Bilateralism Under the World Trade Organization*

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I. Introduction

The establishment of the World Trade Organization (WTO), which replaced the five decades of the GATT regime, has significantly reinforced the multilateral control over international trade on a global scale. As of February 2005, membership in the WTO has reached 148 nations, including the majority of former Soviet bloc and other communist countries,[1] making the WTO the "United Nations of International Trade." WTO disciplines have significant impact on world trade today and have been enforced by monitoring activities of various WTO bodies and by strengthened dispute resolution mechanisms. On the other hand, a significant number of bilateral / regional trade arrangements also co-exist alongside with the WTO: there are over 130 bilateral / regional trade arrangements (RTAs) in force. Around 90 per cent of WTO Members have signed at least one or more RTAs. Thus, bilateralism represented by these RTAs[2] is as much a factor as the multilateralism by the WTO in shaping international trade relations today.

RTAs provide exclusive preferential treatment to the trade of their members. These exclusionary preferences by RTAs create a discriminatory environment in international trade, which is not consistent with the core objective of the multilateral trading system, namely the Most-Favored Nation (MFN) principle.[3] Current GATT/WTO provisions allow

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[1] China obtained WTO membership in 2001, and Russia is currently going through negotiation for its accession to the WTO.

[2] Bilateralism discussed in this paper encompasses the concept of regionalism as opposed to the multilateralism on a global scale under the WTO system.

[3] Article I of the GATT stipulates the MFN principle, which prohibits discriminatory treatment with respect to importation from WTO Members. WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts* (Cambridge University Press, reprint 2003), pp. 424-425.

the establishment of a customs union or free trade area, as an exception to the MFN requirement.[4] The rationale of this exception is that the preferential trade arrangement of a customs union or free trade area could eventually develop into a multinational framework, thereby giving the benefit of lower trade barriers to more countries as the number of participating countries increases. The growth of membership has been seen with many customs areas or free trade areas: e.g. the European Community has grown well beyond its original membership comprised of a limited number of Western European countries to include most of Europe today.[5]

The proliferation of these trade "clubs", which provide trade preferences limited to their members, may undermine the WTO objective of promoting non-discriminatory trade for all nations.[6] Problems are compounded since some of the recent bilateral trade agreements purport to impose regulatory elements beyond the reduction of trade barriers, such as enforcement of intellectual property rights, the requirement of environment and labor standards, and authorization of uninhibited capital transfers. The inclusion and promotion of these regulatory elements in free trade agreements (FTAs) has significant implications on the current multilateral trading system. The next section of this paper discusses the proliferation of RTAs, most of which are FTAs, as well as their impact and consistency with the multilateral trading system. The Mainland China and Hong Kong Closer Economic Partnership Agreement (CEPA) is introduced as an example of a recent bilateral

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[4] Article XXIV of the GATT. WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*, *supra* note 3, pp. 457-460.
[5] The membership grew from six original members of the European Coal and Steel Community (ECSC) in 1950s to twenty-five nations in 2004.
[6] *Supra* note 3.

trade treaty between developed and developing economies and its consistency with relevant WTO requirements is also examined.

This paper also provides a discussion of bilateralism in the regulation of investment measures, as represented by numerous bilateral investment treaties (BITs), and examines its consistency with relevant provisions of the WTO. Unlike trade, there is no comprehensive multilateral framework for investment on a global scale. A previous attempt of the Organisation for Economic Co-Operation and Development (OECD) to create one failed,[7] and over 1,100 BITs around the world provide some regulatory governance in this area at bilateral level. The WTO Agreement on Trade-Related Investment Measures (TRIMs Agreement) provides a few provisions which prohibits some trade-related investment measures. The General Agreement on Trade in Services (GATS) also has provisions that have relevance to the regulation of investment measures. Section III of this paper questions the regulatory consistency of BITs with relevant WTO provisions. Conclusion is provided in Section IV.

II. Regional Trade Agreements and the WTO[8]

[7] The OECD launched negotiations on "Multilateral Agreement on Investment" or "MAI" in 1995 to be a "free standing international treaty, open to all OECD Members and the European Communities, and to accession by non-OECD Member Countries." Its proposed objective was to "provide a broad multilateral framework for international investment with high standards for the liberalization of investment regimes and investment protection and with effective dispute settlement procedures." A series of intense negotiations ceased in 1998 without reaching an agreement on the final version.

