



## CHAPTER 19

# LEGAL ASPECTS OF FREE TRADE AGREEMENTS: IN THE CONTEXT OF ARTICLE XXIV OF THE GATT 1994

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### I. RECENT DEVELOPMENTS OF FTA AND RTA AGREEMENTS

About 90% of the Members of the WTO are participants of FTA and RTA (customs union and free trade areas)<sup>1</sup>. In the year 2000, the four FTAs (the EU, the NAFTA, the MERCOSUR and the ASEAN) occupied 64.5.4% of the total export trade and 69.5% of the total import trade of the world.<sup>2</sup> This fact presents a challenge to the WTO and the multilateral trading system. Proliferation of bilateral and regional agreements may cause erosion of the disciplines of the WTO and thereby the effectiveness of the multilateral trading system may be weakened. But given the fact that there are more than 130 of such agreements and such agreements include important entities such as the European Union, the NAFTA, and the MERCOSUR, the WTO needs somehow to co-exist with them. The core issue is how to recognize the existence of FTA arrangements and yet to exert some disciplines on them so that they would not undermine the WTO principles<sup>3</sup>.

The proliferation of FTA may be attributed to difficulty in the multilateral negotiations conducted at the WTO. Now that WTO negotiations must focus more and more on sensitive issues such as trade and environment, intellectual property rights and epidemics (HDP-Aids, malaria and tuberculosis etc), trade and investment and trade and competition policy and that developing countries are the majority of the Members of the WTO, to reach consensus on a multilateral basis is becoming increasingly difficult.

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<sup>1</sup> For the sake of brevity, the term "FTA" is used in this article to include both FTA/RTA free trade area and customs union.

<sup>2</sup> 2002 Report on the WTO Consistency of Trade Policies by Major Trading Partners (Industrial Structure Council, METI, Japan 2002), p. 488

<sup>3</sup> Some systemic issues with regard to the relationship between the WTO disciplines and FTAs/RTAs are extensively discussed in Synopsis of "Systemic" Issues Related To Regional Trade Agreements, WT/REG/W/37, 2 march 2000.



FTA may be an easy substitute for a more difficult multilateral arrangement. Often nations in close geographical proximity share common interests. There may be common elements in culture, religion, language, history, social and economic system among such nations. Members of the EU share such common heritages to a more or less degrees. Although nations are not geographically close to each other, they may share some common interests. For example, Japan and Mexico are far away from each other geographically. But Japan is interested in establishing an economic relationship with Mexico so that Japanese enterprises can enjoy a reduction of tariff with respect to exporting to the Mexican market and more importantly gain access to the NAFTA market while Mexico may be interested in diversifying its trade connections and thereby reduce an excessive dependence on the U.S. and North American Market. Because of these and other reasons, one has seen an explosion of FTA in the recent years.

In East Asia where there has not been many FTA compared with the North America, Europe and others where many FTA have been concluded and implemented. Until quite recently, Korea and Japan were the only two industrialized trading nations in East Asia which had not entered into bilateral and regional agreements. Of course, the APEC has been active in Asia and Japan and Korea as well as many other countries (such as China, U.S., Canada and Chile) are Members. However, the APEC should be regarded as a "framework for cooperation" rather than a FTA agreement. There are no binding obligations in the APEC. Members are expected to engage in liberalization of trade and investment on a voluntary basis as illustrated by such catchwords as "open regionalism" and "concerted unilateralism". Therefore, the APEC raises little problems with the WTO.

However, recently there is a trend toward FTA in East Asia. Japan has concluded a FTA agreement with Singapore<sup>4</sup> and Korea and Japan will be negotiating a FTA agreement in near future<sup>5</sup>. This trend is partly

<sup>4</sup> For a detailed study of this agreement, see Rajan, Sen & Siregar, *Singapore and Free Trade agreements: Economic Relations with Japan and the United States*, Institute of Southeast Asian Studies, 2001

<sup>5</sup> With respect to a FTA between Korea and Japan, a taskforce composed of Korea and Japanese business persons was established in 2001. This taskforce (Nikkan Business Forum (The Korea/Japan Business Forum)) submitted its report to the President of the Republic of Korea and the Prime Minister of Japan in February 2002 in which it recommended that both governments consider an initiation of negotiation which is aimed at concluding a FTA agreement between Korea and Japan. In response to this recommendation, both governments established a study group composed of experts and this study group will complete its study in two years.

due to disillusionment about the multilateralism as embodied in the WTO which arose when the Ministerial Conference in Seattle broke down in 1999. In light of this new trend, the relationship between Article XXIV of the GATT 1994 and FTA will be an important issue for Korea, Japan and other East Asian nations.

