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As part of its project on the Role of the WTO in the World Economy, supported by the Netherlands Ministry of Foreign Affairs and the Berger International Legal Studies Program at Cornell University, the Cordell Hull Institute held a one-day meeting in Washington, DC, on October 20, 2004, on Developing Countries in the WTO System.

The meeting was at Hogan & Hartson, attorneys-at-law, in its Washington office in the Columbia Square Building (pictured above), designed by I.M. Pei.

Attached is the paper by **Richard Newfarmer** (above) that was presented at the meeting.

About the Author

Richard Newfarmer is Economic Advisor in the

PAUSE FOR REFLECTION…

Coherence Among WTO and Regional Agreements

Richard Newfarmer

MY COLLEAGUE Alan Winters has succinctly put forward, in a separate paper, arguments showing ways bilateral and regional trade agreements – let's call them preferential trade arrangements (PTAs) – undermine the multilateral system. This note briefly reviews recent developments in the formation of PTAs, elaborates on some of Alan Winter's concerns about the effects of PTAs on the multilateral system and discusses some of the development implications.[1]

Recent Developments

The 1990s witnessed the beginning a new wave of PTAs. Since 2000, several major new trends have emerged in the pattern of regional trade agreements:

- the European Union's move towards bilateral free trade agreements and Economic Partnership Agreements with the small African, Caribbean and Pacific (ACP) countries belonging to the Contonou Convention;
- the shift in the position of the United States towards bilateral preferential agreements; and
- the effort of a handful of developing countries to open markets through PTAs.
- One unifying characteristic is that these take preferential trade arrangements well beyond agreements between adjacent countries.

More Agreements are Being Signed

Since 1990 the number of PTAs in force has risen from 50 to nearly 230. The World Trade Organization (WTO) estimates that,

International Trade Department and Prospects Group of the World Bank. He joined the World Bank in 1983.

Prior to this particular position at the World Bank, he was Lead Economist in the Chief Economist's Office of East Asia during the Asia crisis (1997-2000), and earlier, he was the Lead Economist for the China and Mongolia Department from 1995 until July 1997.

Before becoming Lead Economist, Mr Newfarmer was Chief of the Industry and Energy Division in the China Department (1993-1995).

He was also Principal Economist for Argentina in the Latin American region (1988-1992) and has also worked on Chile, Brazil, and other Latin American countries.

Mr Newfarmer served as a Senior Fellow at the Overseas Development Council and he was on the economics faculty at the University of Notre Dame.

Mr Newfarmer earned a Ph.D. and two Masters degrees from the University of Wisconsin, and a B.S. from the University of California at Santa Cruz.

Other Speakers

The meeting was attended by 55 trade-policy specialists, mostly from the Washington, DC, area.

Besides Mr Newfarmer, the others speakers were: **Carlos Primo Braga** and **Alan Winters**, economic advisers at the World Bank; **Hugh Corbet**, president of the Cordell Hull Institute, **John Barceló**, of the Cornell

as of the end of 2004, another 60 agreements are in various stages of negotiation. The boom in PTAs reflects changes in certain countries' trade policy objectives, changing perceptions of the multilateral trade-liberalizing process and the re-integration into the world economy of countries in transition from socialism to becoming market economies. This last factor accounts for many of the new agreements signed in the early 1990s, when countries in Eastern Europe and the former Soviet Union negotiated PTAs with Western Europe – both the European Union and the European Free Trade Association (EFTA) – and with each other.

Trade in PTAs is Rising – but preferential trade is less than it appears

The share of global trade taking place between PTA members is growing as the number of agreements increases. By 2004 it had reached over one third.[2] Disregarding intra-EU trade, bilateral flows between PTA members have been growing at a rate similar to the growth rate of agreements themselves. This overstates, however, the amount of trade that takes place on a preferential basis. Tariff schedules of many PTA members increasingly contain duty-free MFN rates on which no preference can be given. The amount of preferential trade among PTA members, after accounting for MFN rates of zero, is much lower at 21 percent of world trade.

Furthermore, it is often more profitable for enterprises to pay a low MFN tariff when there are high costs to satisfying rules of origin or other administrative procedures that a trader must follow to qualify for preferential treatment under an PTA. If trade covered by tariffs of 3 percent or less is excluded, the amount of global trade taking place under an economically meaningful tariff preference is around 15 percent.

While the number of PTAs has been increasing, the importance of preferential trade has been falling, reflecting lower tariff barriers, especially in countries belonging to the Organization for Economic Cooperation and Development (OECD). Since 1996, the number of zero duty lines in the EU tariff schedule has increased from 13 to 21 percent of the total number of tariff lines; and the increase has been from 18 to 32 percent for the United States. In 2002 about 45 percent of the tariff lines in the EU and U.S. schedules had duties of 3 percent or less. This reflects the impact of multilateral liberalization under the Uruguay Round agreements and earlier trade rounds. Thus a large and growing proportion of EU and U.S. imports from preferential trade partners is unlikely actually to receive preferential access relative to other countries.[3]

EU Preferential Trade Arrangements

During the 1990s, the European Union had been an active sponsor of bilateral arrangements with individual countries and groups of

Law School; and **Douglas Oberhelman**, group president of Caterpillar Inc., Peoria, IL.

The meeting was chaired by **Clayton Yeutter**, of Hogan & Hartson, and **Harald Malmgren**, of Malmgren O'Donnell Ltd, financial advisers, London and Washington, DC.

About the Meeting

In August 2004, after the WTO General Council's "July package" of framework agreements – without detailed negotiating plans – on agriculture and non-agricultural market access, the prospects for the Doha Round negotiations began to look better.

