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Entrenchment of regionalism: WTO legality of MFN clauses in preferential trade agreements for goods and services

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Abstract: The most favoured nation (MFN) clauses in preferential trade agreements (PTAs) under GATT Article XXIV or under GATS Article V entrench the preferential trade relations between the PTA parties because the trade liberalization in future PTAs with third parties will be constrained by the existing PTA MFN clauses. Trade liberalization based on PTA MFN clauses cannot be considered part of the internal trade liberalization required by GATT Article XXIV:8 or GATS Article V:1. The exclusionary effects caused by trade liberalization through PTA MFN clauses increase the burden on trade with third parties. As a result, PTA MFN clauses do not meet the necessity test under the Appellate Body's decision in *Turkey–Textiles*, as reasonable alternatives to the PTA MFN clauses are available. For these reasons, PTA MFN clauses fail the requirements for legal defences under GATT Article XXIV or GATS Article V for their violations of the general MFN clauses under GATT Article I and GATS Article II. For those products or services subject to existing PTA MFN clauses, any preferential liberalization based on PTA MFN clauses should be accorded non-discriminatorily to all WTO members in accordance with GATT Article I or GATS Article II.

1. Introduction

The general most-favoured nation (MFN) clauses under Article I of the General Agreement on Tariffs and Trade (GATT) 1994 and Article II of the General Agreement on Trade in Services (GATS) form the 'cornerstone' of international rules that regulate the world trading system under the World Trade Organization (WTO).[1] However, the world trading system is undermined by

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1 GATT Article I and GATS Article II, respectively, provide the general non-discrimination principles for trade in goods and for trade in services in the world trading system under the World Trade

preferential trade agreements (PTAs), which infringe on the general MFN clauses. Although PTAs that meet the requirements of legal defence under GATT Article XXIV or GATS Article V are permitted under the WTO, they nevertheless cause exclusionary effects to trade with third parties.[2] The exclusionary effect is made worse by PTA MFN clauses in some PTAs, which provide that PTA parties will accord no less favourable treatment to goods and services from each other than to those from third parties. The MFN clauses in PTAs have the effect of entrenching preferential trade liberalization in PTAs because a higher level of trade liberalization with third countries is more difficult to achieve, as trade liberalization to third countries in future PTAs must be accorded to the parties to the existing PTAs with MFN clauses.[3] The entrenchment of preferential trade liberalization caused by PTA MFN clauses further undermines the WTO's aim of eliminating 'discriminatory treatment in international trade relations'.[4]

This paper studies the WTO legality of PTA MFN clauses in regional trade agreements (RTAs) under GATT Article XXIV and economic integration agreements (EIAs) under GATS Article V.[5] Following the introduction, section 2 reviews the general MFN clauses – Article I of the GATT and Article II of the GATS. Then, section 3 introduces the historical MFN clauses in pre-GATT friendship, commerce, and navigation (FCN) treaties and discusses various MFN clauses in the PTAs that are notified to the WTO. The section then further proceeds to examine whether the MFN clauses in RTAs and EIAs conform to WTO law. Section 4 concludes by suggesting how PTA MFN clauses should be brought into conformity with the WTO system.

Organization (WTO). See Executive Branch GATT Studies, No. 9, The Most-Favoured-Nation Provision, Subcommittee on International Grade, Committee on Finance, US Senate, US Government Printing Office, Washington, DC, 1973, at 1, available at www.finance.senate.gov/library/prints. The term MFN is often used in confusion to refer to both general MFN clauses under the GATT or GATS as well as MFN clauses under PTAs.

2 Econometric studies provide evidence for exclusionary effects from PTA formations. See Wong Chan and L. Alan Winters, 'How Regional Blocs Affect Excluded Countries: The Price Effects of Mercosur', **92** (4) *American Economic Review* 889 (2002), at 901. Exclusionary effects are also caused by RTAs that adopt restrictive preferential rules of origin. See Anne O. Krueger, 'Are Preferential Trading Arrangements Trade-Liberalizing or Protectionist?', **13** *The Journal of Economic Perspectives* 105 (1999), at 113.

3 See Carsten Fink and Marion Jansen, 'Services Provisions in Regional Trade Agreements: Stumbling Blocks or Building Blocks for Multilateral Liberalization?', in Richard Baldwin and Patrick Low (eds.), *Multilateralizing Regionalism* (Cambridge: Cambridge University Press, 2009), pp. 221–261 at 247. In a hypothetical situation, where PTA MFN clauses are universally adopted in all PTAs by WTO members, the effect of PTA MFN clauses may emulate the GATT Article I and GATS Article II.

4 See the preamble of the Marrakesh Agreement Establishing the World Trade Organization (WTO Agreement) for the aims of the WTO, reprinted by the WTO in 1995 in *The Legal Texts: The Results of the Uruguay Round of Multilateral Trade Negotiations*.

5 A PTA under GATS Article V is called economic integration agreement (EIA) in this paper. The rise in the number of PTAs has accelerated since the early 1990s. As of January 2013, some 354 PTAs are in force. See 'Trade Topics', *Regional Trade Agreements*, the WTO, available at http://www.wto.org/english/tratop_e/region_e/region_e.htm (visited 20 March 2013).

2. General most-favoured nation treatment

2.1 *General MFN for trade in goods*

GATT Article I, entitled 'General Most-Favoured-Nation Treatment', lays down the most important principle underpinning the multilateral trading system for trade in goods under the WTO. GATT Article I requires that the treatment by a WTO member accorded to goods imported from or destined for any other WTO member should not be less favourable than that accorded to any other country, thus multiplying the effects of trade concessions in goods given to any country to all WTO members. GATT Article I has served the important role of bringing within the GATT system the preferential trade agreements that existed prior to 1948. In comparison to another non-discrimination principle, GATT Article III (National Treatment on Internal Taxation and Regulation), GATT Article I has an elevated status by its inclusion in Part I of GATT 1994, which requires unanimous consent by all WTO members for its amendment.[6] Notwithstanding the importance of GATT Article I, the GATT system permits a lawful derogation from GATT Article I when WTO members form RTAs.

2.2 *General MFN for trade in services*

GATS Article II provides the general MFN obligation for trade in services. According to paragraph 1 of GATS Article II, a WTO member should accord to services and service suppliers of any other WTO members treatment no less favourable than it accords to like services and service suppliers of any other country.[7] As with GATT Article I for trade in goods, Article II of the GATS is the most important principle underpinning the multilateral trading system for trade in services.[8] In parallel with the GATT, the GATS permits lawful derogations from the MFN principle under GATS Article II when WTO members establish EIAs for trade in services under GATS Article V.[9] Despite the similarity in the MFN clauses under GATT Article I and GATS Article II, the MFN principle under GATT Article I for trade in goods may not easily transfer to trade in services under GATS

6 See Article X:2 of the WTO Agreement. Part I of the GATT was fully implemented without exception under the Protocol of Provisional Application in January 1948. See para. 1, United Nations Economic and Social Council, concluded in 1947, E/PC/T214.Add.2 Rev.1, http://gatt.stanford.edu/page/home (visited 28 February 2013). Amendment of Part I of GATT 1994 requires acceptance by all WTO members, whereas amendment of other GATT 1994 provisions including GATT Article III in Part II requires acceptance by only a two-thirds majority of WTO members. See Article X:3 of the WTO Agreement.

7 GATS Article II:1.

8 GATS Article II:1, which lays out the MFN principle, also requires unanimity for its amendment. See Article X:3 of the WTO Agreement.

9 In contrast to GATT Article XXIV, GATS Article V does not provide for a separate definition of a preferential agreement in services that is analogous to a customs union.

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Article II.[10] The difference in the two principles can be found in the fact that GATT Article I is applicable only to the treatment of goods, whereas GATS Article II applies to services as well as service suppliers. Another important contrast is that GATS Article II incorporates 'built-in' exemptions from the general MFN principle when a WTO member lists the exempted measures in the Annex on Article II Exemptions of the GATS, whereas GATT Article I does not provide similar exemptions.[11]

3. Legality of MFN clauses in PTAs

3.1 Historical MFN clauses: pre-GATT FCN treaties

MFN clauses in today's PTAs have their historical origin in MFN clauses in bilateral FCN treaties concluded between the United States (US) and its trading partner during pre-GATT years. FCN treaties were 'the most familiar instruments known to diplomatic tradition'.[12] In these FCN treaties prior to the establishment of the GATT, incumbent parties to the treaties often provided MFN clauses with respect to the trade in goods to ensure that future trade agreements entered into by their bilateral partner country with third parties would not undermine the preferential benefits they earned through the FCN treaties.[13] The MFN clauses in the pre-GATT FCN treaties provided at a minimum that the trade between the FCN parties would not be given less favourable treatment than the trade with third countries.