Although there is a risk that a spread of FTA may undermine the basis for the multilateral trading system, there are advantages of FTA. Compared with multilateral trade negotiations, a bilateral and regional trade negotiation for the conclusion of FTA is generally easier. If a FTA is successful, the trade in the areas covered by the FTA is liberalized and this liberalization promotes economic development of the region. Economic prosperity achieved by the FTA provides a greater opportunity for enterprises outside the region to trade with the region and invest in it. An important task for the WTO and FTA is to maximize the benefit of FTA while minimizing the negative effects of them.

Therefore, an important task for Members of the WTO is to ensure that WTO disciplines are effectively applied to prevent FTA from being too exclusive and discriminatory in relation to outside parties. As discussed later, Article XXIV of the GATT allows FTA on the condition that certain requirements as specified in that article are complied with. The meaning of Article XXIV is by no means clear and amenable to different interpretations. However, a more clarification of the key concepts of Article XXIV is needed today.

With this situation in view, an attempt will be made below to analyze problems of interpretation of Article XXIV of the GATT 1994. Similar issues may arise in connection with the General Agreement on Trade in Services (the GATS). However, unlike the GATT 1994, the GATS takes a gradual and evolutionary approach toward liberalization of trade in services. Members of the WTO are basically obligated to liberalize trade in services to the extent that they have made commitments to liberalize. Also there has been no precedent in the WTO Dispute Settlement Body and elsewhere in which WTO bodies touched on the relationship between the GATS and FTA. For this reason, this article will omit an analysis of the relationship between FTA and the GATS and concentrate on that between FTA and the GATT 1994.

## II. WTO DISCIPLINES AND FTA

Article XXIV of the GATT 1994 is the basic provision on FTA in the WTO regime. This Article was incorporated into the GATT system when the GATT came into being in 1947. At that time, there were something similar to FTA such as the British Commonwealth in which preferential tariffs existed among the Members. Therefore, the framers of the original GATT felt it necessary to allow a room for preferential arrangements such as the British Commonwealth while imposing a sufficient degree of discipline on the formation of FTA. To deal with such situations, Article I:2 and Article XXIV of the GATT 1947 were incorporated.

More recently, however, FTA spread much more widely than the framers of the original GATT envisaged. FTA have grown out of a narrow area in which they were to operate as contemplated by the framers of the GATT 1947.

Globalization is progressing at an unprecedented speed and this requires trading nations to take a global view in regard to trade issues. This necessitates a multilateral approach as incorporated in the WTO. However, as touched upon earlier, trade negotiations at the WTO are slow and often frustrated by divergent views between developed nations and developing nations and sometime even among developed nations and among developing nations. This prompts trading nations to incline toward bilateralism and regionalism. Looking at the situation as a whole, the world economy stands in the midst of those currents which often go against each other.

As seen before, trade negotiations may begin between Korea and Japan to conclude a FTA agreement. Both Korea and Japan are Members of the WTO and the Japanese government has repeatedly pledged that Japan will comply with the requirements of Article XXIV of the GATT 1994 when it enters into FTA agreements with other nations. Therefore, it is essential that Japan as well as Korea carefully review the requirements of Article XXIV of the GATT 1994 and make sure that a FTC which may be concluded between those two nations do not run counter to the WTO principles.

## III. KEY PROVISIONS OF ARTICLE XXIV OF THE GATT 1994 IN RELATION TO FTAs

The essential element of FTA is the preferential treatment for participants in the way of tariff elimination and of other trade and

investment restrictions. Therefore, inevitably some forms of exclusivity is a feature of FTA. Although the WTO permits a degree of deviation from the principles such as the MFN principle and the national treatment principle with regard to FTA, there should be a limit to exclusivity which accompanies the formation of a FTA so that its restrictive features would not unnecessarily distort the multilateral trading system.

The key substantive provisions of the GATT 1994 are Article XXIV:4, Article XXIV:5 (a), (b) and (c), Article XXIV:6, and Article XXIV:(a) (i), (ii) and (b).

Article XXIV:4 declares a general principle 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.

Article XXIV:5 sets out the conditions under which FTA can be formed. Article XXIV:5 (a) provides that a customs union can be formed if the duties or other regulations imposed at the institution of such union with regard to commerce with outside parties shall not on the whole be higher or more restrictive than those applicable prior to the formation of such union. Article XXIV:5 (b) provides the same conditions with regard to a free trade agreement.