It looked as if the next problem to be overcome in the negotiations would be the development dimension, for there are serious divisions over special-and-differential treatment, with the many of developing-country proposals on the subject bearing on agricultural trade.

On the one hand, the developing countries are pressing for special-and-differential treatment through (i) preferential access to markets, (ii) relief from reciprocating fully in market-access negotiations, (iii) deferrals or exemptions from some WTO rules and (iv) technical assistance in implementing new WTO agreements. Some of the countries are bent on preserving "policy space" for the future and a number of others worry about "preference erosion" with the prospect of MFN tariffs being further reduced or eliminated.

On the other hand, those familiar with the system point out that the WTO

countries, and was major player in the PTA game. Prior to its Eastern expansion in 2004, taking in ten new members, the Union had bilateral or regional agreements with 111 countries. Trade agreements became an integral instrument of European foreign policy, particularly after the collapse of the Soviet Union.[4]

Three types of agreements were intended to stabilize the region after 1989. *Europe Agreements* were intended to prepare bordering Eastern European countries for eventual accession to the European Union. They involved bilateral agreements among each other and with the Union to reduce tariffs, develop uniform rules of origin, develop EU-consistent regulatory approaches to services and common treatment of standards, as well as transition rules in sectors such as agriculture. These efforts culminated with the full admission of the ten new members in 2004 – which is why the number of PTAs notified to the WTO that year fell for the first time.

Beyond these, *Euro-Mediterranean Agreements* were intended to build bilateral trade relations among neighbors, with the objective of forming a NAFTA-like free trade area by 2010. Launched in 1995, the European Union and twelve countries have been involved in talks on "association agreements" that would subsume some existing bilateral arrangements. To date, bilateral agreements have been signed with Tunisia (1995), Israel (1995), Morocco (1996), Jordan (1997), the Palestinian Authority (1997), Algeria (2001), Egypt (2001) and Lebanon (2002). In general, services liberalization provisions are limited to restatement of GATS commitments with no new liberalization or with preferential access reserved for suppliers based in member countries. Dispute settlement is state-to-state based on *ad hoc* arbitration.

Finally, a third set of *Partnership and Cooperation Agreement*s (PCAs) with the Western Balkans, Russia and the Commonwealth of Independent States (CIS) were designed to help promote stability on the border of the European Union and in the case of Russia expand trade. The European Union has been providing technical assistance to these governments to help implement the institutional reforms that are part of the PCAs.

To these efforts have been added two new twists since 2000.

- *Economic Partnership Agreements* (EPAs) are designed to replace the preferential systems embodied in the Contonou Agreement (the successor to the Lome Convention), which had received a waiver under the enabling clause from GATT Article XXIV, a waiver that expires in 2007. EPAs are designed to promote trade and development in the ACP countries in a WTO-consistent fashion by establishing agreements between large groups of countries forming customs unions (see Box 2.3).

- *Free Trade Agreements* with South Africa (which entered into force in 2000), Mexico (2000) and Chile (2003) are designed

is not a development agency, but a framework of contractual agreements, setting out internationally agreed rules that promote transparency, predictability and stability – important to businesses in conducting international trade and planning [trade-related] investments.

But the trouble, some say, is that WTO rules are often asymmetrical, reflecting conditions in industrialized countries, as with those on subsidies, anti-dumping actions and intellectual property rights.

The most intractable Doha Round issues, namely liberalizing agricultural trade and trade in labor-intensive manufactures, essentially arise out of discrimination by country and by product.

Recent studies at the World Bank show that generalized tariff preferences, in place since the early 1970s, have not significantly benefited developing economies and that today the proliferation of preferential trade arrangements is adversely affecting developing economies as a whole, even if each one may be benefiting the parties directly involved.

The studies were drawn together in the World Bank's Global Economic Prospects 2005, focusing on trade, regionalism and development.

In seeking to
• liberalize trade in agricultural products and light manufactures,
• make sure WTO rules apply equally to all member countries and
• integrate developing countries into the world economy,
the time may have come to restore non-discrimination to its original position as

to open markets and secure trade. Agreements with the Gulf Cooperation Council (GCC) and the Mercado Comun del Sur (Mercosur) are under active negotiation. These embody free trade provisions for a range of products as well as provisions to liberalize at least some services.[5]

The EU agreements govern services trade in addition to trade in goods. The agreements with Mexico and Chile provide for specific liberalization commitments in the financial sector over and above those included in the General Agreement on Trade in Services (GATS), with the Chilean agreement adding telecommunications and maritime services.[6] The South African agreement alludes to possible services liberalization, but only after discussions that are to take place in 2004 and 2005. The EU agreements differ in important respects from the U.S. agreements in that they are generally less comprehensive and do not provide for investor-state dispute resolution.

U.S. Embraces Bilateralism

Prior to the Bush Administration, the United States had generally eschewed reciprocal preferential trade agreements, whether regional or bilateral. The exceptions were Canada and Israel in the 1980s and the North American Free Trade Agreement (NAFTA) in the early 1990s. Indeed, many U.S. trade observers contend that opening the NAFTA talks were designed primarily to support multilateral trade negotiations – to spur the Europeans and others into acting on the Uruguay Round negotiations. Two years later, the Clinton Administration announced its desire to form a Free Trade Area of the Americas (FTAA), although it had been foreshadowed by President G.H.W. Bush, and it signed a free trade agreement with Jordan in 2000.

Since the approval of Trade Promotion Authority in 2002, however, the United States has given much greater emphasis to securing bilateral free trade agreements in tandem with its efforts to achieve multilateral liberalization through the WTO system. Since 2002, the United States has signed bilateral accords with Chile, Singapore, Australia and Morocco, plus Central America/ Dominican Republic and Bahrain. The United States appears to have intensified its pursuit of PTAs since the WTO Ministerial Conference in Cancun in September 2003.