To illustrate an MFN clause in FCN treaties, the Treaty of Friendship, Commerce and Navigation between Argentina and the US in 1853 (US–Argentina FCN Treaty) contains the following MFN provision:

> No higher or other duties shall be imposed on the importation into the territories of either of the two contracting parties of any article of the growth, produce or manufacture of the territories of the other contracting party, than are, or shall be, payable on the like article of any other foreign country; nor shall any other or higher duties or charges be imposed in the territories of either of the contracting

10 See John H. Jackson, *The World Trading System, Law and Policy of International Economic Relations*, 2nd edn (Cambridge, MA: The MIT Press, 1998), p. 157.

11 A WTO member is exempted from its obligations under paragraph 1 of GATS Article II for those measures listed in the Annex on Article II Exemptions of the GATS. See GATS Article II:2.

12 Herman Walker Jr., 'Modern Treaties of Friendship, Commerce and Navigation', **42** *Minnesota Law Review* 805 (1958), at 805.

13 Bilateral MFN clauses were frequently included in the FCN treaties enacted in the 1800s and 1900s before the GATT. See John Jackson, *The World Trading System, Law and Policy of International Economic Relations*, 2nd edn (Cambridge, MA: MIT Press, 1998), p. 158. See, for an earlier example, Article The Second, 'A Convention to Regulate the Commerce between the Territories of The US and of His Britannick Majesty', done on 3 July 1815, available at http://avalon.law.yale.edu/19th_century/conv1816.asp (visited 22 February 2013).

> parties on the exportation of any article to the territories of the other . . . which shall not equally extend to the like article of any other foreign country.[14]

The MFN clauses in pre-GATT FCN treaties, such as the US–Argentina FCN Treaty, were applicable only to the parties to the FCN treaty. As a result, non-parties to the FCN treaty did not benefit from the preferential treatment exchanged between the FCN treaty parties. Although the FCN treaties during the pre-GATT years were preferential commercial treaties between the parties to FCN treaties, they should be distinguished from PTAs during the GATT and WTO years. In contrast to PTAs during the GATT and WTO years, no question existed about the legal conformity of the pre-GATT FCN treaties to a multilateral system, because they were not operating in a multilateral trading regime that prohibited discriminatory treatment of goods and services from members of the multilateral trading regime. However, during the GATT years, the question was raised as to how the MFN clause in an FCN treaty would operate under the GATT for those FCN treaties in force under the GATT such as the US–Germany FCN Treaty.[15] To resolve this conflict, the US–Germany FCN Treaty explicitly gave the GATT priority over the provisions of the FCN treaty.[16]

3.2 MFN Clauses in PTAs under the WTO

Why do PTAs under the WTO provide MFN clauses? The answer can be deduced from the fact that PTAs usually do not achieve trade liberalization between the PTA parties to the fullest extent possible. For RTAs, GATT Article XXIV:8 requires that 'duties and other restrictive regulations of commerce (ORRC)' with respect to 'substantially all the trade' in goods traded between the RTA parties should be eliminated. The rule does not require that 'all' duties and ORRC be eliminated. As a result, there is room for additional trade liberalization even after an RTA fully completes its formation in accordance with GATT Article XXIV:8.[17] For EIAs, similarly, GATS Article V:1 requires that an EIA have 'substantial sectoral coverage' and provides for 'the absence or elimination of substantially all discrimination' in those sectors between the parties within the meaning of national treatment under GATS Article XVII. A likely result of this requirement is that, even

14 See Article IV, Treaty of Friendship, Commerce and Navigation Between Argentina and the US, entered into force on 20 December 1854, 10 Stat. 1005, available at http://avalon.law.yale.edu/19th_century/argen02.asp (visited 29 January 2013).

15 The Friendship, Commerce and Navigation Treaty between the US of America and the Federal Republic of Germany (US–Germany FCN Treaty), entered into force 14 July 1956, 7 UST 1839, TIAS 3593.

16 Article XXIV of the US–Germany FCN Treaty provides that 'The provisions of the present Treaty relating to the treatment of goods shall not preclude action by either Party which is required or permitted by the General Agreement on Tariffs and Trade during such time as such Party is a contracting party to the General Agreement.' Ibid.

17 See GATT Article XXIV:8(a)(i) for a customs union and GATT Article XXIV:8(b) for a free-trade area.

after the intra-EIA trade liberalization meets the internal trade requirement under GATS Article V:1, there is room for additional intra-EIA trade liberalization. The additional room for trade liberalization between the existing PTA parties in most PTAs raises the possibility that a PTA party may accord more favourable treatment to a third party through a new PTA with that party. Therefore, the parties to the existing PTAs have incentive to provide PTA MFN clauses to assure that they will not receive less favourable treatment than that accorded to a third party. In the following, we first provide an overview of MFN clauses in RTAs and EIAs separately and then examine their legality under the WTO law.

3.2.1 MFN clauses in RTAs under GATT Article XXIV

RTA MFN clauses are not universally found in RTAs.[18] Aside from MFN clauses, some RTAs provide clauses regarding opportunity to negotiate for MFN treatment in the future. In these clauses, whether MFN treatment will be granted will depend on the outcome of the consultation between the RTA parties.

(1) Overview of MFN clauses in RTAs

(a) MFN clauses in US RTAs

The MFN clauses found in the US–Morocco FTA, the US–Peru FTA, and the US–Chile FTA are product-specific MFN clauses that are applicable to a limited number of products.[19] The MFN clauses impose one-sided MFN obligations on the US's RTA partner but not on the US.

In the US–Morocco FTA, for various rice and barley products falling under HS Code 1006 (rice) and 1003 (barley), the MFN clause provides that, 'in the event that Morocco applies a mechanism that results in the application of a customs duty to such a good from any trading partner that is below the customs duty set out in the Tariff Schedule of Morocco pursuant to the Agreement, Morocco shall immediately apply the lower customs duty that results from that mechanism to US imports of that good'.[20] During the staging period of the Tariff Schedule of Morocco, if Morocco applies lower duties on the goods imported from any

18 In contrast to RTA MFN clauses, national treatment clauses are found in all RTAs. Jong Bum Kim, 'WTO Legality of Discriminatory Liberalization of Internal Regulations: Role of RTA National Treatment', **10**(4) *World Trade Review* 473 (2011), at 489.

19 The texts of the US – Morocco Free Trade Agreement (US–Morocco FTA), the US – Peru Trade Promotion Agreement (US–Peru FTA), and the US – Chile Free Trade Agreement (US–Chile FTA) are available at http://www.ustr.gov/trade-agreements/free-trade-agreements (visited 22 February 2013). The US–Morocco FTA, the US–Peru FTA, and the US–Chile FTA entered into force on 1 January 2006, 1 February 2009, and 1 January 2004, respectively.

20 See para. 2, Annex 1 to Morocco General Notes, Annex IV (Goods Schedule), the US–Morocco FTA, http://www.ustr.gov/trade-agreements/free-trade-agreements/morocco-fta/final-text (visited 22 February 2013).

other country than those applicable to the imports from the US, then Morocco is required to apply the lower duty to the imports originating from the US.[21]

The US–Morocco FTA also provides an MFN obligation for some of Morocco's imports from the US for which tariff-rate quotas (TRQs) are applied. The MFN clause provides that, '[i]n the event that Morocco grants or maintains with respect to any other trading partner *market access* better than that granted to the United States under this Agreement for any good listed … below, Morocco shall immediately grant such better *market access* to the United States' (emphasis added).[22] The use of the term 'market access' in the MFN clause brings TRQs within the scope of the MFN clause. In particular, the MFN clause applies to the TRQs for beef products.[23] Under the MFN clause, if the 'market access' accorded to beef products from any other country is more favourable than the TRQs accorded to beef products from the US, Morocco must grant such market access to the US.