Article XXIV:6 states that, if a Member increases tariffs above the concession rate as a result of forming a customs union, it negotiate with other Members outside the union under Article XXVIII of the GATT 1994.

Article XXIV:8 defines customs unions and free trade areas. Article XXIV:8 (a)(i) states that a customs union is an entity in which duties and restrictions of commerce are eliminated with respect to substantially all the trade between the members of the union except those restrictions permitted under Articles XI, XII, XIII, XIV, XV and XX. Article XXIV:8 (a)(ii) states that a customs union establishes common tariffs and other restrictions of commerce with respect to commerce with Members that are outside parties to the union. Article XXIV:8(b) provides the same requirements with respect to a free trade area except for the fact that there is no requirement equivalent to (ii) which applies to a customs union.

In the past, there were many instances in which working parties were established to examine compatibility of FTA with GATT/WTO disciplines under Article XXIV of the GATT. However, in almost all of

such working parties, there was a sharp difference of views regarding compatibility of a FTA with GATT/WTO rules and, in the reports of those working parties, usually there are two opposing views listed side by side. One advocates that a FTA is compatible with GATT/WTO rules and other criticizes the FTA as not compatible with GATT/WTO rules.<sup>6</sup>

The issue of how to interpret Article XXIV in relation to FTAs was raised first when EEC Treaty was negotiated in 1957. Since that time until 1994, 69 working parties were established to examine compatibility of FTAs under GATT rules but, in only 6 out of 69 working parties, a consensus was reached.<sup>7</sup> The reason for this poor accomplishment is conflicting interests among Members. Those which formed a FTA advocate their interests in maintaining it and those outside the FTA criticize it. In part, the difficulty is the vagueness of the text of Article XXIV such as "substantially all", "other trade restrictions" and "on the whole". Only 3 panels were established to examine the legality of FTA in light of Article XXIV but, in all of them, the panel reports remain unadopted.<sup>8</sup>

#### IV. UNDERSTANDING ON THE INTERPRETATION OF ARTICLE XXIV OF GATT 1994

Attempts were made to clarify meanings of Article XXIV of the GATT 1994 in the Uruguay Round. As the result, a limited number of issues were clarified.

- (a) (i) The level of tariffs should be calculated by using weighted average rates.
- (ii) The period for the completion of FTA is in principle 10 years.
- (iii) When a member of a customs union raises tariff above the concession rate as a result of joining the customs union, that member negotiate with outside WTO Members in accordance with XXVIII of the GATT 1994.
- (vi) An outside Member which enjoys the reduction of tariffs due to the joining of a member in a customs union is under no obligation to offer compensation.
- (v) omitted

<sup>6</sup> See note (1), *supra*, p. 495.

<sup>7</sup> Id.

<sup>8</sup> Id.

(b) Article 4.3 of the Antidumping Agreement

When the degree of integration of a customs union has reached the level as provided for in Article XXIV:8 (a), the totality of an industry in the region covered by the customs union is deemed to be a domestic industry.

(c) The principle of (b) applies to CVD.

(d) Article XXI:1, footnote

No provision in Article XXIV of the GATT 1994 prejudices interpretation of the relationship between Article XIX of GATT and Article XXIV:8 of the GATT 1994.

(e) Omitted

**V. THE RELATIONSHIP BETWEEN ARTICLE XXIV:4 AND ARTICLE XXIV:5-9**

Article XXIV:4 announces general principles and Article XXIV:5-9 provide for specific requirements. A question is what is the relationship between Article XXIV:4 and Article XXIV:5-9. In particular, a question is whether the requirement of Article XXIV:4 is satisfied as long as the requirements provided for in Article XXIV:5-9 are fulfilled. If the answer is yes, then all that is required is to fulfill the requirements of Article XXIV:5-9 and Article XXIV:4 does not give an independent cause of action. If the answer is no, there can be a cause of action under Article XXIV:4 even if all of the requirements in Article XXIV:5-9 are satisfied.

The EU has maintained that, as long as the requirements provided for in Article XXIV:5-9 are satisfied, the requirement of Article XXIV:4 is automatically satisfied and, therefore, Article XXIV:4 does not give any independent cause of action. In particular, the EU has maintained that, although a new restriction is created by the formation of a customs union in respect to each independent measure, there is no increase of trade barriers in relation to outside countries as prohibited in Article XXIV:4 as long as there is no increase of the level of protection as provided for in Article XXIV:5 (a).