Negotiations are officially[7] underway with Peru, Ecuador, Colombia, the Southern Africa Customs Union (SACU), Panama and Thailand. Other countries deemed to be in the queue are Bolivia, Egypt, South Korea, New Zealand, Pakistan, the Philippines, Sri Lanka, Taiwan (China) and Uruguay.[8] This intensified pace appears designed in part to prod both the multilateral negotiations and the FTAA, as well as to respond to U.S. businesses that fear being shut out of export markets by a growing number of PTAs in which the United States is not a member.

the cornerstone of the multilateral trading system.

Developing countries actively pursue major markets

The launching of NAFTA soon spawned a new flurry of interest among developing countries in using PTAs to secure market access. Mexico and Chile have been at the forefront of these developments. Mexico, having created a world-class trade negotiating team for NAFTA, turned its attention to Central America and other countries in Latin America. It established arrangements with Costa Rica (1995), Bolivia (1995), Nicaragua (1998), the European Union (2000), EFTA (2001) and Japan (2004). After NAFTA was signed, Chile immediately solicited entry into the accord. Rebuffed initially, the country embarked on a wider strategy. Chile established agreements with Mercosur (1996), Canada (1997), Peru (1998), Mexico (1999), Central America (2002), the United States and the European Union (2003), and EFTA (2004). By 2004, Chile had signed free trade agreements that provided over 60 percent of its exports with duty free access to markets around the world.[9]

Many existing regional organizations in Africa also moved aggressively to intensify preferential trade liberalization during the 1990s. For example, the COMESA Treaty, which was signed in 1993 to replace the Preferential Trade Area, called for a free trade area by 2000 and a customs union by 2004. The East African Community was formed in the mid-1990s to accelerate economic integration among three COMESA members (Tanzania, Uganda, and Kenya). The SADC Trade Cooperation Protocol was signed in 1996 as part of an effort to reintegrate South Africa into the regional economy after the end of *apartheid*.

Asian countries have launched similar negotiations since 2001. India has concluded or is negotiating limited arrangements with Mercosur and Thailand, while China has launched bilateral accords with ASEAN countries, to mention a few. In 2004, India, Pakistan and other South Asian countries announced the South Asian Free Trade Agreement (SAFTA), which is intended to encompass all of the countries of the region.[10]

PTAs have increasingly been designed to cover much more than liberalization of tariffs and quotas.

Challenges to Multilateralism

Alan Winters in discussing discrimination rightly expresses several concerns about the proliferation of PTAs:

- PTAs are usually not the first-best policy option to trade policy.
- PTAs hurt excluded countries, if only slightly.
- PTAs tend to reduce incentives to participate in multilateral negotiations

PTAs have increasingly been designed to cover much more than the liberalization of tariffs and quotas.

Let me elaborate on these points, if in reverse order.

Exclusionary consequences of PTAs can impede development

Preferences for some countries mean *discrimination against* others. Indeed, the General Agreement on Tariffs and Trade, born out of the sad experience of discrimination in the inter-war years, was founded on the principle of non-discrimination.

Today the adverse consequences for the excluded countries are much less severe than at the time of the founding of the GATT because tariffs and other barriers have come down sharply, mitigating the exclusionary effects of regional arrangements to all. Another mitigating factor is that many countries excluded by trade agreements between the United States and the European Union enjoy some degree of preferential access through voluntary preference schemes, such as the Generalized System of Preferences (GSP), America's Growth and Opportunity Act (AGOA) and the European Union's Everything But Arms (EBA) program. To be sure, these programs lack the certainty of market access that most-favored-nation agreements and regional trade agreements provide because preferences are voluntary and subject to political whim. But they do mitigate the effects of exclusions for selected, very low-income, countries. Finally, some developing countries – the spokes in the hub-and-spoke analogy – are signing bilateral agreements with each other and with other hubs.

This sanguine view has to be tempered by the fact that, despite low tariffs into rich countries particularly, products that developing countries – especially the poorest -- export tend to face tariff peaks, quotas, or restrictions. One example of non-negligible importance is agriculture. The banana regime for Europe or the case of sugar imports into the United States underscore the importance of the exclusionary costs of preferences.

Inevitably some countries get left out, either because they are not favored politically or because they cannot afford the costs of many separate negotiations, or because their neighborhood is less open. Countries as diverse as Mongolia, Sri Lanka, Bolivia, Pakistan and India do not enjoy the same level of access to the United States or the European Union as Mexico, Jordan or Chile, and see their trade diminished when bilateral agreements are signed. Even a small country such as Chile can displace other countries' exports into preferential markets.[11]

Casual empiricism suggests that, among developing countries, it is the countries of South Asia that suffer the greatest exclusionary effects.

RTAs can undercut incentives for multilateral liberalization
Regional trade agreements may also undercut incentives of governments to press for multilateral trade liberalization, which would otherwise improve global trade rules. But it is easy to overstate this issue. The major actors – and leading developing countries – are well aware that the most significant trade benefits accrue from a multilateral agreement. It seems hard to argue that major players in the current WTO negotiations have so far changed their negotiating positions or retreated from the multilateral process even as they avail themselves of regional trade deals. That said, as the discussions become politically difficult, the risk is ever-present that even they will abandon multilateralism in favor of satisfying regionalism.

