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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 General Agreement on Tariffs and Trade ("GATT") regime,[1] has significantly reinforced multilateral control over international trade on a global scale. As of October 2005, membership in the WTO has reached 148 nations, including the majority of former Soviet bloc and other communist countries,[2] making the WTO the "United Nations of International Trade."[3] WTO disciplines have significant impact on world trade today; they have been enforced by the monitoring activities of various WTO bodies and by strengthened dispute resolution mechanisms. In addition, a significant number of bilateral/regional trade agreements co-exist alongside the WTO. There are over 130 of these agreements in force. Around 90% of WTO members have signed at least one or more regional trade agreements ("RTAs"). Thus, the bilateralism represented by these RTAs is as much a factor as the multilateralism of the WTO in shaping international trade relations today.[4]

RTAs provide exclusive preferential treatment to trade with member

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[1] The General Agreement on Tariffs and Trade (GATT) was implemented in 1947 as a post war discipline of international trade. For the history of the GATT, see JOHN H. JACKSON, THE WORLD TRADING SYSTEM 31–43 (1997).

[2] China obtained WTO membership in 2001; Russia is currently going through negotiations for its accession to the WTO.

[3] Currently WTO membership includes all major economies and trading nations, except perhaps Russia.

[4] The bilateralism discussed in this paper encompasses the concept of regionalism, as opposed to multilateralism, under the WTO system.

states. These exclusionary preferences by RTAs create a discriminatory environment in international trade. This is not consistent with the core objective of the multilateral trading system, namely the Most-Favored Nation ("MFN") principle.[5] Current GATT/WTO provisions allow for the establishment of a customs union or free trade area as an exception to the MFN requirement.[6] The rationale for 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 also been seen in many customs or free trade areas. For example, the European Community has grown well beyond its original membership, which was comprised a limited number of Western European countries, to include most of Europe today.[7] The proliferation of these trade "clubs," which provide trade preferences limited to their members, may undermine the WTO's objective of promoting non-discriminatory trade for all nations.[8] Problems are compounded because 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 environmental and labor standards, and the 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. Section IIof this article discusses the proliferation of RTAs, most of which are FTAs, as well as their impact on and consistency with the multilateral trading system. The Mainland China and Hong Kong Closer Economic Partnership Agreement is introduced as an example of a recent bilateral trade treaty between developed and developing economies; its consistency with relevant WTO requirements is examined.

This article 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

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[5] Article I of GATT stipulates the MFN principle, which prohibits discriminatory treatment with respect to importation from WTO Members. *See* GATT Secretariat, *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Text* 486–87 (June 1994) [hereinafter *Uruguay Round*].

[6] General Agreement on Tariffs and Trade, October 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194, Art. XXIV [hereinafter GATT]. *Id.* at 522–25.

[7] The membership grew from the six original members of the European Coal and Steel Community (ECSC) in the 1950s to twenty-five nations in 2004. The History of the European Union, http://europa.eu.int/abc/history/index_en.htm (last visited Jan. 18, 2006).

[8] *Uruguay Round, supra* note 5, at 486–87.

for investment on a global scale. A previous attempt by the Organization for Economic Co-Operation and Development to create one failed,[9] while over 1,100 BITs around the world provide some regulatory governance in this area at the bilateral level. The WTO Agreement on Trade-Related Investment Measures provides a few provisions that prohibit some trade-related investment measures. The General Agreement on Trade in Services 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.

II. REGIONAL TRADE AGREEMENTS AND THE WTO[10]

A. Proliferation of RTAs

Most RTAs create free trade areas among signatory countries by eliminating both tariff and non-tariff trade barriers. These FTAs can be bilateral agreements, as in the Jordan-U.S. Free Trade Agreement, or they can be multilateral agreements, such as the European Union ("EU") agreement. In addition to creating free trade, multilateral FTAs can create powerful economic entities, as is the case with the EU, the North America Free Trade Area ("NAFTA"), the Association of Southeast Asian Nations Free Trade Area ("ASEAN"), and the Mercado Comum der Sur: The Southern Common Market in Latin America ("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."[11] The latter requirement is meant to ensure that RTAs do not develop into exclusive trade blocs, such as those that proliferated in the 1930s[12] and contributed to deepening the worldwide depression and

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[9] The OECD launched negotiations on the Multilateral Agreement on Investment (MAI) in 1995 as 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.

[10] The background information of sections II.A & B of this paper are drawn from the author's forthcoming article, Y.S. Lee, *Foreign Direct Investment and Regional Trade Liberalization: A Viable Answer for Economic Development?*, 29 J. OF WORLD TRADE 701, 701–17 (2005).

