

WTO-X aspects of recent RTAs

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Abstract

Regional trade agreements (RTAs) have not only become increasingly prevalent but also changed qualitatively. They go beyond traditional tariff reduction and the WTO mandates, to cover issues lying outside the WTO, which are called “WTO-X”. The evolution of such RTAs is related to the internationalization of supply chains. New features of recent RTAs raise a number of issues in understanding their effects and consequences.

1. Introduction

Since the early 1990s, regional trade agreements (RTAs) have become increasingly prevalent. The WTO reports that as of January 2012, some 511 notifications of RTAs (counting goods and services separately) had been received by the GATT/WTO. Of these, 319 were in force¹.

The growing number of RTAs is well known, but it is important to note that there have been significant expansions in the contents of the RTAs going beyond the WTO mandates, which is the focus of this paper. Horn et al. (2010) started the analysis of such recent aspects of RTAs. Their idea is to divide the contents of the RTAs into 14 ‘WTO+’ and 38 ‘WTO-X’ areas. WTO+ provisions are the ones that come under the current mandate of the WTO, and WTO-X provisions are those that deal with issues lying outside the current WTO mandate.

The focus of Horn et al. (2010) was on EC and U.S. RTAs with other countries. WTO (2011) extended the study by covering 96 RTAs of the world to find that in recent RTAs, commitments in services, investment, intellectual property rights, technical barriers to trade, and competition policy have become significant. This is the qualitatively important feature of today’s RTAs.

This paper reviews the literature on WTO-X aspects of recent RTAs, and aims to provide issues and prospects of RTAs and the WTO. The next section summarizes in more detail what Horn et al. (2010) and WTO (2011) have found about WTO+ and WTO-X. The argument by Baldwin (2011) on why RTAs have changed like this is introduced in section 3. Section 4 briefly reviews what has been thought about on the economic impacts of RTAs. Section 5 considers potential economic implications of recent RTAs that contain WTO-X provisions. Section 6 looks into a particular RTA as a case study. Section 7 offers a preliminary view on issues and prospects relating to RTAs and the WTO.

2. WTO+ and WTO-X provisions in RTAs

Horn et al. (2010) applied the WTO+ and WTO-X classifications to the RTAs involving the EC and the U.S. They have also evaluated the texts from the viewpoint of legal enforceability, that is, whether the texts specify clear obligations. Their finding, among others, is that a substantial portion of the agreements goes way beyond traditional tariff reductions to include issues not covered in the WTO². RTAs are no longer agreements solely on preferential tariff reduction. Table 1 lists the 14 areas under the current WTO mandate along with other 38 WTO-X areas outside the mandate. WTO (2011) extended the approach by Horn et al. (2010) by covering 96 RTAs of the world. While it is found that tariffs are becoming less important in the RTAs worldwide, the WTO study also finds that in recent RTAs, commitments in services, investment, intellectual property rights, technical barriers to trade, and competition policy have become significant. This is an important new characteristic of recent RTAs.

Further, according to WTO (2011), average number of WTO+ areas covered by RTAs has been increasing. WTO-X provisions have been increasing as well, except for the decline in the 1990s. One difference between the WTO+ and the WTO-X provisions is that the WTO+ provisions appear to be more enforceable: While most WTO+ provisions during the years 2000-2010 are enforceable, on average less than half of the WTO-X provisions during the same period are considered enforceable.

Turning to the areas covered, competition policy, intellectual property rights, investments, and movement of capital are the main WTO-X provisions. It is found that these are also the most legally enforceable provisions. The next largest groups of legally enforceable provisions are environmental laws, labor market regulations, and visa and asylum.