Whatever its consequences for multilateral negotiating positions, two consequences are real. One, the major players are clearly engaged in a race to set up preferential trading arrangements around the world and developing countries are now becoming major players. Two, a very real consequence of the spread of regional agreements, however, is that many poorer developing countries have diverted scarce negotiating resources to regional negotiations at the expense of more active participation in the Doha Round negotiations. The average developing country belongs to five separate regional trade agreements and is negotiating more all the time.

A potentially more important problem in the future is the incentive of countries enjoying preferences to fight multilateral or even further regional liberalization to keep their privileged access. A few small developing countries are indeed likely to lose advantages in preferential markets and they may scuttle a deal if their legitimate concerns are not addressed. So far this seems confined to a handful of commodity dependent exporters and textile producers benefiting from the Agreement on Clothing and Textiles.

Challenges for Development

The discussion so far has concentrated on concerns for ways regional and bilateral trade agreements affect developing countries as a group, participants and non-participants alike. For those countries determined to pursue regional strategies, prospective participants should consider ways to integrate PTAs into a more coherent strategy.

Policy Options for Developing Countries

Preferential trade agreements in isolation are not the first best option. In fact, those RTAs with high external border protection are particularly susceptible to the adverse effects of trade diversion. A statistical analysis based on findings from several econometric studies suggests that many agreements cost the economy more in lost trade revenues than they earn because they discriminate against efficient low-cost suppliers in non-member

countries.[12] Of course, this finding does not take into account potential dynamic gains, positive effects associated with services liberalization or any benefits from adopting new regulations. But it does underscore the point that regional agreements carry sufficient risk that they merit close scrutiny of would be participants.

That said, governments everywhere are pursuing them with unprecedented intensity. An argument can be made that PTAs can be a useful complement to both a multilateral strategy and a unilateral strategy of trade policy. Regional trade agreements often are one component of a larger political effort to deepen economic relations with neighboring countries. As such, they can create new opportunities to expand trade through joint action on institutional as well as policy barriers to trade.

At a basic level, it is often easier to motivate reciprocal reductions in border barriers when the number of participants is fewer and policy-makers feel more in control of outcomes. Moreover, regional trade agreements have the flexibility to take up trade-expanding policies not addressed well in multilateral trading rules. Trade agreements therefore usually go beyond slashing tariffs to include efforts to reduce trade impediments associated with standards, customs and border crossings and services regulations, as well as broader rules that improve the overall investment climate. Finally, these agreements often form the cornerstones of larger economic and political efforts at regional cooperation. These agreements can help motivate and reinforce broader reforms in domestic policy. In a wider sense, they could be designed to contribute to a political environment more conducive to stability, investment and growth.

PTAs can only succeed, however, in buttressing wider regional cooperation if they are well designed and purposefully implemented – and in so doing create pro-liberalization business constituencies that support further opening. As noted above, too many are not. The hallmarks of trade expanding agreements include low external MFN tariffs, few sectoral and product exemptions, non-restrictive rules-of-origin tests that build towards a framework common to many agreements, measures to facilitate trade, large ex-post markets, measures to promote new cross-border competition, particularly in services, rules governing investment and intellectual property appropriate to the development context. Neither North-South agreements nor South-South agreements receive universally high marks when measured against these criteria.

Uneven Terms – North-South hub-and-spoke integration

The substantial number of bilateral agreements involving large northern countries, most of which have been signed since 1990, suggests that a hub-and-spoke structure in world trade is emerging. Of the 109 North-South bilateral agreements, 86 have been created since 1990. In a hub-and-spoke trading system, the

largest markets sign individual agreements with a wide range of peripheral countries among which market access remains restricted. Such agreements can marginalize the spokes, where market-access conditions are usually less advantageous than in the hub, which enjoys improved access to all of the spokes. In comparison with a broad preferential trade agreement, a hub-and-spoke approach in theory generates lower gains, which accrue mainly to the hub.[13] Hubs and spokes are already clearly discernible as the European Union and United States extend restrictive rules of origin from one bilateral agreement to another.[14]

PTAs Can Complicate Administrative Procedures

An important feature of the rise in the number of PTAs is the growing number of over-lapping agreements and the so-called "spaghetti bowl" that has emerged from the proliferation of bilateral agreements. The associated myriad of rules strain institutions charged with administering trade agreements. A web of differing trade arrangements can tangle administrative procedures – customs procedures, technical standards, rules of origin, and so on – and so raise costs for both enterprises and governments. This complexity undermines work towards greater trade facilitation in developing countries.

On average, each country belongs to six PTAs, though there is considerable variation across regions and levels of development. East Asian countries join sign fewer agreements than countries in other regions. Northern countries have participated to the greatest extent, each signing on average thirteen agreements. A substantial number of developing countries (45) have signed bilateral preferential agreements with a Northern partner. This activity, however, is not spread evenly across regions. Most activity has been in Eastern Europe, North Africa and Latin America. There are no countries in South Asia that have signed a bilateral agreement with a Northern partner.

Many agreements between country pairs are duplicated by other agreements to which the same two countries are parties. In Sub-Saharan Africa, for example, about one-half of the pair-wise trade relationships covered by a PTA are also covered by another agreement. In other regions, over-lapping agreements also comprise a substantial share of the total number of agreements. There would be significant benefits, in terms of lower administrative costs and more effective implementation, from a rationalization of the current structure of overlapping agreements.

Are Rules Appropriate to All Countries?

US free trade agreements commonly provide market access to partners in exchange for increased access to services markets plus adoption of US-style rules. Among other issues FTAs include new rules for services, investment and intellectual property rights. Other noteworthy provisions include labor protections and

environment issues that figured prominently in the Singapore, Chile and CAFTA agreements, among others.