[8] The background information of sections II. a and b of this paper draws from the author's forthcoming article, "Foreign Direct Investment and Regional Trade Liberalization: A Viable Answer for Economic Development?", *Journal of World Trade* (forthcoming August 2005).

a. Proliferation of RTAs

Most of RTAs are free trade agreements (FTAs) eliminating both tariff and non-tariff trade barriers and thereby creating a free trade area among participating countries. RTAs include both bilateral trade arrangements (e.g. the Jordan-U.S. Free Trade Agreement and the Korea-Chile Free Trade Agreement) and multilateral arrangements that have created important economic entities, such as the European Union, NAFTA, ASEAN and MERCOSUR. The WTO approves the formation of an RTA where it eliminates trade barriers with respect to substantially *all* the trade among its members *and* where it does not raise trade barriers to non-members after its formation.[9] The latter requirement is to ensure that these RTAs do not develop into exclusive trade blocs such as those proliferated in the 1930s[10] that contributed to deepening the worldwide depression and that provided a cause of the Second World War.[11] As mentioned above, the rationale for the authorization of an RTA is that its membership would eventually increase to include more countries to benefit from free trade.[12]

It has also been observed that RTAs have proliferated as the subjects of multilateral negotiations in the WTO framework have been expanded into politically sensitive areas such as trade and investment, trade and competition policy, intellectual property rights, and

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[9] *Supra* note 4.
[10] Major economic powers, such as Britain, France, and the United States of America erected trade barriers in their home and colonial markets. As a result, exporters from countries without vast domestic or colonial markets, such as Germany and Italy, were put at a substantial disadvantage.
[11] For the economic causes of the Second World War, *see* Andrew J. Crozier, *The Causes of the Second World War* (Blackwell Publishers, Oxford, 1997).
[12] The expansion of the European Community is an example. *Supra* note 5.

epidemics, and therefore, have become more difficult.[13] As an alternative to multilateral negotiations on a global scale that could take years to come to any consensus, nations have begun to resort to trade negotiations among a more limited number of countries sharing common interests in trade and investment, closer economic and cultural ties, and geographic proximity. This trend has led to the formation of a number of RTAs around the world as previously noted. In 2002, the four largest free trade areas (the EU, NAFTA, MERCOSUR and ASEAN) accounted for 64.5 per cent of world exports and 69.5 per cent of world imports.[14] Concerns have been expressed against this proliferation of RTAs, since it may erode WTO disciplines and distract Members from important multilateral negotiations.

b. Undermining the Objectives of the WTO?

The fundamental problem of RTAs is that the exclusive nature of their trade preference is not consistent with the MFN principle of GATT/WTO disciplines. It may have been a political requirement in the beginning of the GATT in 1947 to accommodate the remaining colonial trade preferences of the world powers[15] and to support the reconciliation effort of the war-torn European countries by permitting exclusive trade preferences among themselves.[16]

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[13] Mitsuo Matsushita, "Legal Aspects of Free Trade Agreements In the Context of Article XXIV of the GATT 1994", paper presented at the seminar, *The Way Forward to Successful Doha Development Agenda Negotiation*, United Nations University, Tokyo, Japan (May 24-25, 2004). The failure of the WTO ministerial conference in Cancun has shown this difficulty. *See* Sungjoon Cho, "A Bridge Too Far: The Fall of the Fifth WTO Ministerial Conference in Cancun and the Future of Trade Constitution" (2004) 7 *Journal of International Economic Law* 219-244.

[14] *Id.*

[15] Article I, paras 2 and 3 of the GATT, WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*, *supra* note 3, pp. 424-425.

[16] Reconciliation was an important motivation behind the establishment of the European Communities, whose membership has increased substantially over the years. *Supra* note 5.

Even if the trade barriers to non-member countries do not increase after the formation of an RTA,[17] exclusive trade preferences still put competing non-member countries at a *relative* disadvantage with respect to their trade. It is particularly true with developing countries whose export industries are not as competitive as those of developed counterparts. The late Professor Robert Hudec, an eminent trade scholar, was critical of trade preference regimes for this reason, and believed that an MFN-based regime is the only genuine protection available to developing countries as "a legal substitute for economic power on behalf of smaller countries."[18]