The MFN clauses in the US–Morocco FTA referenced above apply to some products in which the US has strong export interests. To protect its export interests, the US tried to ensure that other countries would not receive more favourable access to Morocco's market than the US. To this end, the MFN obligation is triggered in all events where Morocco is giving more favourable treatment to the covered products from a non-party, irrespective of whether the more favourable treatment is granted unilaterally by Morocco or is based on an agreement under GATT Article XXIV or the Enabling Clause.[24]

Similarly, the US–Peru FTA contains an MFN clause with respect to duties applicable to some agricultural products.[25] The MFN clause applies to situations where third parties are given more preferential treatment in arrangements signed since 7 December 2005, a few months before the signing of the US–Peru FTA.[26] As another example, the US–Chile FTA provides an MFN clause to some limited categories of agricultural products.[27] In contrast to the US–Peru FTA, the MFN clause in the US–Chile FTA does not limit its scope to those arrangements by Peru with third countries signed after a certain date.

21 Ibid.

22 Ibid., para. 3.

23 Ibid., para. 6. The TRQ provides that the out-quota rate will remain at the MFN level while the in-quota rate will be reduced in ten equal annual stages with the aggregate quantity subject to in-quota rate annually specified.

24 See GATT Document, 'Differential and More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries', GATT Document, L/4903, Decision of 28 November 1979 (Enabling Clause).

25 See para. 2, Appendix I, General Notes, Tariff Schedule of the Republic of Peru, the US–Peru FTA, above n. 19. Agricultural goods are defined as those goods referred to in Article 2 of the WTO Agreement on Agriculture. See Article 2.22 of the US–Peru FTA.

26 The US–Peru FTA was signed on 12 April 2006. See above n. 19.

27 The products subject to the MFN treatment are wheat, wheat flours, and vegetable oils. See para. 3 (b), ANNEX 1 of Annex 3.3, General Notes, Tariff Schedule of Chile, the US–Chile FTA, above n. 19.

(b) MFN Clauses in ANZCERTA

The MFN clause in the Australia New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) provides that tariffs on imports of goods originating from the other party shall 'in no case be higher than the lowest tariff applicable to the same goods if imported from any third country'.[28] The MFN clause is applicable only to tariffs but not to quantitative restrictions. However, for both Australia and New Zealand, the MFN clause is not applicable when the imports from third countries are from those countries 'eligible for any concessional tariff treatment accorded to less developed countries'.[29] The MFN clause in ANZCERTA has the effect of constraining tariff liberalization by both Australia and New Zealand in future RTAs with third countries, because any lower tariffs accorded to any third party must be accorded to ANZCERTA parties.

In addition, ANZCERTA requires that 'the margin of preference' – the difference between the preferential tariffs under ANZCERTA and the tariffs that are applicable to goods that are not imported at preferential tariff rates – shall not be reduced 'wherever practicable' and that 'sympathetic consideration' should be given to maintain the margin of preference of at least at 5%.[30] The MFN clause and the clause on the margin of preference together will pose barriers to achieving a more enhanced level of tariff liberalization by both Australia and New Zealand in the future on imports from third countries through other RTAs or through multilateral trade rounds, thus causing the entrenchment of the preferential tariff liberalization under ANZCERTA.[31]

(c) Opportunity to negotiate for MFN treatment

Some RTAs provide clauses entitled 'Most-Favoured-Nation Treatment', which, however, provide RTA parties opportunities to negotiate in the future for MFN treatment (MFN-consultation clause). An example of an MFN-consultation clause is provided in the Singapore – European Free Trade Association (EFTA) FTA. It provides that, '[i]f a Party concludes a preferential agreement with a non-Party under Article XXIV of the GATT 1994, it shall, upon request from another Party, afford adequate opportunity to negotiate any additional benefits granted therein'.[32]

28 See Article 4, The Australia New Zealand Closer Economic Relations Trade Agreement (ANZCERTA), paras. 9 and 10, entered into force 1 January 1983, available at http://www.dfat.gov.au/fta/anzcerta/ (visited 1 March 2013).

29 Ibid. Additional exceptions are made with regard to Australia's imports from the Cook Islands, Niue, Tokelau and Western Samoa and with regard to New Zealand's imports from Papua New Guinea.

30 See above n. 28, Article 4 of ANZCERTA, para. 11. The MFN clause, as weakened by the qualifiers 'wherever practicable' and 'sympathetic consideration', cannot be interpreted as a binding obligation of the parties.

31 See above n. 3, for explanation of the entrenchment effect.

32 See Article 10 of the Singapore – European Free Trade Association FTA (Singapore–EFTA FTA), entered into force 1 January 2003, available at http://www.fta.gov.sg/fta_esfta.asp?hl=11 (visited 23 February 2013).

The obligation to accord an opportunity to negotiate MFN treatment is triggered if an RTA party enters into an RTA with a third party under GATT Article XXIV. However, the MFN obligation will not arise, for example, if a party grants preferential tariffs to developing countries under the Enabling Clause.[33]

Similarly, the India–Singapore CECA provides an MFN-consultation clause, which provides that, '[i]f a Party concludes a preferential agreement with a non-party, subsequent to the signing of this Agreement, it shall, upon request from the other Party, afford adequate opportunity to negotiate for the more favourable concessions and benefits granted therein'.[34] The MFN-consultation clause makes it clear that the obligation is triggered by any 'preferential agreement' entered into by an RTA party with a non-party. The term 'preferential agreement' encompasses RTAs under GATT Article XXIV and the Enabling Clause, allowing the possibility that India may enter into an RTA with a developing country under the Enabling Clause.[35]

The rationale for MFN-consultation clauses in Singapore's RTAs can be found in the fact that Singapore eliminates tariffs on all tariff lines while its RTA partners leave a significant percentage of tariff lines at positive levels under the RTA. In the India–Singapore CECA, Singapore eliminates tariffs on 100% of tariff lines on imports from India, whereas India eliminates tariffs on only 23.6% of tariff lines on imports from Singapore. In the Singapore–EFTA FTA, Singapore eliminates tariffs on 100% of tariff lines on imports from the EFTA, whereas the EFTA eliminates tariffs on 88% of tariff lines on imports from Singapore.[36] Singapore accepted the asymmetric exchange of tariff concessions in return for the promise that its RTA partners would provide adequate opportunity to renegotiate the deal with Singapore if they were to give more favourable concessions to a third party in future RTAs.

(2) Legality of MFN clauses in RTAs

MFN clauses in RTAs are inconsistent with GATT Article I, as they accord less favourable treatment to products from third countries with whom the RTA parties

33 The Enabling Clause permits preferential tariff treatment accorded by developed members of the WTO to products originating in developing countries in accordance with the Generalized System of Preferences. See paragraph 2(a) of the Enabling Clause, above n. 24.

34 See Article 2.11 of the India – Singapore Comprehensive Economic Cooperation Agreement (India–Singapore CECA), para. 3, entered into force 1 August 2005, available at http://www.fta.gov.sg/fta_ceca.asp?hl=6 (visited 23 February 2013).

35 The Enabling Clause permits arrangements between less-developed WTO members to accord preferential treatment to products imported from one another. See paragraph 2(c) of the Enabling Clause, above n. 24.

36 See WTO Document, Factual Presentation Comprehensive Economic Cooperation Agreement between India and Singapore, Report by the Secretariat, WT/REG228/1/Rev.1, 1 October 2008, at 8–9. See also WTO Document, Free Trade Agreements between The EFTA States and Singapore, Questions and Replies, WT/REG148/6, 26 April 2006, at 5. Note that all the reported calculation of tariff lines are based on HS 8-digit.

have not entered into other RTAs.[37] As measures taken by the RTA parties, the MFN clauses must fulfil the requirements of the legal defence under GATT Article XXIV in order to be consistent with the WTO law.[38] To determine whether a measure taken under an RTA meets the requirements under GATT Article XXIV, the WTO Appellate Body in *Turkey–Textiles* laid down a two-pronged test.[39] The first prong of the test requires that 'the measure at issue is introduced upon the formation of a customs union that fully meets the requirements of sub-paragraphs 8 (a) and 5(a) of Article XXIV'.[40] The second prong of the test – the necessity test – examines whether the formation of an RTA would be prevented if the RTA party were not allowed to introduce the challenged measure.[41] The necessity test will not be met if a 'reasonable alternative' to the challenged measure is available to the RTA party.[42]

Under the first prong of *Turkey–Textiles*, the 'timing' and 'legality' elements must be met.[43] The 'timing' element requires that the measure coincides with the formation of the RTA. The 'legality' element has two parts: the internal trade requirement under GATT Article XXIV:8 and the external trade barrier requirement under GATT Article XXIV:5. The first part of the legality element requires that 'duties' and ORRC be eliminated in 'substantially all the trade' (SAT) of goods originating in the RTA parties; the second part of the legality element prohibits RTA parties from taking measures that raise barriers to trade with third parties after the formation of an RTA as compared to before.