[11] *Uruguay Round*, *supra* note 5, at 457–60 (emphasis added).

[12] Major economic powers, such as Britain, France, and the United States 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.

provided a cause for the Second World War.[13] As mentioned above, the rationale for the authorization of an RTA is that its membership eventually increase to include more countries to benefit from free trade.[14]

It has also been observed that RTAs have proliferated because multilateral negotiations on a global scale have become more difficult in certain areas, 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 epidemics.[15] 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% of world exports and 69.5% of world imports.[16] Concerns have been expressed against this proliferation of RTAs, since they may erode WTO disciplines and distract members from important multilateral negotiations.

B. Undermining the Objectives of the WTO?

The fundamental problem with RTAs is that the exclusive nature of their trade preference is not consistent with the MFN principle of the GATT/WTO disciplines. At its inception GATT may have been a political requirement to accommodate the remaining colonial trade preferences of the world powers[17] and to support the reconciliation efforts of the war-torn European countries by permitting exclusive trade preferences among themselves.[18] Even though trade barriers to non-member countries do not increase after the formation of an RTA,[19] exclusive trade preferences still

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[13] For the economic causes of the Second World War, see ANDREW J. CROZIER, THE CAUSES OF THE SECOND WORLD WAR (1997).

[14] The expansion of the European Community is an example. *See supra* note 7.

[15] 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*, 7 J. INT'L ECON. L. 219, 219–44 (2004).

[16] Matsushita, *supra* note 15.

[17] GATT Art. I, ¶¶ 2–3; *Uruguay Round*, *supra* note 5, at 486–87.

[18] Reconciliation was an important motivation behind the establishment of the European Communities, whose membership has increased substantially over the years. *Supra* note 7.

[19] GATT Art. XXIV. *Uruguay Round*, *supra* note 5, at 522–25.

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 their developed counterparts.[20] 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."[21]

The proliferation of RTAs creates a risk of fragmenting the world trading system, which may ultimately threaten the integrity of the multilateral trading regime. This occurs despite the perceived benefit *within* these trade clubs and the possibility of their expansion to confer the benefit of free trade on more nations. How can the dilemma be resolved? Because 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 the Asia-Pacific Economic Cooperation ("APEC").[22] In this scenario, the danger of fragmenting the world trading system and the threat to the trade of non-member developing countries will be minimized. Nonetheless, this approach may defeat the very purpose of RTAs—that is, to provide exclusive trade preferences to their members. Therefore, this approach may not be followed by the countries that favor exclusive trade preferences.

Yet another possibility has been suggested by 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 agreement's members are extended to all WTO members in five years.[23] 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

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[20] For instance, it is easily conceivable that China will have many more difficulties in exporting their automobiles to France than Germany would have because of the trade preference received by Germany under the EU regulations, as well as the difference in the quality and efficiency of the automobile industries between the two countries.

[21] ROBERT E. HUDEC, DEVELOPING COUNTRIES IN THE GATT LEGAL SYSTEM 216–17 (1987).

[22] Press Release, WTO, WTO Director-General Cites Progress in Telecoms and Calls on the Singapore Agenda to Address Problems of Least Developed Countries (April 26, 1996), http://www.wto.org/english/news_e/pres96_e/pr046_e.htm.

[23] Summary of WTO High-Level Symposium on Trade and Development (1999), http://www.wto.org/english/tratop_e/devel_e/summhl_e.htm.

other WTO members after the expiration of this fixed period. This proposal is in some sense a reassertion of the MFN principle, which has been waived for the formation of a customs union/free trade area under Article XXIV.[24] Both of the above proposals aim to eliminate exclusive trade preferences enjoyed by the members of RTAs. Nevertheless, the question is whether these members would 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 ("IPR"), the requirement of environmental and labor standards, and authorization of uninhibited capital transfers.[25] 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. This will complicate and cause inconsistencies in the discipline of world trade.

This new type of RTA has been negotiated by developed and developing countries (e.g., the United States-Chile Free Trade Agreement[26] and the United States-Central America Free Trade Agreement[27]). There is concern that the effects of the new regulatory requirements in these RTAs are not limited to trade, but may cause adverse consequences for the economic growth 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 a legal system to protect IPRs can also be costly[28] and may cause a substantial diversion of scarce

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[24] GATT Art. XXIV. *Uruguay Round*, *supra* note 5, at 522–25.