The proliferation of RTAs creates a risk of fragmentizing the world trading system which may ultimately threaten the integrity of the multilateral trading regime despite the perceived benefit *within* these trade clubs and the possibility of their expansion to confer benefit of free trade on more nations. How could the dilemma be resolved? Since the source of the problem is the gap in trade concessions made multilaterally and those made regionally, one possibility is to narrow this gap by eliminating trade barriers within regional trade areas gradually at more or less the same rate and on the same timetable as the lowering of barriers towards non-members. Renato Ruggiero, former General Director of the WTO, has observed this possibility in certain regional trade areas, such as Asia-Pacific Economic Cooperation (APEC).[19] In this scenario, the danger of fragmentizing the world trading system and the threat to the trade of non-member developing countries will

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[17] *Supra* note 4.
[18] Robert Hudec, *Developing Countries in the GATT Legal System*, Thames Essays (Trade Policy Research Centre, London, 1987), pp. 216-217.
[19] WTO New Release (April 26, 1996).

be minimized. Nonetheless, this approach may defeat the very purpose of RTAs that is to provide exclusive trade preferences to their members, and therefore, may not be followed by many countries which favor exclusive trade preferences.

Yet another possibility has been suggested by a Yale economist, T.N. Srinivasan, who stated in a 1999 WTO high-level symposium on Trade and Development that a "sunset clause" should be introduced to regional agreements whereby preferences available to the members of regional agreements is extended to all WTO members in five years.[20] This proposal allows members of the existing RTAs to maintain exclusive trade preferences temporarily, but these preferences will no longer be "exclusive" vis-à-vis other WTO members after the expiration of this fixed period. This proposal is in some sense a re-assertion of the MFN principle, which has been waived for the formation of a customs union / free trade area under Article XXIV.[21] Both of the above proposals aim to eliminate exclusive trade preferences enjoyed by the members of RTAs. Again, the question is whether these members be willing to give up exclusive trade preferences.

A new breed of RTAs, promoted by certain developed countries such as the United States, complicates the issue since they not only seek to eliminate tariff and non-tariff barriers, but also attempt to instill certain regulatory elements in trade relations. These elements include enforcement of intellectual property rights (IPRs), the requirement of environment and

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[20] World Trade Organization, *The Report of the WTO high-level symposium on trade and development* (1999), available online at <www.wto.org>.
[21] *Supra* note 4.

labor standards, and authorization of uninhibited capital transfers.[22] These new requirements go beyond the facilitation of international trade by reducing trade barriers and pose new problems of another dimension – these RTAs impose a new set of trade rules on their members which are not yet agreed upon multilaterally at the WTO level, which will complicate and cause inconsistencies in the discipline of world trade.

These new type-RTAs have been negotiated between developed and developing countries (e.g. United States - Chile FTA, United States – Central America FTA). There is concern that the effects of the new regulatory requirements in these RTAs are not limited to trade but may cause adverse consequences on the economic development of developing countries. For instance, the stringent requirement of IPR protection will diminish the availability of new information and technology necessary for development and will make its use costly. The establishment and enforcement of an IPR regime itself can also be costly and may cause a substantial diversion of scarce human and capital resources in developing countries that could be used more productively elsewhere.[23] The other requirements, such as labor and environmental standards, could equally be costly and burdensome on developing countries.[24]

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[22] Alvin Hilaire and Yongzheng Yang, "The United States and the New Regionalism/Bilateralism" (2004) 38 *Journal of World Trade* 609.

[23] According to a study, implementing an IPR regime such as the one required by the WTO's TRIPS (Trade-Related Aspects of Intellectual Property Rights) obligations would cost each of the least developed countries $150 million, representing a full year's development budget of many of the least developed countries, to invest in buildings, equipment, training, and so forth. J. Michael Finger, "The WTO's Special Burden on Less Developed Countries" (2000) 19(3) *Cato Journal*, p. 435.

[24] RTAs should not be used as a means to get around the terms of the multilateral trade agreement of the WTO and impose various regulatory requirements on developing countries that are not directly relevant to the facilitation of trade, such as IPR enforcement and labor and environmental standards. Of course, a developing country is not required to

c. The Mainland China and Hong Kong Closer Economic Partnership Agreement (CEPA)

A recent FTA between developed and developing economies presents an example of how the consistency between a bilateral trade arrangement and the multilateral trading system can be sought. On June 29, 2003, the Government of Hong Kong Special Administrative Region (hereinafter "Hong Kong") and the Central People's Government of China signed the Mainland and Hong Kong Closer Economic Partnership Agreement (CEPA), which went into effect on January 1, 2004. This is the first major trade agreement between the Mainland China and Hong Kong since the latter joined China on the principle of "one country, two systems."[25] As both Hong Kong and mainland China retain separate membership in the WTO, CEPA is regulated by GATT Article XXIV, authorizing the establishment of a free trade area.