Under the timing requirement of the first prong of *Turkey–Textiles*, the issue is whether the measures based on RTA MFN clauses are 'introduced upon the formation of' an RTA. According to GATT Article XXIV:5(c), an RTA completes its 'formation' by transitioning from an 'interim agreement' to a final RTA within 'a reasonable length of time'. A reasonable length of time is viewed as exceeding

37 The WTO Appellate Body stated that 'any act or omission attributable to a WTO Member can be a measure of that Member for purposes of dispute settlement proceedings'. See Appellate Body Report, *United States – Sunset Review of Anti-dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan* (*US – Corrosion-Resistant Steel Sunset Review*), WT/DS244/AB/R, adopted 9 January 2004, para. 81. Thus, a provision of an international treaty such as the MFN clauses in RTAs to which a WTO member is a party is an act attributable to that WTO member and should be deemed a measure challengeable under the WTO dispute settlement proceedings.

38 An RTA MFN Clause falls within the scope of GATT Article XXIV defence because it is a GATT violating measure 'introduced upon the formation of' an RTA. See WTO Appellate Body Report, *Turkey – Restriction on Imports of Textiles and Clothing Products* (*Turkey–Textiles*), WT/DS34/AB/R, adopted 19 November 1999, para. 46.

39 Ibid., Appellate Body Report, *Turkey–Textiles*, para. 58.

40 Ibid.

41 Ibid. See also Joel P. Trachtman, 'Toward Open Recognition? Standardization and Regional Integration under Article XXIV of GATT', **6** *Journal of International Economic Law* 459 (2003), at 481.

42 See Appellate Body Report, *Turkey–Textiles*, above n. 38, para. 62.

43 See Lorand Bartels, 'The Legality of the EC Mutual Recognition Clause under WTO Law', **8** *Journal of International Economic Law* 691 (2005), at 712.

ten years only in exceptional cases.[44] If the measures based on an MFN clause are taken during the implementation of the interim agreement and before the formation of an RTA, the timing requirement is satisfied because the measures are introduced upon the formation of an RTA.[45] The 'timing' requirement has an additional wrinkle. The WTO panel in *US–Line Pipe* ruled that the measure in the case met the timing requirement as long as the basis of the measure – the safeguard provisions – was provided in the RTA.[46] As applied to RTA MFN clauses, even if the measures based on the RTA MFN clauses were adopted after the formation of an RTA, the timing requirement under *Turkey–Textiles* is deemed to be satisfied as long as the MFN clauses are included in the RTA upon its formation.

In addition to the timing element, the legality element must be satisfied under the first prong of the *Turkey–Textiles* test. The test requires that the RTA must conform to the internal trade requirement under GATT Article XXIV:8 and the external barrier requirement under GATT Article XXIV:5. The internal trade requirement is determined by the extent of the elimination of duties and ORRC between the RTA parties. Hypothetically, an RTA may exist where the internal trade liberalization, without taking into account the additional trade liberalization induced by the RTA MFN clause, may be insufficient to meet the GATT Article XXIV:8 requirement. This can happen, for example, when a 'major sector' of traded goods is excluded from trade liberalization.[47] The major sector may be added to the trade liberalization later based on the RTA MFN clause after the formation of the RTA.

If the elimination of duties and ORRC on goods traded between the RTA parties has yet to occur, the agreement is still an 'interim agreement' necessary for the formation of an RTA.[48] An interim agreement should include a plan to complete its formation 'within a reasonable length of time' according to GATT Article XXIV:5(c).[49] However, since the intra-RTA trade liberalization based on the MFN clause is conditioned on the treatment of goods from a third party, the GATT Article XXIV:8 condition will not be met, because there can be no plan to complete the formation of an RTA 'within a reasonable length of time'.[50] Therefore, the MFN clause should not be considered part of the measures to fulfil

44 Paragraph 3 of the Understanding on the Interpretation of Article XXIV of the GATT 1994 (Understanding).

45 The US RTAs may all be viewed as *de facto* interim agreements before the expiration of the ten-years period but they are all notified as *de jure* full RTAs. See Lorand Bartels, '"Interim agreements" under Article XXIV GATT', **8** *World Trade Review* 339 (2009), at 339.

46 WTO Panel Report, *US – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea* (*US–Line Pipe*), WT/DS202/R, para. 7.141, n. 128, adopted as modified by the Appellate Body Report, WT/DS202/AB/R, on 8 March 2002. In the case, the panel viewed that the safeguard measure met the timing requirement because the safeguard provision was provided in the RTA.

47 See chapeau of the Understanding, above n. 44.

48 See chapeau of GATT Article XXIV:5.

49 Ibid.

50 See paragraph 3 of the Understanding, above n. 44.

the internal trade liberalization requirement under GATT Article XXIV:8. In addition to the above reason, the trade liberalization based on the RTA MFN clauses in the US FTAs and in ANZCERTA discussed before should not be considered part of GATT Article XXIV:8 trade liberalization, because they do not require 'elimination' of duties and ORRC. The RTA MFN clauses result in reduction, but not necessarily elimination, of the intra-RTA trade barriers.[51]

The MFN clauses in RTAs must also satisfy the external trade barrier requirement under GATT Article XXIV:5 that 'duties and other regulations of commerce' that are 'in respect of' trade with third parties or 'applicable' to the trade of third parties shall not be 'higher or more restrictive' after the formation of an RTA than before the formation of an RTA.[52] This is an 'economic test' of determining whether the trade barriers with third parties after the RTA have become more restrictive in comparison to those before the RTA.[53]

The MFN clauses in the previously discussed US RTAs on agricultural products and the MFN clause in ANZCERTA apply to goods from the RTA parties, not from third parties. The RTA MFN clauses are not 'duties or other regulations of commerce' that are 'in respect of' trade with third parties or 'applicable' to the trade of third parties. The ordinary meaning of the terms 'in respect of' and 'applicable' do not cover those measures that indirectly affect trade with third parties.[54] Therefore, the measures based on the RTA MFN clauses in the above RTAs do not infringe on the external trade barrier requirement under GATT Article XXIV:5 as they are not 'in respect of' trade with or 'applicable' to the trade of third parties.

Now, under the second prong of *Turkey–Textiles*, the RTA MFN clauses must satisfy the necessity test. The MFN clauses in the US RTAs illustrated before permit further trade liberalization in some limited scope of agricultural products when the MFN obligation is triggered. However, the preferential trade liberalization in the RTAs causes exclusionary effects on goods imported from third parties.[55] The exclusionary effects arise because imports from third parties are subject to higher trade barriers in comparison to imports from the RTA parties even if the RTA

51 See the US–Morocco FTA, above n. 19, para. 3 and Article 4 of ANZCERTA, above n. 28, paras. 9 and 10.

52 The term 'in respect of' is used for a customs union GATT Article XXIV:5 (a) and the term 'applicable' is used for a free-trade area under GATT Article XXIV:5(b).

53 WTO Panel Report, *Turkey – Restrictions on Imports of Textile and Clothing Products*, WT/DS34/R, adopted 19 November 1999, as modified by Appellate Body Report WT/DS34/AB/R, DSR 1999: VI, 2363, para. 9.121. Affirmed by the Appellate Body above n. 38, para. 55.

54 The external trade barrier requirement would cover internal marketplace regulations that affect both imports from the RTA parties and from third parties because the measures fall within the meaning of 'other regulations of commerce' that are 'in respect of' trade with or 'applicable' to the trade of third parties under GATT Article XXIV:5.

55 In an empirical study of Mercosur, the export prices of products from non-member countries of Mercosur were lower after the formation of Mercosur than before, providing evidence that non-parties of Mercosur are hurt even if the external tariffs of the PTA are unchanged. See Chan and Winters, above n. 2, at 901.

parties do not change external tariffs applicable to third parties.[56] Similar exclusionary effects are caused by the intra-RTA trade liberalization required by GATT Article XXIV:8, but they are necessary for the formation of an RTA. In contrast, the exclusionary effects caused by the MFN clauses in the RTAs discussed above cannot be considered an inherent consequence of forming the RTAs, because the measures based on the RTA MFN clauses are not part of the elimination of the intra-RTA trade barriers under GATT Article XXIV:8.