[25] Alvin Hilaire & Yongzheng Yang, *The United States and the New Regionalism/ Bilateralism*, 38 J. WORLD TRADE 603, 609 (2004).

[26] Full Text of the United States-Chile Free Trade Agreement (2003), *available at* http://www.ustr.gov/assets/Trade_Agreements/Bilateral/Australia_FTA/Final_Text/asset_upload_file148_5168.pdf (last visited Jan. 18, 2006).

[27] Full Text of the Central America-Dominican Republic-United States Free Trade Agreement (2004), *available at* http://www.ustr.gov/Trade_Agreements/Bilateral/CAFTA/CAFTA-DR_Final_Texts/Section_Index.html (last visited Jan. 18, 2006).

[28] J. Michael Finger has pointed out that:

> 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*, 19 CATO J.

human and capital resources that could be used more productively elsewhere. Other requirements, such as labor and environmental standards, could be equally costly and burdensome on developing countries.[29]

C. The Mainland and Hong Kong Closer Economic Partnership Arrangement

A recent FTA between a developed and a developing economy illustrates consistency between a bilateral trade arrangement and a multilateral trading system. On June 29, 2003, the Government of Hong Kong Special Administrative Region ("Hong Kong") and the Central People's Government of China signed the Mainland and Hong Kong Closer Economic Partnership Arrangement ("CEPA"), which went into effect on January 1, 2004. This is the first major trade agreement between Mainland China and Hong Kong since the latter joined China in the principle of "one country, two systems."[30] As both Hong Kong and mainland China retain separate memberships in the WTO, GATT Article XXIV regulates CEPA and authorizes the establishment of a free trade area.[31]

CEPA requires the progressive elimination of both tariff and non-tariff measures on trade between Mainland China and Hong Kong. These trade

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425, 435 (2000).

[29] 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 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.

Lee, *supra* note 10, at 714.
In order to safeguard the interests 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.

Id. at 714–15 (citing article 11.1 of the WTO Agreement on Safeguards, *Uruguay Round, supra* note 5, at 321).

[30] Under this system, Hong Kong will preserve its political, economic and social autonomy from 1997–2047.

[31] *Uruguay Round, supra* note 5, at 522–25.

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:

> To strengthen trade and investment cooperation between the Mainland and the Hong Kong Special Administrative Region . . . and promote joint development of the two sides, through the implementation of the following measures:
> 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.[32]

Article 5 of CEPA further provides the timetable for "zero tariffs" on goods traded between Mainland China and Hong Kong.[33] 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).[34]

The first consideration is whether CEPA is consistent with the 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 of the trade between Mainland China and Hong Kong.[35] Higher barriers are not set against the imports of other countries after the implementation of CEPA. Such actions are consistent with Article XXIV requirements. Nonetheless, by January 1, 2006, China will impose no tariff on imports from Hong Kong. Thus, Hong Kong exporters will enjoy a competitive advantage over other exporters to China (Hong Kong already imposes no tariffs on Chinese imports). As discussed above, exclusive trade

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[32] Closer Economic Partnership Agreement, P.R.C.-H.K., June 29, 2003, http://www.tid.gov.hk/english/cepa/files/main_e.pdf [hereinafter CEPA].

[33] 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.

Id. at art. 5.

[34] *Id.* at arts. 6–17.

[35] GATT Art. XXIV ¶ 8(b).

preferences among a customs union or free trade area operate as an exception to the MFN principle of the WTO. An exclusive preference will justifiably exist between Hong Kong and mainland China by way of trade concessions to an extent that is not available to other WTO members.

Second, CEPA is not classified as a new breed of RTA. This is because CEPA does not impose new regulatory schemes, such as IPR protection and enforcement, labor and environmental standards, or 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.[36] Therefore, the commitment to not apply these measures is a welcome initiative to facilitate trade between the two economies.

For trade in services, the trade liberalization initiatives of CEPA are subject to the MFN requirement of the General Agreement on Trade in Services ("GATS").[37] Unlike Article XXIV of the GATT governing trade in goods, the GATS does not have a device 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 that the agreement enters into force for the country.[38] Preferences for trade in goods under the terms of CEPA will have to be extended to all other WTO Members as neither China nor Hong Kong has made such an exception from MFN treatment.

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[36] For a more detailed discussion of the trade effects of these measures, see Y.S. LEE, RECLAIMING DEVELOPMENT IN THE WORLD TRADING SYSTEM chs. 3–4 (forthcoming 2006).