Others, however, maintained that, if a particular new trade measure is applied as a result of the formation of a customs union, that



new measure constitutes an increase of trade barriers prohibited by Article XXIV:4 and, therefore, this is an independent cause of action under Article XXIV:4 regardless of whether the requirements of Article XXIV:5-9 are satisfied. The gap between those two positions has not been narrowed and this remains to be one of the issues of interpretation of Article XXIV. It is to be noted, however, that the term “should” is used in Article XXIV:4 and this may be an indication that Article XXIV:4 provides only for general principles of interpretation and is hortatory in nature.

**VI. THE MEANING OF “SUBSTANTIALLY ALL” – THE INTERPRETATION OF ARTICLE XXIV:8 OF GATT 1994**

Article XXIV:8 states that “substantially all of trade” must be liberalized if a customs union or a free trade area is qualified to meet the requirements for exemption under Article XXIV. A question is what is “substantially all”, i.e., what is the rate of liberalization of internal trade of a FTA to meet the requirements and whether it is a quantitative requirement only or a quantitative and qualitative requirement. If it is merely a quantitative requirement, there is room to interpret this to mean that “substantially all” is satisfied even if, for example, agricultural sector of a customs union or a free trade area is not liberalized as long as the trade of the customs union or the free trade area is quantitatively liberalized on the whole. For example, the portion of import of agricultural products from Korea to Japan is about 10 % of the total imports from Korea to Japan. If the 90 % quantitative test is adopted, this may mean that the exclusion of agricultural sector is justified as long as other sectors are totally liberalized.

However, if the test is a qualitative as well as quantitative one, a mere fact that the trade of a member country is liberalized as the whole is not sufficient for the customs union or free trade area to be qualified to be exempted under Article XXIV if a particular sector (for example, agriculture) is not liberalized. In this view, the total exclusion of Korean import of agricultural products to Japan is not justified. .

This question was raised many times even before the coming into being of the WTO in 1995. This question was raised once in connection with the EFTA (the European Free Trade Association) when the Treaty of Stockholm exempted agriculture from the liberalization. In the Working Party, there was a view that “substantially all” should be interpreted to

have not only quantitative but also qualitative features. This view maintained that even if the rate of liberalization of internal trade reached 90 % quantitatively, this should not be regarded as an automatic approval of the FTA<sup>9</sup>. The representatives of the EFTA maintained that Article XXIV of the GATT 1947 allowed some restrictions with regard to products by providing that “substantially all of trade” instead of “substantially all products.” Although no consensus was reached in this Working Party, the prevailing view was that at least both qualitative and quantitative tests should be used.

Another Working Party which examined the EEC-Finland Free Trade Agreement in 1973 took the view that the “substantially all” test should be interpreted to liberalization of all products and should not be interpreted to allow an exemption of a particular sector of the economy in its entirety<sup>10</sup>. In this view, to exempt the entire sector of the economy from liberalization would be contrary to Article XXIV of the GATT no matter what the quantitative coverage of this sector may be in the total trade. The Preamble of the Understanding on the Interpretation of Article XXIV of the GATT 1994 endorses this view by stating that if main areas of trade are exempted from the obligation to abolish restrictions, the contribution of FTA toward liberal trade is reduced.

The Working Party which reviewed the U.S./ Canada Free Trade Agreement took a positive view with regard to the Agreement for the reason that this did not attempt to exclude the agricultural sector as the whole from liberalization although some Contracting Parties expressed skepticism to the Agreement since some specific agricultural products (such as fresh fruits, vegetables, corn and corn products, eggs, and milk products) were exempted<sup>11</sup>. In those Working Parties, a focus of discussion was the treatment of agricultural sectors and products.

In view of this, the WTO Secretariat issued a report in 1998 in which it examined 69 FTA and RTA agreements and stated that 56 FTA agreements excluded some agricultural products and, in 2 FTA agreements, all of agricultural products were excluded<sup>12</sup>. As one can see from this finding, agricultural issues are an “Achilles Heel” for the WTO and FTA. However, this is a hurdle that the WTO will have to overcome if a sound relationship between the WTO and FTA is to be established.