Instead of providing the RTA MFN clauses, which increase the burden on the trade with third parties, reasonable alternatives are available to the RTA parties. One reasonable alternative is for the RTA parties to incorporate the trade liberalization anticipated by the RTA MFN clauses as part of the unconditional elimination of duties and ORRC between the RTA parties under GATT Article XXIV:8.[57] Another reasonable alternative is to provide an MFN-consultation clause that will be effective from the beginning of an interim agreement until the formation of an RTA. The trade liberalization resulting from the MFN-consultation clause must be implemented before the RTA completes its formation. The MFN-consultation clause leaves open the possibility of negotiating for additional market access during the formation of an RTA if imports from third parties are accorded with more favourable treatment by the RTA partner. It provides the opportunity for the RTA parties during the formation of an RTA to renegotiate the remaining above-zero tariff lines and other market access barriers instead of agreeing to an MFN clause without a time limit. The alternative measures would remove the contingent nature of the trade liberalization induced by the RTA MFN clauses. Since reasonable alternatives to the RTA MFN clauses are available, the RTA MFN clauses fail the necessity test under *Turkey–Textiles*. In sum, the RTA MFN clauses fail the requirements of GATT Article XXIV defence because they are not considered necessary for the formation of the RTAs.

An MFN-consultation clause in an RTA does not in itself raise questions about its legal consistency with the WTO law, because the RTA parties are not bound to adopt market access measures based the MFN-consultation clause. However, a WTO consistency issue may arise if the parties enter into an agreement to accord additional market access based on an MFN-consultation clause after the RTA has completed its formation or ten years after the adoption of an 'interim agreement'.[58] If agreements to accord additional market access are enacted after the formation of the RTA, they should be considered new agreements that are distinct from the original RTA with the MFN-consultation clause.

56 The study shows that exporters outside Mercosur had to reduce their export prices under competitive pressure created by the preferential tariffs liberalization between the parties of Mercosur.

57 See Appellate Body Report, *Turkey–Textiles*, above n. 38, para. 62.

58 See Paragraph 3 of the Understanding, above n. 44.

3.2.2 *MFN clauses in EIAs under GATS Article V*

The general MFN clause under GATS Article II for trade in services under the WTO is a less onerous obligation than GATT Article I because GATS Article II permits exceptions more liberally than GATT Article I.[59] An exception from GATS Article II is permitted 'provided that such a measure is listed in, and meets the conditions of, the Annex on the Article II Exemptions'.[60] For those services included in the Annex on Article II Exemptions, WTO members are not obligated to accord the MFN treatment under GATS Article II. In addition to the built-in MFN exemptions, GATS Article V permits exceptions from GATS Article II when WTO members form EIAs.[61]

The development of EIA MFN clauses can be attributed to the liberal exceptions permitted under GATS Article II. In view of the possibility of discriminatory treatment in services trade permitted under the GATS, a WTO member is guaranteed that its services and service providers will be accorded treatment no less favourable from its EIA partner country than treatment accorded to those from third countries through the MFN clauses provided in its EIAs.

MFN clauses in EIAs vary widely in their coverage of situations that trigger MFN obligations.[62] In particular, variations in EIA MFN clauses are observed with respect to the scope of exemptions from the coverage of EIA MFN clauses. Some EIA MFN clauses exclude from their scope those measures that are exempted from GATS Article II.[63] Other EIA MFN clauses provide separate MFN exemption lists, which exclude the listed sectors from the coverage of the EIA MFN clauses. In addition, certain measures, such as subsidies granted by the parties are entirely excluded from the scope of the EIA.[64]

In the following, we review MFN clauses in EIAs concluded by the US, the European Union (EU), the EFTA, and the Association of Southeast Asian Nations (ASEAN). At one end of the spectrum, the US EIAs provide MFN clauses with little limitation on their scope. At the other end of the spectrum, some ASEAN EIAs do

59 See MD. Rizwanul Islam and Shawkat Alam, 'Preferential Trade Agreements and the Scope of GATT Article XXIV, GATS Article V and The Enabling Clause: An Appraisal of GATT/WTO jurisprudence', **56** *Netherland International Law Review* 1 (2009), at 24.

60 GATS Article II:2. Paragraph 6 of the Annex on Article II Exemptions of the GATS provides that '[i]n principle, such exemptions should not exceed a period of 10 years'.

61 WTO members who failed to include service sectors in the Annex on Article II Exemptions of the GATS at the end of the Uruguay Round might have been tempted to use EIAs as covers for GATS Article II violations. See Rudolf Adlung and Antonia Carzaniga, 'MFN Exemptions under the General Agreement on Trade in Services: Grandfathers Striving for Immortality?', **12**(2) *Journal of International Economic Law* 357 (2009), at 379.

62 See Table 1 below for an overview of the scope of EIA MFN clauses.

63 Ibid.

64 See KORUS FTA, below n. 67, para. 4(d); Article 2.5 of the EU–Mexico FTA, below n. 71; Article 4 (b) of the ASEAN–Australia New Zealand FTA, below n. 107; Article 14 of the ASEAN–China FTA, below n. 106.

Table 1. Scope of EIA MFN clauses

		Measures under GATS Article II Exemptions	Measures under GATS Article V	Measures under GATS Article VII	Availability of Separate MFN Exemptions List
US EIAs	NAFTA	Applicable	Applicable	Applicable	Not Available
	KORUS	Applicable	Applicable	Applicable	Not Available
EU EIAs	EU–Mexico	Applicable	Excluded	Excluded	Not Available
	EU–Korea	Excluded	Applicable*	Excluded	Available
EFTA EIAs	EFTA–Mexico	Applicable	Excluded	Excluded	Not Available
	EFTA –Singapore	Excluded		Excluded	Not Available
	EFTA–Colombia; EFTA–Korea; EFTA–Ukraine	Applicable	Excluded†	Excluded	Available
	EFTA–Chile	GATS Article II governs the MFN obligations between the parties.			
ASEAN EIAs	ASEAN–China; ASEAN–Korea	No EIA MFN clauses.			
	ASEAN–Australia–New Zealand	Provides opportunity for consultation for MFN treatment.			

Notes: *Applicable to measures under future EIAs only. The measures under the EEA and the measures based on the ratchet clauses in EIAs with third parties are not covered.

† Measures under GATS Article V *bis* are also excluded from the EIA MFN clauses.

not provide MFN clauses in order to protect the differential treatment agreed to in the EIAs untouched by other services market concessions.

(1) Overview of MFN clauses in EIAs.

(a) MFN clauses in US EIAs

MFN clauses are provided in the trade in services chapters of US FTAs concluded with its trading partners.[65] For example, North American Free Trade Agreement (NAFTA) provides an MFN clause in its trade in services chapter, which states that '[e]ach Party shall accord to service providers of another Party treatment no less favourable than that it accords, in like circumstances, to service providers of any other Party or of a non-Party'.[66] Similarly, the MFN clause in the cross-border trade in services chapter of the Free Trade Agreement between the US and the Republic of Korea (KORUS FTA) provides that '[e]ach Party shall accord to service suppliers of the other Party treatment no less favourable than that it accords, in like circumstances, to service suppliers of a non-Party'.[67] The EIA MFN provision in NAFTA is distinct from those in other US EIAs, because it also requires that a NAFTA party shall not discriminate between the service providers of other NAFTA parties.[68]

The MFN clauses in NAFTA and in the KORUS FTA do not exclude from their scope the discriminatory measures permitted under the Annex on Article II Exemptions of the GATS.[69] For example, the US included in its list of the Annex on Article II Exemptions an entry regarding more favourable market access to Canadian small businesses for 'simplified registration and periodic reporting forms with respect to their securities'.[70] Under the EIA MFN clauses in NAFTA and in the KORUS FTA, the US is obliged to provide the same market accesses to small

65 MFN clauses are found in services chapters of all enacted US 'free trade agreements' except for the US–Jordan FTA and the US–Israel FTA. The US–Israel FTA does not include a chapter on trade in services. The US–Jordan FTA includes provisions on trade in services under Article 3; however, it does not provide for an MFN clause.

66 Article 1203 of the North American Free Trade Agreement (NAFTA), entered into force 1 January 1994, available at http://www.nafta-sec-alena.org/en/view.aspx?x=343, visited (18 March 2013).

67 See Article 12.3 of the Free Trade Agreement between the US and the Republic of Korea (KORUS FTA), entered into force 15 March 2012, available at http://www.ustr.gov/trade-agreements/free-trade-agreements/korus-fta/final-text (visited 18 March 2013).