Signatory countries undertook commitments to enforce their own labor laws in five areas: right of association; the right to organize and bargain collectively; prohibitions on forced labor; a minimum age for employment of children; and acceptable working condition.

Complaints can be filed, and, after agreed procedures to mediate the dispute fail, a panel of experts reviews the case and can, if findings warrant, impose a fine to be used for the enforcement of labor rights; notably, trade sanctions are not an agreed remedy.[15] However, the appropriateness of rules governing investment and intellectual property merit the closest examination.

Investment Access and Protections

The FTAs have incorporated the provisions of bilateral investment treaties (BITs), and in some case provide new measures covering investment. Agreements, especially post-NAFTA ones, include broad definitions of investment, including not only foreign direct investment, but also portfolio flows, private debt and even sovereign debt issues as well as intellectual property.[16] The inclusion of short-term debt, together with pre-establishment rights, led the U.S. Treasury to demand that Chile modify its controls on capital inflows that were designed to curtail destabilizing "hot money" inflows.[17] Such broad definitions expose countries to dispute-settlement proceedings across a range of assets that go far beyond multilateral commitments.

Two issues are important. On the one hand, there is virtually no evidence that providing investors with new protections in bilateral investment treaties actually increases the flow of foreign investment to developing countries.[18] NAFTA did appear to increase investment, but whether that increase was attributable to the new protections or the free trade provisions is unclear. On the other, developing countries are assuming important contingent liabilities through the investor-state arbitration commitments. The rising number of suits under bilateral investment treaties argues that countries should thoroughly discuss remedies in advance. For example, the a tribunal in Stockholm required the government of the Czech Republic to pay one company, Central European Media (CME), $350 million for violation of a bilateral investment treaty that deprived CME of a stake in an English language TV station in Prague.[19] Broad definitions of "investment" expose countries to dispute settlement across a range of assets that go far beyond multilateral commitments.

Intellectual Property Rights

The IPR provisions embedded in all recent U.S. free trade agreements go beyond the multilateral IPRs standards established

in the TRIPS Agreement. These include such diverse provisions as extending copyright protections to author life plus 70 (up from 50 in TRIPS), a requirement to provide patent protection for plants and animals, limitations of the use of compulsory licenses to national emergencies, as anti-trust remedies, and for public non-commercial use, and for pharmaceuticals, restraints on parallel importation (see Annex 1).

Creation and enforcement of intellectual property have an important role to play in development, but neither theory nor available studies provide abundant guidance on the likely outcomes of adopting in trade agreements the strongest of IPRs or none at all. On the one hand, stronger IPR enforcement in general is likely to enhance the overall investment climate, especially for high technology firms. On the other, recognizing full patent protection for firms may require poor countries to pay higher prices, with little additional incentive either to innovate or to make investments in the local market.[20] Full enforcement of patents[21] could produce substantial financial flows, estimated roughly at $19 billion to the United States and $7 billion to Germany.[22] Moreover, administrative costs of upgrading IPRs systems are not trivial.[23]

It was the prospect that developing countries would have to pay higher prices for patented drugs that motivated the international community to agree to clarify flexibilities embedded in the TRIPS Agreement at the WTO Ministerial Conference in November 2001. The resulting Doha Declaration on TRIPS and Public Health reaffirmed the right of WTO members to use the flexibilities of TRIPS in the area of compulsory licensing and parallel importation to "*promote access to medicines for all*".[24] Moreover, in August 2003, WTO members created a special mechanism under the TRIPS Agreement that allows countries with insufficient manufacturing capacity to effectively use compulsory licenses by importing generic drugs.

At first blush, the TRIPS-plus portions of the U.S. free trade agreements seem to circumscribe policy space provided in the Doha Declaration. In particular, provisions on the linkage between patent status and marketing approval, as well as data exclusivity appear to put limits on the spirit of the Doha Declaration, as they may prevent countries from effectively employing compulsory licenses to introduce competition from generic drug producers.[25] To address these concerns, the U.S. bilateral agreements with Morocco, CAFTA-Dominican Republic and Bahrain contain side letters that share understandings that the intellectual property chapters do not affect the ability of governments to "*take necessary measures to protect public health by promoting medicines for all […].*"[26] In other words, if government measures in the four areas outlined above can be justified as protecting public health, they seem to be permitted under the two free trade agreements, even though they may be inconsistent with specific provisions in the agreements' respective intellectual property chapters. This

interpretation was recently confirmed by the General Counsel to the U.S. Trade Representative.[27]

Notwithstanding the important flexibilities provided by these side letters, they raise several questions. How widely will the parties to the three agreements define the "protection of public health" – or, if it comes to it, what definitions would an arbitration panel use? Uncertainty in this respect may become itself a barrier to making use of the flexibilities and may open the door for restrictive interpretations by vested interests. Also, several of the other U.S. free trade agreements do not contain comparable side letters, raising questions about conflicts between intellectual property obligations and public health objectives in at least some of the affected countries.

All in all, this suggests that the general conclusion that countries have to develop an IPR strategy appropriate to their level of development, and then analyze carefully which if any ought to be contained in trade treaties. In general, for some countries, improving other property rights – for example, land rights or small business assets – may be a priority; for others, especially middle income countries. The choice for a particular individual country depends very much on its own characteristics – notably, its level of development, ability to absorb advanced technology, and capacity for enforcement – and the market access that such an agreement would leverage. One size, indeed, does not fit all. From this follows which if any of the IPR provisions should logically figure in regional trade agreements.