[37] Article II:1 of 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." *Uruguay Round*, *supra* note 5, at 329.

[38] Annex on Article II Exemptions, *Uruguay Round*, *supra* note 5, at 352; GATT Art. II ¶ 2.

III. BILATERAL INVESTMENT TREATIES AND THE GATS

A. Investment and International Trade

Another area where bilateralism is important is investment. Foreign direct investment ("FDI") has increased over thirty-fold during the past two decades[39] and FDI and its regulation have become relevant to international trade. The impact of FDI regulation on trade is 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 each facility's output. The investors may export more than they would have without such a requirement, leading to an increase in exports from Country A. Alternatively, the government may require foreign investors to buy domestically-produced products instead of imported products which may in turn lead to a reduction in imports.

In order to prevent such "trade-distortion" caused by investment measures, WTO disciplines regulate certain trade-related investment measures ("TRIMs") in a rather brief set of rules entitled the Agreement on Trade-Related Investment Measures ("TRIMs Agreement"), which is comprised of nine articles and an annex.[40] The TRIMs Agreement prohibits investment measures that are inconsistent with Articles III and XI of the GATT, which requires national treatment and the general elimination of quantitative restrictions respectively.[41]

The Annex to the TRIMs Agreement provides an illustrative list of prohibited TRIMs.[42] The list includes:

> (1) local content requirements (imposing the use of a certain amount of local inputs in production); (2) import controls (requiring imports used in local production to be equivalent to a certain proportion of exports); (3) 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 (4) export controls (obligating exports to

[39] FDI outflows increased from 28 billion USD in 1982 to 612 billion USD in 2003, valued at current prices. U.N. Conference on Trade and Development [UNCTAD], *World Investment Report 2004 the Shift Towards Services* 9 (July 2004) (note Table 1.3: Selected Indicators of FDI and International Production, 1982–2003).

[40] Agreement on Trade-Related Investment Measures, *Uruguay Round, supra* note 5, at 163–67.

[41] LEE, *supra* note 36, at 116 (citing to GATT Article III regarding national treatment and to GATT Article XI regarding quantitative restrictions, *Uruguay Round*, *supra* note 5, at 427–29, 437).

[42] *Id.* at 117 (citing to Agreement on Trade-Related Investment Measures, *Uruguay Round*, *supra* note 5, at 166–67).

be equivalent to a certain proportion of local production).[43]

The rationale for this prohibition is that these particular TRIMs distort trade by requiring investors to make certain export or import commitments.[44]

"Nonetheless, the TRIMs Agreement is not meant to provide a comprehensive multilateral legal framework for investment."[45] The scope and the objective of the Agreement, which is to prevent the distortion of trade by TRIMs, seems too limited to be considered 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.[46] In the absence of a comprehensive, multilateral regulatory regime on investment a number of BITs have governed FDI.[47] Some developed countries believe that a multilateral agreement on investment that is more comprehensive than the TRIMs Agreement is desirable and have taken initiatives to begin discussions at the WTO.[48] However, this attempt has faced considerable resistance from some developing country members, such as India, who fear that extensive rules on investment might place considerable restraints on government measures and policies on foreign investment.[49] Also, doubt exists as to whether the WTO is the best international body to address investment issues.[50] Thus, uncertainty remains as to whether the initiatives to create a multilateral investment agreement at the WTO will prove

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[43] *Id.* at 116–17.

[44] *Id.* at 116.

[45] *Id.*

[46] *See supra* note 9; *see also* OECD, Agreement on Investment: Documentation for Negotiations, http://www1.oecd.org/daf/mai/intro.htm (last visited Jan. 18, 2006).

[47] World Bank, International Centre for Settlement of Investment Disputes, Bilateral Investment Treaties, http://www.worldbank.org/icsid/treaties/intro.htm (last visited Jan. 18, 2006) (finding over 1,100 BITs are known to exist and "more than 800 have been concluded since 1987"); *see also* RUDOLF DOLZER & MARGRETE STEVENS, BILATERAL INVESTMENT TREATIES (1995) (offering a comprehensive review of BITs).

[48] WTO, Ministerial Declaration of 20 November 2001, WT/MIN(01)/DEC/1, ¶¶ 20–22.

[49] *See* LEE, *supra* note 36, at 114–15 (finding that "governments of developing countries may" prefer to have latitude in prescribing investment policies to "maximize the contribution of foreign investment" to their "development objectives").

[50] T.N. Srinivasan highlighted:

> [t]he 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.