<sup>9</sup> BISD, 9S/84-85

<sup>10</sup> BISD, 21S/79

<sup>11</sup> BISD, 38S/73

<sup>12</sup> WT/REG/W/26



The Japanese government has taken the position that, at the minimum, tariff should be eliminated with regard to 90% of trade within the area and no specific sector should be exempted from the liberalization. In the agreement between Japan and Singapore, it is provided that tariff is eliminated with regard to 98% of trade between the two countries. There is no block exemption from this liberalization of any sector, not even agricultural and marine products. It is to be noted, however, that there is little exports of agricultural and marine products from Singapore to Japan and, in this sense, this is not a real issue between the two countries. A real challenge will come when the governments of Korea and Japan negotiate a FTA since there are substantial agricultural products and marine products (such as sea weed products) in Korea which can be exported to Japan and strong oppositions agricultural groups in Japan are anticipated.

**VII. THE TEST OF “SHALL NOT BE ON THE WHOLE HIGHER OR MORE RESTRICTIVE THAN BEFORE”**

Article XXIV: 5(a) requires that tariffs and other trade restrictions imposed by a FTA to outside parties shall not on the whole be higher or more restrictive than those before the formation of the FTA. With regard to tariffs, this requirement seems to be fairly straightforward. Article 1 (a) (I) of the Understanding on Interpretations of Article XXIV of the GATT 1994 provides that, for the purpose of Article XXIV: 5(a), the weighted average rate should be used. The words “on the whole” seems to suggest that the weighted average level of tariffs of the members of a FTA before the formation of the FTA can be compared with the average of tariffs which resulted from the formation of the FTA.

This requirement, however, may cause a difficult problem of interpretation with regard to “other trade restrictions”. Especially difficult is the treatment of rules of origin. One of the questions in this regard is whether or not rules of origin are “other restrictions”. Although there are views that rules of origin should be regarded as restrictions of trade, there are strong opposition to it also. In the Working Party which examined the compatibility of the NAFTA with GATT rules, the United States argued that rules of origin are not trade restrictions in the same sense as tariffs and quantitative restrictions are<sup>13</sup>. In this view, rules of origin are a test by which to determine which product benefits from the preferential treatment of a FTA but not a trade restriction in itself. It is true that rules

<sup>13</sup> WT/REG/M2 (February 21, 1997), p. 10

of origin do not erect barriers such as tariffs and quantitative restrictions. At the same time, it is a common knowledge that rules of origin is a very important trade issue and may operate as *de facto* trade restrictions.

In the Uruguay Round Negotiation, negotiators tackled the issue of whether or not rules of origin were “other restrictions”. However, they were unable to reach any conclusion as to whether they were or were not “other restrictions”<sup>14</sup>. No panel or Appellate Body reports have clarified this issue. Therefore, this remains unresolved.

If rules of origin are “other restriction of trade” in the sense of Article XXIV, there is still a problem. Article XXIV:5 (a) requires that tariffs and other trade restrictions after the formation of a FTA shall not be higher or more restrictive than those before its formation. The question here is: What is “before”? If an existing FTA is enlarged to another FTA (such as the transformation of the U.S./ Canada Free Trade Agreement into the NAFTA), the answer may be a comparison between the common rules of origin at the time of the U.S./Canada Free Trade Agreement with that of the NAFTA. However, what if a new FTA is entered into? There were no common rules of origin before. The common rules of origin were created only after the formation of the FTA. Then the question is what rules should be compared with what rules. Should the common rules of origin be compared with those of each Member at the time before the formation of the FTA? However, a Member may have exercised “tariff classification rule” while others may have exercised “the substantial transformation rule”. This would make it very difficult to compare situations before and after.

Questions such as above still remain unanswered. Definitive rules of origin are still not determined by the WTO bodies yet. This question may have to be discussed in connection with future negotiations on rules of origin at the WTO and the answer may have to await until this is completed.

In the Uruguay Round Negotiation, negotiators discussed the issue of rules of origin in the context of FTA. However, the only result was to state that there be transparency in the enforcement of rules of origin in FTA. Other issues are left to future negotiations and clarifications.