In terms of country characteristics, RTAs between developed and developing countries contain on average a higher number of enforceable WTO+ provisions. They also contain higher number of WTO-X provisions, although many are not enforceable. Agreements between developed countries have the highest number of enforceable provisions. RTAs between developing countries have the

Table 1: WTO+ and WTO-X provisions in RTAs

WTO+ (WTO mandate)	WTO-X (Outside current WTO mandate)	
1 Industrial tariffs	1 Competition policy	20 Approximation of legislation
2 Agricultural Tarrifs	2 Intellectual property rights	21 Statistics
3 Customs	3 Investment	22 Human rights
4 Anti-dumping	4 Movement of capital	23 Political dialogue
5 Counterveiling measures	5 Environmental laws	24 Economic policy dialogue
6 Export tax	6 Agriculture	25 Illicit drugs
7 Technical barriers to trade	7 Research and technology	26 Money laundering
8 CATS	8 Regional cooperation	27 Anti-corruption
9 TRIPS	9 Education and training	28 Data protection
10 State aid	10 Energy	29 Audiovisual
11 Public procurement	11 Labor market regulation	30 Illegal immigration
12 SPS measures	12 Industrial cooperation	31 Mining
13 State trading enterprises	13 Visa and asylum	32 Taxation
14 TRIMS	14 Cultural cooperation	33 Health
	15 Social matters	34 Public administration
	16 Financial assistance	35 Terrorism
	17 Consumer protection	36 Nuclear safety
	18 Information society	37 Innovation policies
	19 SMEs	38 Civil protection

Note: Ordered in terms of frequency

Source: Original table by Horn et al. (2010) modified using the results by WTO (2011)

smallest number of WTO-X provisions.

It is somewhat puzzling why non-enforceable provisions are included in the RTAs, although it could be that such provisions are to be finalized later in future negotiations. Sokol (2008) offers some reasons why RTAs have non-enforceable competition policy provisions, from a South American perspective. It includes symbolic value, facilitation of relationships across antitrust agencies, and signaling domestic constituencies. Indeed, building relations across antitrust agencies could contribute to the capacity building of their staffs, particularly of those in the developing countries. In any case more needs to be done to understand the background of these WTO-X provisions and their implications and consequences.

3. Why have recent RTAs gone beyond the WTO?

The structure of trade has become complex following the supply chain internationalization, resulting in the kind of trade known as outward processing and/or vertical processing trade. World trade has become qualitatively different compared to that in the previous centuries when mainly final goods were shipped across countries in manufacturing. Behind this are the extremely large North-South wage differences that motivate the firms to geographically unbundle their production

process, and the ICT revolution that enables them to do so (Baldwin (2011)).

Such change in the production structure calls for RTAs that contain the WTO+ and WTO-X provisions, in addition to tariff reductions, as described in the previous section. Specifically, the internationalization of supply chain requires less restriction on international movement of capital and on investment, and firms competing in the knowledge-based economy today demand proper protection of intellectual property. Such WTO+/WTO-X agreements were made possible not only because the Northern government had responded to the needs of their global firms, but also because governments in the South recognized the importance of taking part in the international supply chain for domestic employment and technological transfer.

4. Traditional views on RTAs

One of the most popular terms when it comes to RTAs is 'trade diversion'. The work by Viner (1950) raised awareness that preferential tariff reduction in RTAs can cause trade to be diverted to inefficient countries, leading to global loss in economic welfare.

Another issue raised by Bhagwati (1995) is known as the "spaghetti bowl" phenomenon which is about the additional costs arising from having to manage various RTAs. In particular, the rules of origin, that is necessary in a FTA to identify the nationalities of goods, becomes a burden in terms of judicial and administrative costs, at the expense of consumers. Kawai and Wignaraja (2009) studied whether there is a "spaghetti bowl" problem in Asia. (They have called it the "noodle bowl" problem instead.) Based on firm surveys, it is revealed in their study that the problem does exist, but somewhat limited to large firms exporting to multiple destinations.

In addition, applying political economy analyses, Levy (1997) among others started considering mechanisms of how regionalism affects multilateralism. For those who believe in multilateral trade liberalization, it is worrying whether RTAs eventually lead to the realization of multilateral trade liberalization. Levy (1997) finds that the multilateral trade liberalization halts in a trade model of product differentiation combined with voting, when the gains from trade are unequally distributed among the voters, while it does not occur in a Heckscher-Ohlin framework.

The above mentioned studies in the late 20th century are therefore somewhat negative on the use of RTAs, from various viewpoints. One exception is by Baldwin (1993) who presented the 'domino theory' to show that RTAs with simply tariff reductions can be building blocks of multilateral free trade. The analysis is based on a differentiated goods trade model using monopolistic competition, with a political economy feature as in Grossman and Helpman (1994). It is applied to EC expansion. Non-EC governments consider the social welfare, political donation, and their nation's non-economic resistance to becoming a member. Countries differ in the level of non-economic resistance. As the

membership increases, the increased size of the EC market promotes more countries to join in order of the level of the resistance³.