CEPA, comprising 23 Articles in 6 Chapters, requires the progressive elimination of both

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join any RTA, but it may not afford to stay outside where strong initiatives for RTAs are made by powerful economies bilaterally or regionally where the developing country has an essential economic interest. In order to safeguard the interest of developing countries secured under the multilateral system, consideration should be given to specifying in the relevant WTO provisions that Members are prohibited from engaging in any arrangement bilaterally or otherwise that would undermine these rights of developing countries protected under the WTO provisions. The current WTO provision stipulates a similar requirement where it prohibits Members from entering into *any* arrangement that allows *gray-area measures* by which trading countries agree to restrain trade for the benefit of the domestic producers of the importing country. Article 11.1 of the WTO Agreement on Safeguards stipulates such prohibition. WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts, supra* note 9, p. 321. *See* Y.S. Lee, *supra* note 8.

[25] Under this system, the political, economic and social autonomy of Hong Kong is to be preserved for the fifty years from 1997.

tariff and non-tariff measures on trade between mainland China and Hong Kong. Trade liberalization efforts are to be made for both trade in goods and trade in services. The objectives of CEPA are laid out in Article 1, which provides in relevant part:

> To strengthen trade and investment cooperation between the Mainland and the Hong Kong Special Administrative Region (hereinafter referred to as "Hong Kong") and promote joint development of the two sides, through the implementation of the following measures:
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> 1. progressively reducing or eliminating tariff and non-tariff barriers on substantially all the trade in goods between the two sides;
> 2. progressively achieving liberalization of trade in services through reduction or elimination of substantially all discriminatory measures;
>
> 3. promoting trade and investment facilitation.

Article 5 of CEPA further provides the timetable for "zero tariffs" on goods traded between mainland China and Hong Kong.[26] Other Articles regulate the application of certain trade measures (Articles 6 through 9), the rules of origin (Article 10), progressive liberalization of trade in services (Articles 11 through 15), and trade and investment facilitation (Articles 16 and 17).

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[26] Article 5 of CEPA provides:

> 1. Hong Kong will continue to apply zero tariff to all imported goods of Mainland origin.
> 2. From 1 January 2004, the Mainland will apply zero tariff to the import of those goods of Hong Kong origin listed in Table 1 of Annex 1.
> 3. No later than 1 January 2006, the Mainland will apply zero tariff to the import of goods of Hong Kong origin that are outside Table 1 of Annex 1. Detailed implementation procedures are set out in Annex 1.
> 4. Any new goods that are subject to elimination of import tariffs in accordance with paragraph 3 of this Article shall be added to Annex 1.

Is CEPA consistent with WTO disciplines? To the extent that it governs trade in goods, CEPA conforms to GATT Article XXIV requirements for the creation of a free trade area: i.e. CEPA purports to eliminate trade barriers with respect to substantially *all* the trade between the Mainland China and Hong Kong (Article XXIV: 8(b)). Higher barriers are not set against the imports of the other countries after the implementation of CEPA, which is consistent with Article XXIV requirements. Nonetheless, as China will impose zero tariff on all imports from Hong Kong by January 1, 2006, Hong Kong exporters will enjoy a competitive advantage over the other exporters to China (Hong Kong has already been imposing no tariffs on imports). As discussed above, exclusive trade preferences among a customs union or free trade area operate as an exception to the MFN principle of the WTO, and the exclusive preference will justifiably exist between Hong Kong and mainland China to the extent that is not available to other WTO Members by way of trade concessions.

Secondly, CEPA is not classified as the new breed of RTA discussed earlier. CEPA does not impose new regulatory schemes, such as IPR protections and enforcements, labor and environment standards, and the authorization of uninhibited capital transfers. CEPA focuses on the traditional function of a free trade agreement, which is the liberalization of trade. In line with the facilitation of trade liberalization, CEPA requires the non-application of anti-dumping measures (Article 7) and of countervailing measures (Article 8). These measures have frequently been criticized for inhibiting trade on dubious grounds and

targeting cheaper imports from developing countries.[27] Therefore, the commitment of the non-application of these measures is a welcome initiative for the facilitation of trade between the two economies.