<sup>14</sup> Background Note by the Secretariat, Systemic Issues Relating to “Other Regulations of Commerce,” WT/REG/W17 (October 31, 1997)

**VIII. THE TRADE REMEDIES – THE RELATIONSHIP BETWEEN ARTICLE XXIV OF THE GATT 1994 AND OTHER WTO AGREEMENTS**

Whether or not trade remedies can be applied within a FTA is an important question.<sup>15</sup> It is not only important as the matter of legal interpretation of Article XXIV of the GATT 1994 but also as the matter of internal politics when negotiating a FTA agreement. In many countries, there are sensitive sectors of the economy in which interest groups react strongly to any proposal to conclude a FTA as exemplified by agricultural groups in Japan. Whenever a proposal was made to negotiate a FTA agreement or any international agreement in which a plan for liberalization of trade in agriculture was involved, it was met with a strong opposition of interest groups in agriculture in Japan. This proves that whenever a negotiation for FTA is initiated, the negotiators should be able to present some proposals to domestic interest groups that there would be some remedies to injury that may be caused to the economic sector. As discussed already, Article XXIV of the GATT 1994 requires an extensive liberalization of trade inside the FTA.

The question here is whether trade remedy measures such as antidumping duties, countervailing duties and safeguard measures are a solution to the above problem. The question here is whether or not interest groups in both countries which would be adversely affected by a FTA agreement are comforted by the possibility of using trade remedy measures when they are confronted with difficulties. This is primarily the issue of examining whether or not Article XXIV of the GATT 1994 allows an interpretation that trade remedies such as antidumping and countervailing duties and safeguard can be applied to imports coming from other partners of the FTA. However, reports of panels and the Appellate Body on this issue are not decisive.

Let us first look at Article XXIV and see how this provision can be interpreted. Article XXVI:8 of the GATT 1994 states that tariffs and trade restrictions must be liberalized but measures under Articles XI, XII, XIII, XIV, XV and XX are exempted from the obligation to liberalize and can be maintained. It is to be noted that Article XIX of the GATT 1994 and

<sup>15</sup> A detailed analysis of this issue is found in: Nozomi Sagara, Provisions for Trade Remedy Measures (Anti-dumping, Countervailing and Safeguard Measures) in Preferential Trade Agreements, RIETI Discussion Paper Series 02-E-13 (September 2002), pp. 1-67. RIETI -> Research Institute of Economy, Trade & Industry, a research institute affiliated with the Ministry of Economics, Trade and Industry, the Japanese Government. Much of the following passages owe to this work.

antidumping and countervailing duty measures are not mentioned here. Therefore, *a contrario* interpretation may be that the obligation to liberalize applies to the trade remedy measures and there is obligation under Article XXIV:8 of the GATT for a member of a customs union or a free trade area to refrain from applying a safeguard or antidumping and countervailing duty measures. In this interpretation, a member of a customs union or a free trade area which is also a Member of WTO can and should apply safeguard or antidumping and countervailing duty measure to imports coming from other WTO members which are not members of the customs union or a free trade area while not applying the same measures to members of the customs union or a free trade area.

On the other hand, there is a counter-argument that the trade remedy measures such as safeguard and antidumping and countervailing duty measures apply even within the FTA area. The rationale for this interpretation is that the premise of trade remedy measures is that trade is already liberalized. If trade is still not liberalized, there is no need for trade remedy measures. Trade remedy measures apply once trade is open. In this view, trade remedy measures apply within the FTA area since the essence of a FTA is to liberalize trade. In this interpretation, it is a mistake to overemphasize the wording of Article XXIV:8 and deny the possibility of applying trade remedy measures within the FTA area.

However, if the economic integration within a customs union has progressed to the extent that industries of the participants have become a “community industry” (such as in the EU), there is no domestic industry in a participating country which needs to be protected from imports, dumping and subsidization of another participating country.

The question of what types of trade remedy measures should be instituted was debated when the negotiation took place between Singapore and Japan with a view to concluding an EPA/FTA agreement. With regard to antidumping and countervailing duty measures, four views were presented with regard to this issue. One is that there should be no trade remedy measure to be applied between the two countries. The second is that there should be no trade remedy measure provided that a sufficient degree of harmonization of competition laws is achieved. This view advocates that trade remedy rules be supplanted by the law of predatory pricing.

The third is that there should be stricter disciplines on trade remedy measures between the two countries with regard to antidumping

and countervailing duties than the WTO disciplines require such as a higher *de minimis* rule. The fourth is that antidumping and countervailing duty measures can be applied between the two countries on the basis of WTO disciplines.

The negotiators decided to adopt the fourth approach and incorporated the rule that antidumping and countervailing duty measures apply in accordance with WTO rules. Other approaches would be effective only if there were a closer economic integration between the participating countries as exemplified by the European Union and the Closer Economic Relations Agreement between Australia and New Zealand. In respect of safeguard, the negotiators decided to include a provision for regular safeguard under the requirements of Article XIX of the GATT 1994 and the Safeguard Agreement.