68 The WTO panel in *Canada–Autos* ruled that it would be inconsistent with GATS Article V if the parties of an EIA accord less favourable treatment to service provider of one party than those from another party of the same EIA. See WTO Panel Report, *Canada – Certain Measures Affecting the Automotive Industry* (*Canada–Autos*), WT/DS139/R, WT/DS142/R, adopted 19 June 2000, as modified by Appellate Body Report WT/DS139/AB/R, WT/DS142/AB/R, para. 10.270.

69 See Article 1203 of NAFTA and Article 12.3 of the KORUS FTA, above n. 66 and n. 67, respectively. Also, both EIA MFN clauses in NAFTA and the KORUS FTA do not adopt separate MFN exemptions lists for EIAs.

70 WTO Document, The US, Final List of Article II (MFN) Exemptions, General Agreement on Trade in Service, GATS/EL/90, 15 April 1994.

businesses from Mexico and Korea with respect to simplified registration and periodic reporting forms for its securities.

In addition, the MFN clauses in NAFTA and in the KORUS FTA are applicable to discriminatory measures adopted by the EIA parties when they form new EIAs with non-parties pursuant to GATS Article V. As a result of the inclusion of GATS Article V measures within the scope of the EIA MFN clauses, the MFN clauses are likely to 'entrench' the preferential trade liberalization in the EIAs because the parties in new EIAs will be less likely to offer each other market accesses in services greater than those accomplished in the existing EIAs with MFN clauses.

(b) MFN clauses in EU EIAs

The EU–Mexico FTA. The EU entered into EIAs that provided MFN clauses. The scope of MFN clauses in EU's EIAs varied significantly across the EIAs. The EIA MFN clause in the EU–Mexico FTA provides that the parties' treatment accorded to 'services suppliers of the other Party shall be no less favourable than that accorded to like services suppliers of any third country'.[71] The EIA MFN clause does not exclude from its scope those measures taken pursuant to the entries in the list of the Annex on Article II Exemptions of the GATS. Therefore, a more favourable treatment of services from third countries based on the Annex on Article II Exemptions will give rise to the EIA MFN obligations in the EU–Mexico FTA.

Two exceptions from the EIA MFN clause should be noted. First, the MFN clause will not cover differential treatment deriving from the harmonization of regulations for mutual recognition based on an agreement concluded by either Mexico or the EU with a third country in accordance with Article VII of the GATS.[72] Second, the MFN clause will not apply to more favourable treatment granted to a third country based on another EIA concluded between the EU or Mexico with a third country pursuant to GATS Article V.[73]

To examine situations in which the EIA MFN obligations may arise under the EU–Mexico FTA, each EIA party's GATS Article II Exemptions list must be examined. Mexico has listed only two measures in its Annex on Article II Exemptions list: first, a measure permitting the supply of road transport service by

71 Article 5.1 of the EU–Mexico FTA provides the MFN clause for trade in services other than maritime and financial services. For financial services, a separate MFN clause is provided in Article 15.1 of the EU–Mexico FTA. See The Decision no. 2/2001 of the EU–Mexico Joint Council of 27 February 2001 implementing Articles 6, 9, 12(2)(b) and 50 of the Economic Partnership, Political Coordination and Cooperation Agreement (EU–Mexico FTA), WTO document, Free Trade Agreement between the European Communities and Mexico, Services, WT/REG109/4, 31 March 2003, entered into force 1 October 2000, available at http://rtais.wto.org/UI/PublicShowRTAIDCard.aspx?rtaid=73 (visited 22 February 2013).

72 Ibid. No parallel clause is provided for trade in financial services.

73 Ibid., Article 5.2 of the EU–Mexico FTA. Article 5.3 of the EU–Mexico FTA provides that if a party enters into an RTA in services with a third country, it shall give adequate opportunity to the other party to negotiate the benefits granted to a third country.

US suppliers into and across the territory of the US; second, a measure based on a bilateral agreement between the US and Mexico, which grants tax deductions to individuals attending business conventions in the other party's territory.[74] Under the MFN clause of the EU–Mexico FTA, if Mexico provides preferential treatment to the service providers from the US as permitted under the Annex on Article II Exemptions of the GATS, Mexico will be obliged to provide no less favourable treatment to the service providers from the EU. Specifically, Mexico must permit service providers from the EU to operate the road transport service in Mexico. In addition, Mexico must grant tax deductions to Mexican citizens attending business conventions in the EU.

In contrast to the entries in Mexico's GATS Article II exemptions, the EU had significantly greater number of 28 entries in its schedule of GATS Article II MFN exemptions.[75] A significant number of these measures reflect preferential treatment based on historical, geographical, or cultural proximity.[76] For example, for citizens of British Commonwealth members, if a grandparent of the citizen is born in the United Kingdom (UK), the UK will waive the requirement for a work permit in all service sectors.[77]

Some of the EC's other Article II MFN exemptions are applicable to all WTO members but are subject to a condition of reciprocity. For example, market access in France for press agency services is granted to all WTO members on a condition of reciprocity.[78] Therefore, in accordance with the EIA MFN clause, the EC will be required to provide market access for press agency services in France to Mexican press agency service providers if Mexico reciprocally provides the same market access to French press agency service providers.[79]

The EU–Korea FTA. The EIA MFN clause in the EU–Korea FTA is significantly different from the MFN clause in the EU–Mexico FTA in its scope of measures covered under the MFN clause.[80] The most significant difference is that the MFN

74 See GATS/EL/56, 15 April 1994, available at http://docsonline.wto.org/?language=1 (visited 22 February 2013).

75 The number of entries is based on the GATS commitments by the European Communities (EC) and its 12 member states. See European Communities and Their Member States, Final List of Article II (MFN) Exemption, GATTGATS/EL/31, 15 April 1994, available at http://docsonline.wto.org/?language=1 (visited 22 February 2013).

76 See Adlung and Carzaniga, above n. 61, at 369.

77 Ibid. See the EC's Final List of Article II (MFN) Exemptions.

78 Ibid.

79 Note that the EU–Mexico FTA entered into force on 1 October 2000; however, the adoption of the list of commitments establishing the level of liberalization in trade in services has been postponed until the conclusion of a new multilateral round (Doha Round) of services trade liberalization in accordance with the footnote to Article 7.3 of the agreement.

80 See the Free Trade Agreement between the European Union and its Member States, of the one part, and the Republic of Korea, of the other part (EU–Korea FTA), entered into force 1 July 2011, available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:127:0006:1343:EN:PDF (visited 13 February 2013).

clause in the EU–Korea FTA covers those future measures adopted by one of the parties with third parties under other EIAs[81] 'signed after the entry into force' of the EU–Korea FTA.[82] The MFN clause does not apply to those measures listed in the GATS Annex on Article II Exemptions. The MFN clause in the EU–Korea FTA also raises the issue of the entrenchment of preferential trade liberalization through the EIA, as it includes those measures adopted in the context of the formation of other EIAs within the scope of the EIA MFN clause. The automatic extension of the preferential trade liberalization to the EU and Korea through the EIA MFN clause will reduce 'the value of preferences, and thereby the willingness of countries to strike reciprocal bargains' in new EIAs.[83]

However, even if a measure is based on an EIA, the MFN clause excludes from its coverage the preferential treatment of third parties if the treatment is granted under EIAs that stipulate 'a significantly higher level' of obligations in service liberalization.[84] A significantly higher level of obligations is defined as the creation of an 'internal market on services and establishment'[85] or 'both the right of establishment and the approximation of legislation' as defined in Annex 7-B of the EU–Korea FTA. Annex 7-B of the EIA states in its footnote that, at the time of the conclusion of the agreement, the European Economic Area (EEA) was the only example of an internal market with third countries of the EU on services and establishment meeting the definition provided in the annex.[86] Thus, the services liberalization under the EEA does not give rise to the EU's MFN obligation to services and services suppliers from Korea.

In addition, the MFN clause of the EIA explicitly removes from its scope those measures for mutual recognition that are 'in accordance with Article VII of GATS or its Annex on Financial Service' and measures 'under any international agreements or arrangements relating wholly or mainly to taxation'.[87] In addition to the above exclusions, the EIA adopts its own list of MFN exemptions.

81 The EU–Korea FTA defines an economic integration agreement as an agreement liberalizing trade in services pursuant to GATS Article V and GATS V *bis* of the GATS. Ibid., Article 7.2 of the EU–Korea FTA, para. 1. In this section, we use the same acronym EIA for this definition of an economic integration agreement.