For trade in services, trade liberalization initiatives of CEPA are subject to the MFN requirement of the General Agreement on Trade in Services (GATS).[28] Unlike the GATT governing trade in goods, the GATS does not have a device, such as Article XXIV, that authorizes a customs union or a free trade area as an exception to the MFN principle. This means that any favorable treatment that a WTO Member provides pursuant to the terms of a regional agreement on trade in services cannot be kept exclusive among its member countries but will have to be extended to all other WTO Members. There is an exception in that the MFN requirement will not apply if a Member exempts certain measures from MFN treatment at the time of entry into force of the agreement (GATS, Article II.2).[29] Preferences for trade in goods that is to be provided by the terms of CEPA will have to be extended to all other WTO Members as neither China nor Hong Kong has made such exception from the MFN treatment.

III. Bilateral Investment Treaties and the GATS

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[27] For more detailed discussions on the trade effects of these measures, *see* Y.S. Lee, *Reclaiming Development in the World Trading System* (Cambridge University Press, forthcoming 2005), Chapters 3 and 4.

[28] Article II:1 of the GATS provides, "With respect to any measure covered by this Agreement, each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and service suppliers of any other country." WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*, *supra* note 3, p. 287.

[29] *See* Annex on Article II Exemptions, WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*, *supra* note 3, p. 308.

a. Investment and International Trade

Another area where bilateralism is an important factor is investment. Foreign direct investment (FDI) has increased over thirty-fold during past two decades,[30] and FDI and its regulation have become closely relevant to international trade. The impact of FDI regulation on trade can be easily seen. For instance, suppose that the government of Country A requires foreign investors who have built manufacturing facilities in the host country to export a certain portion of outputs produced by these facilities. To meet this requirement, the investors may export more than they would have without such requirement, and this would lead to an increase in exports from Country A. Alternatively, the government may require foreign investors to buy domestically-produced products instead of imported products, and this may, in turn, lead to a reduction in imports.

In order to prevent the "trade-distortion" caused by investment measures, WTO disciplines regulate certain trade-related investment measures (TRIMs) in a rather brief set of rules, entitled "Agreement on Trade-Related Investment Measures" (TRIMs Agreement), which is comprised of nine articles and an annex.[31] The TRIMs Agreement prohibits investment measures that are inconsistent with Articles III and XI of the GATT, which requires the national treatment[32] and the general elimination of quantitative restrictions, [33] respectively.

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[30] FDI outflows increased from 28 billion USD in 1982 to 612 billion USD in 2003 (valued at current prices). UNCTAD, *World Investment Report 2004*, Table 1.3 Selected Indicators of FDI and International Production, 1982-2003, p. 9.

[31] WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts, supra* note 3, pp. 143-146.

[32] The national treatment principle prohibits discriminatory treatment to imported products once passed through customs. GATT Article III. *Id.,* pp. 427-429.

[33] GATT Article XI. *Id.*, p. 437.

The Annex of the TRIMs Agreement provides an illustrative list of prohibited TRIMs.[34] The list includes: local content requirements (imposing the use of a certain amount of local inputs in production); import controls (requiring imports used in local production to be equivalent to a certain proportion of exports); foreign exchange balancing requirements (requiring the foreign exchange made available for imports to be a certain proportion of the value of foreign exchange brought in by the foreign investment from exports and other sources); and export controls (obligating exports to be equivalent to a certain proportion of local production). The rationale for this prohibition is that these particular TRIMs distort trade by requiring investors to make certain export or import commitments.

Nonetheless, the TRIMs Agreement is not meant to provide a comprehensive multilateral legal framework for investment. The scope and the objectives of the Agreement, which is to prevent the distortion of trade by TRIMs, seem too limited to be considered to be comprehensive disciplines on investment. Unlike in the area of trade, no multilateral disciplines on investment exist. An attempt made by the OECD to create a Multilateral Agreement on Investment (MAI) was not successful.[35] In the absence of a comprehensive, multilateral regulatory regime on investment, FDI has been governed by a number of bilateral investment treaties (BITs).[36] Some developed countries believe that a multilateral agreement on investment that is more comprehensive than the TRIMs Agreement is

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[34] *Id.*, pp. 146.

[35] Supra note 7. The background and negotiations of the MAI are introduced in the official OECD site, <http://www1.oecd.org/daf/mai/intro.htm>.