International Institute for Sustainable Development, Report on the WTO High-Level Symposium on Trade and Development (March 17–18, 1999), http://www.wto.org/english/tratop_e/envir_e/sumhldev.pdf.

successful.

B. Bilateral Investment Treaties and GATS

As discussed above, over 1,100 BITs regulate FDI on a bilateral basis and their consistency with certain core provisions of WTO disciplines applying to trade in services is questionable. The general purpose of a BIT is to provide national treatment to the investors of the other signatory country.[51] The specific terms of numerous BITs are by no means identical but BITs typically require non-discriminatory treatment for foreign investors with respect to the admission and regulation of investment, prohibit certain government investment measures,[52] guarantee transfer of capital and liquidation of investment, protect foreign investment against arbitrary expropriation, and provide a fair and effective dispute resolution process.[53] 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 provide exclusive preference to investors from the other signatory country. Where this preference for foreign investment facilitates the supply of a service, it is then also subject to the jurisdiction of GATS, which applies to trade in services.[54] GATS prescribes that the supply of services can be made through "commercial presence in the territory of any other member."[55] 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 GATS is applied to this preference. Article II:1 of 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."[56]

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

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[51] 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.

[52] Agreement on Trade-Related Investment Measures, *Uruguary Round*, *supra* note 5, at 166–67 (listing examples under the annex of the TRIMs Agreement).

[53] *See* DOLZER & STEVENS, *supra* note 47.

[54] 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.

[55] Article I.2 GATS, *Uruguary Round*, *supra* note 5, at 328.

[56] Article II.1 GATS, *Uruguary Round*, *supra* note 5, at 329.

MFN requirement of GATS, under which such preference should be extended to all other WTO Members. GATS, unlike the GATT, does not require national treatment as a general principle since national treatment applies only to the service sectors that have been scheduled for market access, subject to the limitations and qualifications therein.[57] Thus, 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 GATS to the extent that the stated exceptions under the Annex on Article II are not applied.[58] GATS does not have a GATT Article XXIV-type exception to the MFN requirement that allows regional trade arrangements and no other provision exists in GATS that exempts 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 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 preferences stipulated in the BIT and the MFN requirement under GATS. Korea felt this problem was solved because the Korean regulatory practice required that any preference agreed to in bilateral investment treaties be incorporated in relevant laws and regulations that are applied to *all* foreign investors.[59] If preferential treatment of BITs that facilitate the supply of services are made generally applicable to all foreign investors, as is the Korean practice, it will then meet the MFN requirement under Article II of 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 that BIT.[60]

Another way to avoid the conflict is to mark the exemption of the MFN requirements under Article II.2 of GATS in the specific sectors scheduled. However, it is required that these exemptions be in place already at the entry into force of the WTO Agreement,[61] and any subsequent exemptions can only be made by waiver under Article IX of the WTO

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[57] Article XVII GATS, *Uruguary Round*, *supra* note 5, at 342–43.

[58] Annex on Article II Exemptions GATS, *Uruguary Round*, *supra* note 5, at 352.

[59] In Korea, laws and regulations that provide investment preferences are not drafted to grant preferences exclusively to a certain group of foreigners but instead they provide preferences to all foreigners.

[60] DOLZER & STEVENS, *supra* note 47, at 65–66.

[61] Marrakesh Agreement Establishing the World Trade Organization, *Uruguay Round*, *supra* note 5, at 6–18.

Agreement, which requires a decision based on consensus at the Ministerial Conference.[62] Unlike national treatment, the MFN requirement is more difficult to waive under GATS and acquiring MFN exemptions to preserve exclusive preferences under BITs will be extremely cumbersome, if not entirely impossible.

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 GATS and there may be vested interests to maintain exclusive preferences. On the other hand, 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, whose export industries may not be competitive enough, will have more difficulties. The MFN principle of 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 supply of a service) are inherently inconsistent with the objectives of the multilateral trading system to facilitate non-discriminatory trade among *all* nations when these bilateral arrangements attempt to preserve exclusive preferences among the participating member countries. These preferences may facilitate trade among the participants, but may also 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 concerns. WTO Members may feel pressure to join these exclusive trade-clubs so as not to be left out. 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 these new types of RTAs for economic and other incentives offered by powerful economies that promote such RTAs. Creating another layer of trade disciplines beyond what has been established under the WTO could

[62] *Id.* at 11.

undermine the consistency of global trade disciplines.

Convergence, 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, 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 GATS, the enforcement of the MFN requirement in GATS will work to expand trade-related preferences in BITs to all WTO members.