Conclusion: Importance of the Doha Round

The policy solution to these twin concerns – the need to design regional agreements that create trade and regional agreements that have minimal exclusionary effects – come together in the form of low MFN tariffs and other border barriers. The first order of business for the international community is to accelerate progress on the Doha Round agenda and to fill in the blanks of the July framework agreement with reductions in protection, especially for products produced by the poor. An agreement that lowers border protection around the world promotes open regionalism by mitigating trade diversion. It simultaneously would mitigate the exclusionary effects of discriminatory preferences built into regional agreements.

Minimizing the discriminatory effects of regional trade agreements at the multilateral level requires all countries to assume greater responsibility for the maintenance of the multilateral trading system. The international community, working through the World Trade Organization, should revisit Article V of its charter. If the stated disciplines cannot be enforced in the near term for collective political reasons, then – as a minimum first positive step – increasing transparency and information should become a priority. At present, the WTO collects little if any information on updating

specific provisions, their implementation and the trade consequences. It fails even to take advantage of extant public monitoring efforts in specific regions that could inform their data collection effort. Collecting and publishing specific information on regional trade agreements would allow members that find themselves excluded to challenge these agreements in the court of public opinion. Even the more modest goal of transparency will require building a new consensus and providing the staff of the WTO with more resources than are currently available.

Annex
U.S. FTAS: Selected Elements of Behind-the-Border Rules

Key components of dealing with services and investment include:

- Opening services markets to competition from foreign suppliers – or locking in prior autonomous liberalization – except in those sectors excluded (a negative list). Since most of the countries with which the US has concluded bilateral FTAs are already open in most sectors, as a general statement the agreements lock in prevailing openness and effect changes in only a few still-restricted activities. Significant market openings took place in the Costa Rican telecommunications and insurance sectors, and less dramatically the banking sector in Bahrain. Provisions range from inclusion of insurance, financial advisory services, and selected telecommunications services to arguably relatively minor changes to already open regimes, such as the commitment of Singapore to cease cross subsidies in express mail delivery or the commitment of Chile in insurance services and a few other sectors.

- All agreements contain ratchet provisions and negative list exclusions. The ratchet clauses mean that new autonomous liberalization will automatically be subsumed under the terms of the agreements. Negative lists ensure that yet-to-be-invented new service areas are guaranteed to be covered by the treaty. Notable for their absence is the exclusion of labor services, except provisional visas for professionals associated with investing firms.

- Investment rights, with provisions for national treatment, non-discrimination, pre-establishment provisions for companies based in each others markets, bans on trade-related investment measures (TRIM), and investor-state arbitration of dispute limited only by a negative list of exclusions;
- All agreements provide for treatment of foreign investors on the same footing as domestic investors (*national treatment*) and have provisos banning discrimination among investors from member countries (*MFN treatment*). For many of the

initial FTA countries, these had long been included in national legislations and/or have been incorporated into bilateral investment treaties, mainly on a post-establishment basis.

- What is new is the extension of the *pre-establishment* right to invest in businesses and activities in all sectors, except where expressly prohibited via a negative list. These pre-establishment rights lock in the right of Mexican and Canadian investors under NAFTA to invest in all activities in the US. Exceptions for the US include foreign investment with NAFTA guarantees in selected areas of communication, media, transportation and social services. Pre-establishment rights mark a broad expansion of market access by foreclosing future government policies that would raise barriers to foreign investment. The rationale for accepting such disciplines is that it provides certainty on the rules of the game that will in turn translate into increased investment inflows.

- Another area of disciplines on government that is more expansive than multilateral accords is in *trade-related investment measures (TRIMs).* The WTO TRIMs agreement of 1995 attempted to clarify disciplines on government policies that require foreign companies to establish joint ventures, export in a certain portion of its sales or balance trade, use local inputs to achieve value-added objectives, or local hiring requirements. However, the agreement failed to provide adequate definitions of disciplines, poorly formulated implementation periods, and inadequate notification and monitoring procedures; the operation of the agreement was to be reviewed by January 1, 2000, but so far the review has not occurred. [28] All of the bilateral FTAs ban in some form trade-related investment requirements, such as local content rules, value-added requirements, and restrictions on management. The US bilateral agreements have, in effect, established a "TRIMs Plus" set of obligations that include outright bans on certain performance requirements, including exports, minimum domestic content, domestic sourcing, trade balancing and technology transfer. In general, exempt are government procurement, environmental standards, some health measure, and requirements for local R&D. [29]

The **mockingbird** is the state bird of Tennessee.

- Freedom to make transfers is a nontrivial investment right granted under the investment agreements. This assures investors that they will be able to transfer profits, make investments or lend without government interference.

- Finally, all but the Australian FTA create an *investor-state dispute resolution* provision that permits investors to take foreign governments to dispute resolution for violation of the treaty's national treatment, nondiscrimination or expropriation provisions, among others. NAFTA's Chapter 11

Cordell Hull represented a district of Tennessee in the Congress of the United States, and was elected a senator from there, before becoming U.S. Secretary of State (1933-44).

"The mockingbird is known for fighting for the protection of his home – falling, if need be, in its defense. Mockingbirds are not intimidated by animals larger than themselves and have been known to attack eagles"

– Diana Wells, *100 Birds and How They Got Their Names* (Chapel Hill, NC: Algonquin, 2002)

Trade Policy Analyses

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and Chile's Chapter 10 are the most widely known mechanisms,

but these mechanisms are also contained in the other bilateral agreements as well.

Key Elements of U.S. FTA TRIPS-Plus Provisions

"TRIPS-plus" elements found in many—but not all—of the IPRs chapters include: [30]

- Extension of the patent term for delays caused by regulatory approval processes; extension of the term of copyright protection to life of author plus 70 years (compared to life of author plus 50 years in TRIPS).

- A requirement to provide patent protection for plants and animals.