[36] According to the World Bank record, over 1,100 BITs are known to exist, and 800 of them were concluded after 1987.
<http://www.worldbank.org/icsid/treaties/intro.htm>
For a comprehensive review of BITs, *see* Rudolf Dolzer and Margrete Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff Publishers, 1995).

desirable, and have taken initiatives to begin discussions at the WTO.[37] However, this attempt has faced considerable resistance from some developing country Members, such as India, as they feared that extensive rules on investment might place considerable restraints on government measures and policies on foreign investment.[38] It has also been doubted that the WTO would be the best place to address an issue of investment.[39] Thus, it is uncertain whether the initiatives to create a multilateral investment agreement at the WTO will prove to be successful.

b. Bilateral Investment Treaties and the GATS

As discussed above, over 1,100 BITs regulate FDI on a bilateral basis, and a question is raised about their consistency with certain core provisions of WTO disciplines applying to trade in services. The general purpose of a BIT is to provide the national treatment[40] to the investors of the other signatory country. The specific terms of numerous BITs are by no means identical, but BITs typically require non-discriminatory treatment to foreign investors with respect to the admission and regulation of investment, prohibit certain

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[37] WTO Ministerial Declaration, WTO doc. WT/MIN(01)/DEC/1 (November 20, 2001), paras 20-22.

[38] Governments of developing countries may prefer to have latitude in prescribing investment policies to maximize the contribution of foreign investment to their development objectives. Y.S. Lee, *Reclaiming Development in the World Trading System, supra* note 27, Chapter 5.

[39] T.N. Srinivasan highlighted "the folly of trying to achieve too many policy objectives with one instrument and suggested that the TRIPS be taken out of GATT and handled by WIPO; the CTE be wound up and environment tackled by UNEP; and labour be excluded from the purview of GATT and handled by the ILO." WTO, *Report on the WTO high-level symposium on trade and development* (1999), *supra* note 20.

[40] The concept of national treatment in the goods trade can also be applied to the context of FDI, which prohibits discriminatory treatment between foreign and domestic investments.

government investment measures,[41] guarantees transfer of capital and liquidation of investment, protects foreign investment against arbitrary expropriation, and provides a fair and effective dispute resolution process.[42] As discussed in the preceding sections, some of the recent RTAs include provisions that attempt to provide security for foreign investment, such as uninhibited capital transfer, which have traditionally been the contents of BITs,

BITs provides exclusive preference to the investors from the other signatory country. Where this preference for foreign investment facilitates the supply of a service, it would then be also subject to the jurisdiction of the GATS which applies to trade in services.[43] The GATS prescribes that the supply of services can be made through "commercial presence in the territory of any other member."[44] Thus, investment that establishes such a commercial presence for the supply of services would fall under the jurisdictions of both GATS and the BIT, provided that the signatory countries of the BIT are also WTO Members. The MFN requirement of the GATS is applied to this preference Article II:1 of the GATS provides:

> "With respect to any measure covered by this Agreement, each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and

[41] Examples would be those listed under the annex of the TRIMs Agreement. *Supra* note 34.
[42] Dolzer and Stevens, *supra* note 36.
[43] For instance, a BIT may provide foreign investors with a license to establish certain educational services. Providing education services is the supply of a service under the GATS.
[44] Article I.2, GATS. *Id.*

service suppliers of any other country."[45]

The question is how the preference that is applied to the supply of a service limited to the signatories of the BITs can be consistent with the MFN requirement of the GATS under which such preference should be extended to all other WTO Members.

The GATS, unlike the GATT, does not require the national treatment as a general principle since the national treatment applies only to the service sectors that have been scheduled for market access, subject to the limitations and qualifications therein.[46] Thus the national treatment and other preferences offered under the terms of BITs that facilitate the supply of a service should arguably be applied to all other WTO Members by operation of the MFN provision of the GATS to the extent that the stated exceptions under the Annex on Article II are not applied.[47] The GATS does not have a GATT Article XXIV type-exception to the MFN requirement that allows regional trade arrangements, and there is no other provision in the GATS that exempts the exclusive preferential relations from the application of the MFN principle.