A bilateral safeguard was incorporated in the EPA Agreement between Singapore and Japan. Under this provision, both governments are allowed to raise tariffs to the maximum of the WTO concession rates if a domestic industry is seriously injured due to an increase of imports caused by the elimination of tariffs. However, this measure is a temporary measure and will expire after ten years.

#### IX. AUTOMATIC EXTENSION OF TRADE REMEDIES

Another problem is whether a customs union or a FTA is allowed automatically to extend the coverage of an outstanding safeguard or antidumping/countervailing measure with regard to a new entrant entering into the customs union or the FTA. For example, suppose the EU has applied an antidumping measure to products from Japan and when a new member joins the EU, the question arises as to whether the EU can extend the protection of this antidumping measure to this new member and impose antidumping duty on product imported to the territory of this Member from Japan. If this were allowed, would this not mean that an antidumping duty is imposed on product from Japan imported into the territory of this new member without investigation?

When three new members joined the EU and became a 15 member entity, the EU automatically applied the antidumping measure to products from Japan imported into the territories of those three new members. Japan objected and a negotiation was held between EU and Japan in which a compromise was reached that EU would conduct a review of the totality

of that antidumping measure at request. The position of Japan is that this automatic expansion of the antidumping measure is contrary to the requirement of Antidumping Agreement which requires a Member applying antidumping measures to conduct investigation before imposing a measure.<sup>16</sup>

In the Turkish Textiles and Clothing Case<sup>17</sup>, the issue was whether Turkey was justified in imposing a quantitative restriction on the import of textile products coming from the third countries when Turkey entered into a customs union agreement between the EU and Turkey to effectuate the quantitative restriction on textile products which the EU had been applying before the conclusion of this agreement. The Panel and the Appellate Body held that this imposition was contrary to Articles XI and XIII of GATT 1994 and Article 2 of ATC.

#### X. PARALLELISM IN SAFEGUARD MEASURES

In the past few years, several important decisions were rendered by the Appellate Body in which the issue was whether a WTO Member who is also a member of a FTA can exclude from the application of a safeguard measure imports of the product in question coming countries that are members of the FTA. Important cases include the Argentina Footwear Case<sup>18</sup>, the United States-Wheat Gluten Case<sup>19</sup> and the United States Lamb Case<sup>20</sup>. In the Argentina Footwear Case, Argentina took into account the import of footwear from MERCOSUR when determining injury to a domestic industry but excluded the application of a safeguard measure to the import from the members of MERCOSUR. The EU challenged this practice at the WTO and both the Panel and the Appellate Body ruled that the selective application of safeguard measure by Argentina was contrary to Article 1 and cannot be exempted under Article XXIV:8 (a)(i) of the GATT 1994.

In all of those cases, the Appellate Body announced that there should be a parallelism between the scope of investigation for a safeguard

<sup>16</sup> See note (1), *supra.*, pp. 95-96

<sup>17</sup> Turkey-Restrictions on imports of Textiles and Clothing Products, WT/DS34/AB/R, 22 October 1999

<sup>18</sup> Argentina-safeguard Measures on Imports of Footwear, WT/DS121, 14 December 1999.

<sup>19</sup> United States-Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities, WT/DS166/Ab/R/22 December 2000

<sup>20</sup> United States-Safeguard Measures on imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia, WT/DS177/AB/R; WT/Ds178/AB/R, 1 May 2001



measure conducted by a Member and the scope of safeguard which is applied as the result of it. Suppose Country A investigates whether imports of Product X coming from Countries B,C,D,E and F cause a serious injury to a domestic industry in Country A and further that Countries A,B and C are the members of a FTA. The question here is: Can Country A exclude from the application of a safeguard measure imports of Product X coming from Countries B and C for the reason that they are members of the FTA while applying the safeguard measure on imports of Product X coming from Countries D,E and F which are outside the FTA?

The ruling of the Appellate Body in the above cases is that a WTO Member cannot exclude from the imposition of a safeguard measure on imports coming from WTO Members that are members of a FTA while applying the safeguard measure on imports of the same or like product coming from other WTO Members that are not members of the FTA as long as the safeguard investigation was conducted with regard to imports of the product coming from all of the countries unless there is a persuasive evidence that the imports coming from the Members that are also members of the FTA did not cause an injury to the domestic industry.