- A limitation of the use of compulsory licenses to national emergencies, as anti-trust remedies, and for public non-commercial use.

In the area of pharmaceuticals:

- An obligation to prohibit marketing approval of generic drugs during the term of the drug patent.

- A five year period of marketing exclusivity following the submission of safety and efficacy data to drug regulatory authorities (so-called 'data exclusivity'). In addition marketing exclusivity is given extra-territorial effect, so that marketing approval in one market—say, the United States—prevents registration of competing products in another market.

- An additional three year period of marketing exclusivity based on the submission of new clinical data regarding new uses of previously approved drugs. This would also apply to drugs for which the patents have expired (although generic competition for previously approved uses would remain unaffected).

- Imposition of restraints on parallel importation, foreclosing the possibility that parties to the agreements open their markets to the import of products that have already been sold—possibly more cheaply—in foreign markets.

In the area of digital works:

An obligation against circumventing so-called technological protection measures—devices and software developed to prevent

unauthorized copying of digital content. Rules on the liability of internet service providers (ISPs) when copyright infringing content is distributed through their servers and networks. These provisions are based on standards found in the U.S. Digital Millennium Copyright Act of 1998.

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[1] This paper draws on Global Economic Prospects and the Developing Countries 2005 (Washington, DC: World Bank, 2004).

[2]Here are covered only reciprocal agreements. Trade under the Generalized System of Preferences, the Cotonou Agreement and AGOA is excluded.

[3] Some of the PTAs have never been reported to the WTO, for any of several reasons. One is that the WTO does not enforce notification (notification of PTAs is not unique in this regard, the same is true of notification requirements in other WTO agreements). Another is that several countries that have yet to join the WTO have been quite active in forming PTAs. Russia, for example, is in the process of joining the WTO and has signed bilateral FTAs with other members of the Commonwealth of Independent States (CIS). It is also pursuing two regional arrangements that are to become customs unions: the Euro-Asian Economic Community and the Single Economic Space. Because of the lack of a consistent data source that covers all PTAs, data are based on the information contained in the WTO database, supplemented by data from the major unreported agreements.

[4] For this formulation, I am indebted to Gaspar Fontini of the Directorate-General for Trade, European Commission, Brussels.

[5] Heidi Ulrich, "Comparing EU Free Trade Agreements: Services", ECDPM In Brief, forthcoming (2004).

[6] *Ibid*

[7] The United States Trade Representative is required to officially notify the U.S. Congress of its intent to negotiate free trade agreements.

[8] Jeffrey J. Schott, "Free Trade Agreements: Boon or Bane of the World Trading System", in J.J. Schott (ed.), *Free Trade Agreements: US Strategies and Priorities* (Washington: Institute for International Economics, 2004).

[9] Robert Devlin and Antoni Estevadeordal, "Trade and Cooperation: a Regional Public Goods Approach", in Estevadeordal, Brian Franz and Tam R. Nguyen (eds), *Regional Public Goods: From Theory to Practice* (Washington, DC: Inter-American Development Bank and Asian Development Bank, 2005).

[10] Tercan Baysan, *South Asia: Lessons and the Way Forward* (Washington, DC: World Bank, 2004); and Richard Newfarmer, "SAFTA: Promise and Pitfalls of Preferential Trade Arrangements", background paper for *Global Economic Prospects 2005*, World Bank, Washington, May 2004.

[11] Glenn Harrison, Thomas Rutherford and David Tarr, "Trade Policy Options for Chile: The Importance of Market Access", *World Bank Economic Review*, Washington, DC, Vol. 16, No. 1, 2002.

[12] Devlin and Estevadeordal, "Trade and Cooperation: A Regional Public Goods Approach", *op. cit.*; and Maurice Schiff and L. Alan Winters, *Regional Integration and Development* (Oxord and New York: Oxford University Press, for the World Bank, 2003).

[13] Ronald J. Wonnacott, "Trade and Investment in a Hub-and-Spoke System Versus a Free Trade Area", *The World Economy*, Oxford and Boston, Vol. 19, No. 3, May 1993, pp. 237-52.

[14] The provision for regional cumulation in the rules of origin, particularly full cumulation, will tend to offset the hub-and-spoke system. See Paul Brenton and Hiroshi Imagawa, "Rules of Origin, Trade and Customs", in L. De Wulf and J. Sokol (eds), *The Customs Modernisation Handbook* (Oxford and New York: Oxford University Press, for the World Bank, 2004). The European Union, following substantial criticism of the hub-and-spoke system that emerged in the late 1990s, moved to create pan-European cumulation, although in terms of the more limited partial cumulation.

[15] Sidney Weintraub, "Lessons from the Chile and Singapore Free Trade Agreements", in Schott (ed.), *Free Trade Agreements: US Strategies and Priorities* (Washington, DC: Institute for International Economics, 2004).

[16] Howard Mann and Aaron Cosby 2004. "International Investment Agreements: Trends and Impacts for Developing Countries", background paper for *Global Economics Prospects and the Developing Countries* 2005, World Bank, Washington, DC, June 2004; and David Vivas-Eugui, *Regional and Bilateral Agreements and a TRIPS-plus World: the Free Trade Area of the Americas*, TRIPS Issue Papers No. 1 (Geneva: Quaker United Nations Office, 2003).

[17] According to the agreement, if Chile chooses to impose restrictive measures on capital flows it considers speculative, then special dispute settlement rules will apply.

[18] Richard Newfarmer, *From Singapore to Cancun: Investment*, Trade Note No. 2 (Washington, DC: World Bank, 2002).