Currently there is no regulatory provision to resolve the potential conflict between the exclusive preference of BITs and the MFN requirement of the GATS. How can this problem be addressed? A question was raised during BIT negotiations between South Korea and Japan during 1998-99 with respect to a potential conflict between bilateral

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[45] WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*, *supra* note 3, p. 287.
[46] Article XVII, GATS. *Id.*, pp. 299-300.
[47] *Supra* note 29.

preferences stipulated in the BIT and the MFN requirement under the GATS. This problem was solved as far as Korea was concerned because the Korean practice required that any preference agreed in bilateral investment treaties be incorporated in relevant laws and regulations that are applied to *all* foreign investors. If preferential treatments of BITs that facilitates the supply of services are made generally applicable to all foreign investors, as in the Korean practice, it will then meet the MFN requirement under Article II of the GATS. It is also interesting to note that many BITs require that the MFN treatment be applied for the benefit of investors of signatory countries. This means that these investors will benefit from any preference that one signatory country provides to others even if this specific preference has not been negotiated for the BIT.[48]

Another way to avoid the conflict is to mark the exemption of the MFN requirements under Article II.2 of the GATS in the specific sectors scheduled. These exemptions, however, should have been made at the entry into force of the WTO Agreement,[49] and any subsequent exemptions can only be made by the waiver under Article XI of the WTO Agreement which requires the decision based on consensus at the Ministerial Conference.[50] Unlike the national treatment, the MFN requirement is more difficult to waive under the GATS, and acquiring MFN exemptions to preserve exclusive preferences under BITs will be extremely cumbersome if not entirely impossible.

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[48] *Supra* note 36, pp. 65-66.
[49] Marrakesh Agreement Establishing the World Trade Organization. WTO, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*, *supra* note 3, pp. 4-16.
[50] *Id.,* p. 9.

Should a GATT Article XXIV type-exception be permitted for trade in services to allow regional/bilateral arrangements that will authorize exclusive preferences for the supply of a service? Some may consider such an exception to be reasonable as it is allowed for trade in goods. In addition, numerous BITs in force predate the implementation of the GATS, and there may be vested interests to maintain exclusive preferences. On the other hand, as discussed in the preceding section, such an exception could create the danger of fragmentation of trade disciplines and may also cause difficulties to the trade of non-participating countries that do not benefit from the bilateral preferences of BITs. Non-participating developing countries will have more difficulties whose export industries may not be competitive enough. The MFN principle of the GATS should be preserved and should not be compromised with Article XXIV type-exceptions.

IV. Conclusion

Bilateral trade arrangements such as RTAs and BITs (the latter to the extent that it is relevant to the service of a supply) are inherently inconsistent with the objective of the multilateral trading system to facilitate non-discriminatory trade among *all* nations so long as these bilateral arrangements attempt to preserve exclusive preferences among the participating member countries. These preferences may facilitate trade among the participants, but may become a barrier to the trade of other countries even if those barriers are not increased *in absolute terms*; the exclusion from preferences is a *relative* barrier to the trade of other countries, particularly that of less-competitive developing countries.

In this regard, the proliferation of bilateral trade arrangements raises concern. WTO

Members may feel pressure to join these exclusive trade-clubs so as to not to be "left out," and this movement toward bilateral/regional arrangements may increase the fragmentation of trade disciplines throughout the world. It would particularly be true where RTAs attempt not only to reduce trade barriers but to instill new sets of trade-related rules that have not been agreed upon by WTO Members. Some countries, particularly developing countries, may be tempted or even pressured to join this new type of RTAs for economic and other incentives offered by powerful economies that promote such RTAs. Creating another layer of trade disciplines beyond what have been established under the WTO could undermine the consistency of global trade disciplines.

Convergence, and not divergence, should be sought between bilateral/regional trade arrangements and WTO disciplines, and these arrangements should be brought in line with the objectives of the multilateral trading system. Professor Srinivasan's earlier proposal to set expirations for exclusive trade preferences of RTAs would be a way to achieve this convergence and to prevent the fragmentation of the world trading system. Bilateral attempts to impose regulatory burdens on developing countries beyond what has been agreed upon in the framework of the WTO should be restrained. When the noted convergence is achieved, bilateralism will then operate "within" the objectives of the WTO. This new "bilateralism within the WTO" will be positive for the facilitation of trade as a means to expand, and not exclude, trade concessions to all WTO Members. The same applies to BITs. Since the GATT Article XXIV type-exception to the MFN principle does not exist in the GATS, the enforcement of the MFN requirement in the GATS will work to expand trade-related preferences in BITs to all WTO Members.