Empirical studies investigating whether RTAs are stumbling blocks for multilateral trade liberalization are now available. The results are, however, somewhat mixed. An econometric study by Limão (2006) shows that U.S. RTAs are stumbling blocks to multilateral trade liberalization. More recently, Baldwin and Seghezza (2010) find RTAs are neither stumbling blocks nor building blocks.

Much of exiting literature has focused, naturally, on the tariff reduction aspect of RTAs. In the meantime the RTAs in the real world have developed differently, as reviewed in the previous sections.

5. Potential impact of recent RTAs – preferential applicability and third country impact

As the Horn et al. (2010) and the WTO (2011) studies indicate, recent RTAs are not only about preferential tariff reduction but include WTO+ and WTO-X provisions that go beyond the coverage of WTO. The main WTO-X provisions in terms of frequency and enforceability are competition policy, intellectual property rights, investments, and movement of capital. One important aspect of these WTO-X provisions is that they are not necessarily applicable in a preferential manner to a specific country/product, unlike tariffs. Therefore, tariff analyses, on which the existing studies focus, cannot be applied to many of the WTO-X provisions.

The fact that RTAs are not just about tariffs raises new issues on forecasting the economic impact of RTAs. Studies forecasting the economic impacts of RTAs, typically using CGE techniques, understandably calculate the price effects of tariff reduction to which the economic agents respond. Results from these studies offer important guidance, but if one fully takes into account the WTO-X aspects of RTAs, the results may well be very different, although it is practically difficult to implement such a task.⁴

The issue of preferential applicability can be illustrated from measures taken in trade facilitation, although it is a WTO+ rather than a WTO-X area. The complexity is that some measures of trade facilitation can be applied preferentially but others may not. An electronic system of certifying ROO documents will enable the importing foreign country to check the ROO document online using the database created at the country of origin. This facilitates trade between the two countries, benefiting the firms in the exporting country and the importer. It is an example of preferential application of a trade facilitation measure. On the other, if facilitation is about capacity building of the officials at the customs border, it cannot be applied preferentially; the benefit from it is likely to spillover to third countries that export to the RTA economies.

If the WTO-X provisions in RTAs help to improve the business environment of the members of an RTA, third country firms are also likely to benefit from this. Examples of such areas may include competition policy, intellectual property rights, investment, movement of capital, labor market regulation, and anti-corruption.

On the other, environmental laws and consumer protection could mean different regulations being introduced in the RTA members. This may imply that third country firms face different regulations in home and in the RTA member countries, which could become an obstacle for the third country firms.

WTO-X areas also include agreements on specific sectors, such as agriculture, energy, and mining. Much cannot be said in general on the third country impacts of these provisions, since they will depend heavily on what is actually agreed upon in these sector specific provisions.

Eventually it is of interest to see whether the WTO-X RTAs contribute to other larger regional schemes such as the Asia-Pacific Economic Cooperation (APEC) and of course the WTO. In fact APEC, which has been working on (concerted) unilateral most-favored-nation based trade liberalization, now views RTAs as “another way for APEC to make progress towards achieving the Bogor Goals of free and open trade and investment (APEC (2012)).”

6. An example: Japan-Philippines Economic Partnership Agreement (JPEPA)

This section takes a closer look into some of the features of recent RTAs by focusing on a particular RTA. The example raised here is Japan-Philippines Economic Partnership Agreement (JPEPA), a typical North-South free trade agreement (FTA) formed between the two countries in 2002.

Table 3 lists the chapters in JPEPA. Among these, investment, intellectual property, competition, and improvement of business environment can be considered as WTO-X chapters. These are

Table 3: Contents of JPEPA

Chapter	Content	Chapter	Content
1	General Provisions	9	Movement of natural persons
2	Trade in Goods	10	Intellectual property
3	Rules of Origin	11	Government procurement
4	Customs Procedures	12	Competition
5	Paperless trading	13	Improvement of the business environment
6	Mutual recognition	14	Cooperation
7	Trade in services	15	Dispute avoidance and settlement
8	Investment	16	Final provisions

Source: Agreement between Japan and the Republic of the Philippines for an economic partnership.

mostly in line with what WTO (2011) indicated as the frequently observed WTO-X provisions.