[19]Luke Peterson, "Czech Republic Hit With Massive Compensation Bill in Investment Treaty Dispute", *Invest-SD News Bulletin*, International Institute for Sustainable Development, Geneva, March 21, 2003.

[20] J. Michael Finger and Philip Schuler, *Poor People's Knowledge*: *Promoting Intellectual Property Rights in Developing Countries* (Oxford and New York: Oxford University Press, for the World Bank, 2004).

[21] In this sense, full enforcement is equivalent to a TRIPs standard. See Keith Maskus, *Intellectual Property Rights in the Global Economy* (Washington, DC: Institute for International Economics, 2000).

[22] Global Economic Prospects and the Developing Countries 2002 (Washington, DC: World Bank, 2001), p.137.

[23] Finger and Schuler, *op. cit*.

[24] See paragraph 4 of the Doha Declaration on TRIPS and Public Health, available at http://www.wto.org.

[25] Technically, the Doha Declaration does not address questions of marketing approval during the patent term and test data exclusivity. But the provisions of the bilateral free trade agreements in these areas can still be seen as being at odds with the spirit of the Doha Ministerial Declaration, to the extent that they preclude the effective use of compulsory licenses.

[26] See the side letters to the US-Morocco and US-Dominican Republic-CAFTA agreements. The side letters explicitly make reference to "*HIV/AIDS, tuberculosis, malaria, and other epidemics as well as circumstances of extreme urgency or national emergency*". The language chosen, however, mirrors similar wording in the Doha Declaration on TRIPS and Public Health, suggesting that this list of diseases is illustrative rather than limiting. The side letters also clarify that the intellectual property chapters of the FTAs do not prevent the effective utilization of the August 2003 Decision by WTO members described in the text.

[27] See the letter from USTR General Counsel, John K. Veroneau, to Congressman Levin dated July 19, 2004.

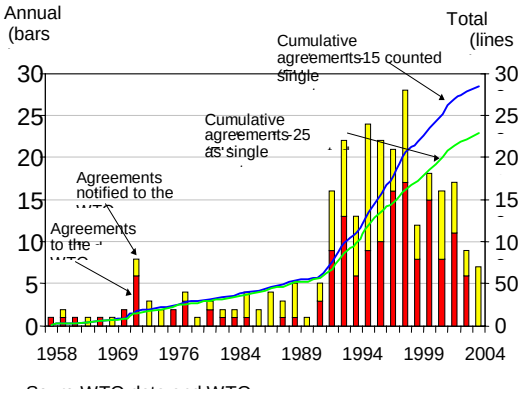
[28] Bijit Bora, *The Agreement on Trade Related Investment Measures, 1995-2002*, Discussion Paper Series No. 15 (Geneva: UNCTAD, 2003).

[29] Dirk te Velde and Miatta Fahnbulleh, *Investment-Related Provisions in Regional Trade Arrangements* (London: Department for International Development, British Government, 2003).

[30] Carsten Fink and Patrick Reichenmiller, "Tightening TRIPS: the Intellectual Property Provisions of Recent US Free Trade Agreements", background paper for *Global Economics Prospects and the Developing Countries 2005*, World Bank, Washington, DC, 2004.

PTAs in pictures

PTAs are



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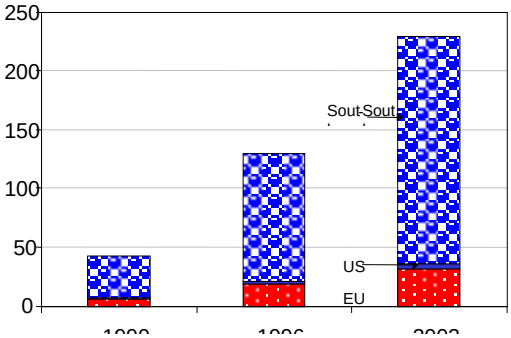

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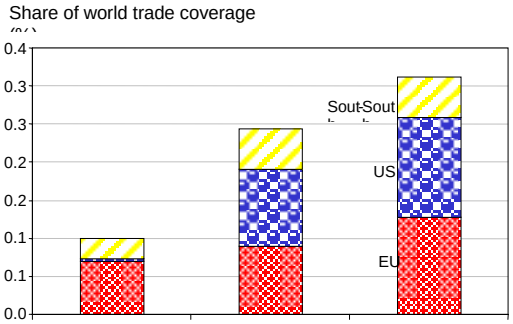

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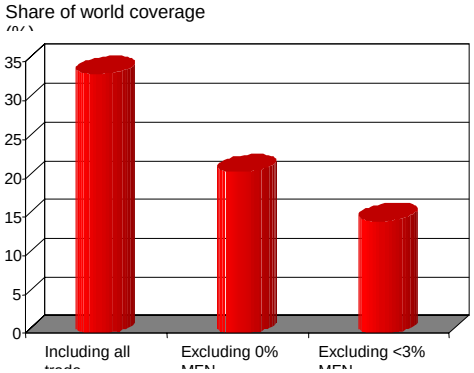
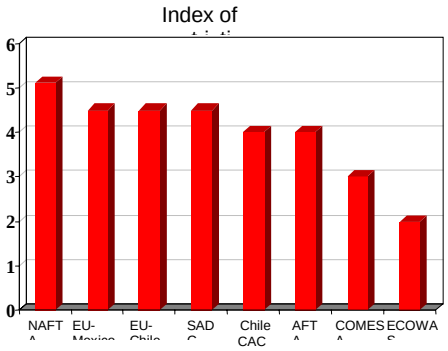


Rules of origin in -South agreements are restrictive than in -South



Note: Higher values of the index equals to more of origin (derived Estevadeordand Suomine2004

Multiple agreements complicate customs

Overlapping agreements in