82 Interestingly, the measures under the KORUS FTA do not fall within the scope of the MFN clause because KORUS FTA was signed 30 June 2007 and the separate agreement (Exchange of Letters) was signed on 10 February 2011, prior to the enactment of the EU–Korea FTA. See for the dates of signature of the KORUS FTA, WTO Document, WT/REG311/N/1, 16 March 2012.

83 Fink and Jansen, see above n. 3, at 247.

84 See Article 7.8 of the EU–Korea FTA, above n. 80, para. 2.

85 See note 1 of Annex 7-b of the EU–Korea FTA, above n. 80.

86 Ibid.

87 See Article 7.8 of the EU–Korea FTA, above n. 80, para. 3. The differential treatment with regard to taxation under international agreements to avoid double taxation is likely to fall under GATS Article XIV, the general exception clause.

The measures covered by the entries in the MFN exemption list in Annex 7-C of the EU–Korea FTA are excluded from the EIA MFN clause.[88]

Adding more complexity to the Annex 7-C exemption lists, the exemption lists for the EU and Korea list measures applicable to all sectors that provide differential treatment based on the ratchet clauses provided in the EIAs to which the EU or Korea is a party. A ratchet clause permits the party to an EIA to 'amend any measure only to the extent that the amendment does not decrease the conformity of the measure, as it existed immediately before the amendment, with obligations on market access, national treatment and most-favoured nation in these economic integration agreements'.[89] The aim of this exemption from the EIA MFN clause is to 'to protect differential treatment deriving from ratchet clauses'.[90]

(c) MFN Clauses in EFTA EIAs

The MFN clause in the EFTA–Mexico FTA excludes from its scope any preferential treatment granted under EIAs pursuant to Article V of the GATS.[91] In addition, the MFN obligation will not arise if the preferential treatments to third parties derive from harmonisation of regulations based on mutual recognition agreement in accordance with Article VII of the GATS.[92] However, the MFN clause in the EFTA–Mexico FTA does not exclude from its scope those measures taken pursuant to the entries in the list of the Annex on Article II Exemptions of the GATS.[93] In addition, the EIA does not adopt its own list of measures that are excluded from the EIA MFN clause. In addition to the MFN clause, the EFTA–Mexico FTA includes an MFN-consultation clause.[94]

Similarly, the MFN clause in the EFTA–Singapore FTA, excludes from its scope any preferential treatment granted through EIAs under Article V and Article V *bis* of the GATS.[95] As with the EFTA–Mexico FTA, the EFTA–Singapore FTA excludes those measures based on a mutual recognition agreement under Article

88 Ibid.

89 See Annex 7-C of the EU–Korea FTA, above n. 80.

90 Ibid., the list for EU Party, Annex 7-C of the EU–Korea FTA, above n. 80.

91 The parties agreed to review the exclusion clause with a view to its deletion within three years after the enactment of the EIA. See Article 22 of the Free Trade Agreement between the EFTA States and the United Mexican States (EFTA–Mexico FTA), para. 2, entered into force 1 July 2001, available at http://www.efta.int/~/media/Documents/legal-texts/free-trade-relations/mexico/EFTA-Mexico%20Free%20Trade%20Agreement.pdf (visited 29 January 2013).

92 Ibid., Article 22 of the EFTA–Mexico FTA, para. 1.

93 Ibid.

94 Ibid., para. 3.

95 See Article 23 and Annex VI of the Agreement between the EFTA States and Singapore (EFTA–Singapore FTA), para. 2, entered into force 1 January 2003, available at http://www.efta.int/~/media/Documents/legal-texts/free-trade-relations/singapore/EFTA-Singapore%20Free%20Trade%20Agreement.pdf (visited 29 January 2013). GATS Article V *bis* provides exception from the GATS for labour market integration agreements.

VII of the GATS from the scope of the EIA MFN clause.[96] In addition to the MFN clause, the EFTA–Singapore FTA includes an MFN-consultation clause.[97]

In contrast to the EFTA–Mexico FTA, the EFTA–Singapore FTA even excludes those measures listed in the Annex on Article II Exemptions of the GATS.[98] Moreover, the EIA does not separately adopt its own list of measures that are excluded from the EIA MFN clause. Because of these exclusions, the MFN obligation in the EFTA–Singapore FTA is likely to arise in narrow circumstances in which the preferential treatment of a third party by the EIA party is in violation of GATS Article II without being exempted under the Annex on Article II Exemptions, GATS Article V, or GATS Article VII.

Among the remaining EIAs concluded by the EFTA, the EFTA–Korea FTA,[99] the EFTA–Colombia FTA,[100] and the EFTA–Ukraine FTA[101] adopt the same template. The EIA MFN clauses exclude those measures based on GATS Article V or Article V *bis* and those measures taken for mutual recognition under GATS Article VII.[102] However, the measures taken pursuant to the Annex on Article II Exemptions of the GATS are not excluded from the scope of the MFN clauses. Instead, the EIAs permit their own lists of MFN exemptions.[103]

Among the MFN clauses in the EIAs into which the EFTA entered into, the MFN clause in the EFTA–Chile FTA is distinct, as GATS Article II is incorporated in the EIA as the EIA MFN clause. The EIA provides that '[t]he rights and obligations of the Parties with respect to the most-favoured nation treatment shall be governed by the GATS'.[104] The interpretation of the provision is unclear, however, because an EIA by definition derogates from GATS Article II as a result of its formation. A GATS Article II obligation is a multilateral obligation, which cannot apply only

96 Ibid., para. 1.

97 Ibid., para. 3.

98 Ibid.

99 See Article 3.4 of the Free Trade Agreement between the EFTA States and the Republic of Korea (EFTA–Korea FTA), paras. 1 and 2, entered into force 1 September 2006, available at http://www.efta.int/~/media/Documents/legal-texts/free-trade-relations/republic-of-korea/EFTA-%20Republic%20of%20Korea%20Free%20Trade%20Agreement.pdf (visited 29 January 2013).

100 See Article 4.3 of the Free Trade Agreement between the Republic of Colombia and the EFTA States (EFTA–Colombia FTA), para. 2, entered into force 1 July 2011, available at http://www.efta.int/~/media/Documents/legal-texts/free-trade-relations/columbia/EFTA-Colombia%20Free%20Trade%20Agreement%20EN.pdf (visited 29 January 2013).

101 The Free Trade Agreement between the EFTA States and Ukraine (EFTA–Ukraine FTA), entered into force 1 June 2012, available at http://efta.int/~/media/Documents/legal-texts/free-trade-relations/ukraine/EFTA-Ukraine%20Free%20Trade%20Agreement.pdf (visited 29 January 2013).

102 See Article 3.4 of EFTA–Korea FTA, above n. 99, paras. 1 and 2; Article 4.3 of the EFTA–Colombia FTA, above n. 100, para. 2; Article 3.4 of the EFTA–Ukraine FTA, above n. 101, para. 1.

103 See the EFTA–Korea FTA, above n. 99, para. 1 and Annex VIII; Article 4.3 of the EFTA–Colombia FTA, above n. 100, para. 1; Article 3.4 of the EFTA–Ukraine FTA, above n. 101, para. 1.

104 See Article 24 of the Free Trade Agreement between the EFTA States and the Republic of Chile (EFTA–Chile FTA), para. 1, entered into force 1 December 2004, available at http://www.efta.int/~/media/Documents/legal-texts/free-trade-relations/chile/EFTA-Chile%20Free%20Trade%20Agreement.pdf (visited 29 January 2013).

between the EFTA countries and Chile. Therefore, it is not clear what MFN obligation arises between the EIA parties. In addition to the MFN clause, the EIA also adds an MFN-consultation clause.[105]

(d) MFN Clauses in ASEAN EIAs

The ASEAN entered into three EIAs in trade in services: the ASEAN–China FTA[106], the ASEAN–Australia–New Zealand FTA[107], and the ASEAN–Korea FTA.[108] None of the three EIAs provides an EIA MFN clause. Instead, among the EIAs, the ASEAN–Australia–New Zealand FTA provides a distinctive MFN-consultation clause. Article 7 of the EIA provides for consultations 'to discuss the possibility of extending' MFN treatment if a party enters into an agreement that provides more favourable treatment to services and service suppliers of a non-party.[109] There are two exceptions in the MFN-consultation clause. The obligation to consult does not arise if the agreement with a non-party includes an ASEAN member country or ASEAN member countries.[110] In addition, the MFN consultation obligation does not arise when the more favourable treatment to a third country is based on an agreement that went into force before the enactment of the ASEAN–Australia–New Zealand FTA.[111]

An important observation has been made that some EIAs provide services trade liberalization commitments that result in 'negative preferences' in comparison to the parties' commitments under the GATS.[112] 'Negative (GATS-minus) preferences' mean market access or national treatment disciplines less liberal than those concessions under the GATS or sectoral scope narrower than that provided for in a party's GATS schedule.[113] For example, under the ASEAN–China FTA, where the national treatment disciplines and sectoral scopes committed by China and some

105 Ibid., para. 2.

106 Agreement on Trade in Services of the Framework Agreement on Comprehensive Economic Co-operation between the Association of Southeast Asian Nations and the People's Republic of China (ASEAN–China FTA), entered into force 1 July 2007, available at http://www.asean.org/news/item/twelfth-asean-summit-cebu-philippines-9-15-january-2007 (visited 28 January 2013).