**XI. ARTICLE XXIV AS A DEFENSE TO THE ALLEGED DISCRIMINATORY NATURE OF A SAFEGUARD**

However, the parallelism as enunciated by the Appellate Body does not resolve the question of whether or not Article XXIV can be raised as a defense by a Member when challenged for discriminatory treatment in favor of Members that are insiders of a FTA with regard to safeguard. This issue was raised in the *United States-Line Pipe from Korea Case*<sup>21</sup> in which Korea challenged the imposition of a safeguard measure on imports of line pipe from Korea. The Panel held that Article XXIV could be invoked as a defense to claims of violation of provisions in the GATT 1994 and Korea appealed this finding. The Appellate Body dismissed the Korean appeal on the ground that the question of whether Article XXIV serves as an exception to the requirement of non-discrimination under the GATT arises only in two situations, i.e. (a) that the administering authority did not consider imports coming from countries that are members of a FTA in determining injury issues and (b) that the administering authority determines that imports coming from Members outside the FTA alone are

<sup>21</sup> *United States-Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea*, WT/DS202/AB/R, 15 February 2002

sufficient to cause a serious injury to a domestic industry. The Appellate Body reasoned that, since neither of such situations existed in this case and, therefore, this issue was legally moot.

Article 17:12 of the DSU requires that the Appellate Body address every legal issue raised in an appeal and, in light of this provision, the appropriateness of dismissing this appeal by Korea on the part of the Appellate Body is questionable. This issue, however, is likely to come up again in connection with future safeguard cases.

## XII. “SUBSTANTIALLY ALL” AND TRADE REMEDIES

A legal aspect of Article XXIV in relation to trade remedies is a question of whether trade remedies are allowed if, after applying trade remedies, substantially all of the internal trade of a FTA is still open. Since the language of Article XXIV requires that there should be liberalization within a FTA of “substantially all” of the internal trade but does not require “all” of the internal trade of the FTA to be open, there may be a room for restrictions to exist even within a FTA as long as substantially all of the internal trade is open. Does it mean that trade remedy measures applied within a FTA are allowed as long as they remain within this limit. The liberal reading of the text seems to allow this interpretation and this approach was suggested by the Appellate Body in the Argentina Footwear Case.<sup>22</sup> If this interpretation is accepted, this may cast doubt on the legitimacy of an argument that Members of the WTO which are also members of a FTA are obligated to exclude the internal trade within a FTA from the application of trade remedy measures under Article XXIV of the GATT 1994 and this exclusion is exempted from the MFN obligations. This is because Members of the WTO which are also members of a FTA can apply trade remedy measures as long as substantially all of the internal trade of the FTA remains open.

It is to be noted, at the same time, that a trade remedy measure that a WTO Member which is a member of a FTA may apply may have such a great impact on the internal trade within the FTA that substantially all of the internal trade of the FTA is not open any more. If this happens, an application of a trade remedy measure within a FTA cannot be justified for the reason that there is still substantially all trade within the FTA open even after the application of the trade remedy measure. A determination

<sup>22</sup> See note (16), *supra*.

as to whether a particular trade remedy measure would restrict the trade within a FTA to the extent that substantially all of the internal trade within the FTA is not liberalized any more should necessarily be made on a case-by-case basis. In any event, however, a justification of a trade remedy measure inside a FTA on the basis of the fact that there still remains open substantially all trade in the FTA may have a serious limitation since an application of safeguard measures or antidumping and/or countervailing duties within a FTA may have big impacts on the internal trade and this would deprive the trade remedy measures of legitimacy based on this justification.

### XIII. CONCLUSION

As discussed above, many of the legal problems surrounding the relationship between the WTO rules and FTA are still unresolved. Therefore, it is accurate to say that legal certainty is still lacking in this regard. Future panels and the Appellate Body may clarify some issues. However, the formation of rules through the dispute settlement mechanism is, by its own nature, piecemeal and somewhat lacks comprehensiveness.

Proliferation of EPA/FTA is a fact of life whether one likes it or not and there are reasons for the tendency of increasing FTA in the world economy. One of such reasons is the fact that the multilateral agreements at the WTO is becoming increasingly difficult due to an increase of the number of the Members, especially developing country Members. However, in spite of risks involved in the proliferation of FTA, there should be a way in which the multilateral trading system as represented in the WTO and FTA can co-exist and complement each other. For this purpose, it is important that legal principles of the WTO and FTA be firmly established. It is highly recommended that future negotiators take up issues of the relationship between WTO disciplines and FTA and come up with clearer rules as regards this relationship.