Competition policy is addressed as follows in Chapter 12 of JPEPA:

Chapter 12 Competition

Article 135 Promotion of Competition

by Addressing Anti-competitive Activities

1. Each Party shall, in accordance with its applicable laws and regulations, take measures which it considers appropriate to promote competition by addressing anticompetitive activities, in order to facilitate trade and investment flows between the Parties and the efficient functioning of its market. Any such measures shall be taken in conformity with the principles of transparency, non-discrimination and procedural fairness.

2. Each Party shall, when necessary, review and improve or adopt laws and regulations to effectively promote competition by addressing anti-competitive activities.

Article 136 Cooperation on Promoting Competition

by Addressing Anti-competitive Activities

1. The Parties shall, in accordance with their respective laws and regulations, cooperate in the field of promoting competition by addressing anti-competitive activities, subject to their respective available resources.

2. The details and procedures of cooperation under this Article shall be specified in the Implementing Agreement.

Summarizing Chapter 12 on competition, as pointed out by Sokol (2008), the contents of the provision do not appear to be enforceable; in fact, it is basically composed of statements on promotion of competition, review/improvement of laws and regulations, and cooperation between the authorities of Japan and the Philippines. It can be said, however, that it will contribute to the capacity building of the authorities, and help to improve the fairness of both markets.

In contrast, Chapter 10 on intellectual property is much more detailed, and goes much further than simply cooperation, and includes articles on “Streamlining and Harmonization of Procedural Matters”, “Promotion of Public Awareness Concerning Protection of Intellectual Property”, “Unfair Competition”, and finally an article on “Enforcement”.

Interestingly, JPEPA has another chapter titled “Improvement of the Business Environment” (Chapter 13). It is documented that a sub-committee, a consultative group, and a liaison office will be set up to improve the business environment. This clearly indicates that JPEPA is agreed upon by the two governments as a response to the demand from the business sector that organizes internationalized supply chains.

7. Issues and prospects on RTAs and the WTO

RTAs have changed substantially as reviewed in this paper. The categorization of the contents into WTO+ and WTO-X are helpful in understanding their qualitative changes. However, when one thinks of their effects it is necessary to look into the agreements to see what is actually intended. As reviewed in the case of JPEPA, a competition policy chapter may simply indicate the cooperation between the two country's antitrust agencies and their capacity building. Instead, a competition policy chapter may contain introduction of particular policy measures in the RTA members. If it changes the competition environment within the RTA members, it could then have significant impact on the third country firms.

Another example is intellectual property rights. Given that regimes on intellectual property are not necessarily harmonized across countries today, different RTAs can establish different kinds of regimes. We will then see a competition of rules, which may hinder the multilateral liberalization process.

Many RTAs contain non-enforceable provisions. These made be left as they are, but they could also be updated in later negotiations as enforceable provisions. In this sense, it could be said that many of the RTAs are not fixed and have the potential to evolve into different schemes.

The apparent halt of the Doha talks and the proliferation of WTO-X RTAs could mean that the role of WTOs is being undermined. Hufbauer and Schott (2012) analyze that despite the failure of the Doha round, the WTO does have new roles to play. They raise a number of new areas in which the WTO should take part as its next steps. The areas include WTO-IMF coordination on currency undervaluation, greenhouse gas and energy measures, and rules of the road for state owned enterprises (SOEs). These remaining global issues indeed need to be considered as they are not necessarily covered by the WTO-X RTAs.

Notes

- 1 I stick to the term RTA to describe various types of reciprocal trade agreements between two or more partners.
- 2 They also point out the differences between the EC and U.S. agreements. The former contain almost four times as many instances of WTO-X provisions. The provisions in the EC agreements, however, are less legally enforceable. U.S. agreements tend to emphasize regulatory areas more.
- 3 More recent argument for regionalism as building blocks to multilateral trade liberalization can be found in Baldwin (2004).
- 4 Kim et al. (2010) estimate the impact of the creation of the Free Trade Area of Asia Pacific (FTAAP) on the world economy. In addition to tariff reductions, they take into account the effect of trade facilitation as well as liberalization in services trade.

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