economic commissions, and the secretariats of the APEC, ASEAN, and regional economic cooperation agreements in Africa and Latin America. Recognizing that the business community is the natural constituency for action on these behind-the-border measures, some form of participation by relevant international business groupings should also be facilitated. The creation of the exchange would be without prejudice to discussion of these topics, as appropriate, in existing WTO bodies, including the GATS and TRIPS Councils, the Committee on Trade and Development, and the Committee on Regional Trade Arrangements (CRTA). In fact, these specialized committees and councils should be encouraged to develop inputs to the discussion in the exchange.

In his contribution to this project, Robert Lawrence has suggested that RTAs, especially the mega-regional RTAs of the future, might be usefully subjected in the WTO multilateral impact assessments (akin to environmental impact assessments required for major projects in many countries). To my way of thinking, this idea could be sensibly added to the RTA Exchange-type proposals that both Kati Suominen and I have raised in other think piece papers.

But WTO Members have to buy into these ideas and embrace them recognizing the constructive spirit in which they are advanced. They need to understand that the functionality of the institution is at stake and act accordingly.

Establishing a dialogue on the mega-regionals and their attendant WTO-plus issues in Geneva on this basis would add to the credibility of the organization by demonstrating that WTO Members are supportive of a multilateral discussion designed to enhance coherence between trade agreements negotiated regionally and bilaterally and that Members are capable of responding to the challenges of today. Even better, if a multilateral discussion led to harmonized approaches, then the exercise would facilitate the eventual multilateralization of key parts of RTAs, including mega-regionals. If we could reach agreement that these would be the objectives of the exercise, why should any WTO Member raise an objection to such an "exchange"? But this will merely help to keep the WTO relevant in a changed role from that which was originally envisaged for the organization. As we look to the future, we need to realize that, for better or worse, the functional utility of the WTO will be different than it has been in the past.

CONCLUSION AND RECOMMENDATIONS

The WTO has to accept that it has to proceed in the future on the basis of something other than the single undertaking.

WTO members should recognize that the WTO of the future will necessarily be different from the WTO of the past. In this connection, and in the spirit of a constructive contribution, I offer the following recommendations for consideration by WTO Members.

Market Access and Trade Liberalization

- In a new era of mega-RTAs and proliferation of RTAs more generally, we should accept the fact that real market access is effected through RTAs and not through multilateral agreements. The exception to this should be accession negotiations of new members of the WTO that (obviously) need to commit to trade liberalization as a part of the accession process.
- The Doha Round is dead. Over the years—and particularly since the framework agreement in 2004—the trade liberalization “modalities” of the Round have become so distorted that they are a real step backwards and the sooner they are buried and forgotten the better.
- No future attempts at trade liberalization through a “single undertaking” process should be considered at the WTO.

Conditional MFN and Critical Mass Plurilaterals

- If the Doha Round has demonstrated anything, it is that the WTO's membership now precludes the idea of moving forward with negotiations based on a one-size-fits-all approach. This means that any progress on rules-based questions (my comments above explain why I do not believe this works for market access) should be on the basis of conditional most favoured nation (MFN) and critical mass plurilateral agreements.
- If WTO Members do not accept that future rules-related agreements should be negotiated on this basis, they must recognize that they will be driving all such activity into the RTA and mega-regionals context.

RTA Exchange and Impact Assessment

- As explained above, it is critically important for the future relevance of the WTO that it initiates a meaningful multilateral dialogue on the issues and commitments developed in the context of today's RTAs and tomorrow's mega-regional agreements.
- One important objective of such an exercise should be to try to gauge the impact of future mega-regionals on the multilateral system (and its functionality).
- Another objective of the exercise should be to develop shared understandings of ways in which problems can be best addressed and the creation of some shared views on best practice approaches that might be “multilateralized” at some future date.

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