107 The Agreement Establishing the ASEAN – Australia – New Zealand Free Trade Area (ASEAN–Australia–New Zealand FTA), entered into force 1 January 2010, available at http://www.asean.fta.govt.nz/assets/Agreement-Establishing-the-ASEAN-Australia-New-Zealand-Free-Trade-Area.pdf (visited 28 January 2013).

108 The Agreement on Trade in Services under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the Association of Southeast Asian Nations (ASEAN–Korea FTA), entered into force 1 May 2009, available at http://www.fta.go.kr/pds/fta_korea/asean/20100413_asean.pdf (visited 28 January 2013).

109 Ibid., Article 7 of the ASEAN–Korea FTA, 1.

110 Ibid., para. 2.

111 Ibid., para. 4.

112 See Rudolf Adlung and Peter Morrison, 'Less than the GATS: "Negative Preferences" in Regional Services Agreements', **13** *Journal of International Economic Law* **1103** (2010), at 1125–35.

113 Ibid.

ASEAN members are less than the parties' GATS commitments.[114] In the presence of the negative preferences, if an EIA MFN clause were provided in the service chapter of the ASEAN–China FTA, then it would erase the negative preferences by restoring the GATS market access commitments.[115] Though the EIA MFN clauses may neutralize the 'negative preferences', the question still remains whether the EIA MFN clause is legal under WTO law.

The negative preferences as provided in the ASEAN–China FTA between the EIA parties are inconsistent with the ASEAN countries' GATS schedules.[116] Since they roll back the trade liberalization between the EIA parties, the intra-EIA trade liberalization requirement under GATS Article V:1 is not likely to be met. They also detract from the aim of an EIA 'to facilitate trade between the parties to the EIA' under GATS Article V:4. Therefore, the inconsistency of the negative preferences in the ASEAN–China FTA with the GATS schedule of commitments is likely to fail the legal defence under GATS Article V.

The negative preferences raise the possibility of conflict between the ASEAN–China FTA and the GATS.[117] While lawful under the China–ASEAN FTA, the negative preferences will be inconsistent under the GATS because of the failure to meet the GATS Article V defence. The conflict is not clearly resolved because the ASEAN–China FTA does not explicitly state that it is in pursuant to GATS Article V.[118] Nevertheless, since the parties to the China–ASEAN FTA later notified the agreement to the WTO as an EIA pursuant to GATS Article V:7(a), the GATS rights and obligations should take precedence over the GATS-minus provisions in the China–ASEAN FTA.[119]

(2) Legality of MFN clauses in EIAs

EIA MFN clauses result in GATS Article II (Most-Favoured Nation Treatment) violations. The measures taken by the EIA parties accord more favourable treatment to services and service providers from the EIA parties to whom the MFN obligation is owed than to those from third countries with whom the EIA parties have not entered into EIAs with MFN clauses. The measures will be

114 Ibid., at 1135.

115 The ASEAN–China FTA possibly did not provide for EIA MFN clauses, because they would erase the 'negative preferences'.

116 See Adlung and Morrison, above n. 112, at 1125–35.

117 For the definition of conflicts of treaties, see Gabrielle Marceau, 'Conflicts of Norms and Conflicts of Jurisdiction, The Relationship between the WTO Agreement and MEAs and other Treaties', 35(6) *Journal of World Trade* 1081 (2001), at 1084.

118 See the China–ASEAN FTA, above n. 106. This contrasts with Article 1(a) of the EU–Mexico FTA, which states that the objective of the agreement is 'the progressive and reciprocal liberalisation of trade in services, in conformity with Article V of GATS.' See the EU–Mexico FTA, above n. 71.

119 See Notification of Regional Trade Agreement, WTO Document, S/C/N/463, 2 July 2008.

inconsistent with the GATS unless they fulfil the requirements for legal defence under GATS Article V.[120]

The requirement of GATS Article V will be interpreted in light of the purpose of an EIA as set forth in GATS Article V.[121] The purpose of an EIA is 'to facilitate trade between the parties to the agreement and shall not in respect of any Member outside the agreement raise the overall level of barriers to trade in services within the respective sectors or subsectors compared to the level applicable prior to such an agreement'.[122] The first part of this purpose – the internal trade requirement – provides that the PTA parties should facilitate the internal trade between the PTA parties through the PTA. The second part of the purpose – the external trade barrier requirement – provides that PTA parties should not raise the 'overall level of barriers' to trade in services with third parties through the PTA. In view of the fact that the purpose of an EIA as provided in GATS Article V:4 is largely identical to that of an RTA under GATT Article XXIV:4, the two-pronged test under *Turkey–Textiles*, which decided a challenged measure under GATT Article XXIV, should also inform our interpretation of GATS Article V to test the legality of the EIA MFN clauses.

The first prong of *Turkey–Textiles* under GATS Article V, which is analogous to that under GATT Article XXIV, provides the timing and legality elements. However, the timing element under GATS Article V for EIAs diverges from that of GATT Article XXIV for RTAs. The timing element for an RTA under GATT Article XXIV provides that GATT violating measures should be introduced upon the formation or adoption of an interim agreement for the formation of an RTA.[123] In contrast to GATT Article XXIV, GATS Article V does not explicitly provide for a *de jure* 'interim agreement' leading to a formation of an EIA. Nevertheless, paragraph 1 of GATS Article V leaves open the possibility of a *de facto* interim agreement, stating that '[t]his Agreement shall not prevent any of its Members from *being a party to or entering into* an agreement liberalizing trade in services between or among the parties to such an agreement' (emphasis added).[124] Therefore, the intra-EIA trade liberalization under GATS V:1 should be implemented 'either at the entry into force of that agreement or on the basis of a

120 We excluded from our legality analysis MFN-consultation clauses and the MFN clause in the EFTA–Chile FTA because they do not operate as MFN clauses.

121 Paragraph 1 of Article 31 of the Vienna Convention on the Law of Treaties (VCLT) provides that '[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose'. See VCLT, done at Vienna on 23 May 1969, entered into force on 27 January 1980, United Nations, Treaty Series, vol. 1155, at 331. We inferred the object and purpose of GATT Article XXIV and GATS Article V from the stated purposes of RTAs under GATT Article XXIV:4 and EIAs under GATS Article V:4.

122 GATS Article V:4.

123 See Appellate Body Report, *Turkey–Textiles*, above n. 38, at para. 58.

124 See Bartels, above n. 45, at 339.

reasonable time-frame'.[125] The MFN Clauses should be provided in the EIAs at the time of their enactment or provided on the basis of a 'reasonable time-frame'. As long as this requirement is met, the MFN measures that are applied later should be deemed to be in conformity with the timing requirement.[126]

In addition to the timing requirement, the legality element also can be uncovered from the provisions of GATS Article V. The legality element test whether the EIAs meet (1) the internal trade requirement under GATS Article V:1, and 2) the external trade barrier requirement under GATS Article V:4. The test focuses on the EIAs, not the EIA MFN clauses. The internal trade requirement under GATS Article V:1 has two operational elements: 'substantial sectoral coverage' under GATS V:1(a), and 'absence or elimination of substantially all discrimination in the sense of Article XVII' under GATS V:1(b).[127] The first element, 'substantial sectoral coverage', is understood to mean that the 'number of sectors, volume of trade affected and modes of supply' should all be considered, and there should be no '*a priori* exclusion of any mode of supply' according to the footnote to Article V.[128] The second element, 'absence or elimination of substantially all discrimination in the sense of Article XVII', requires the EIA parties to accord national treatment to services and service suppliers of the other party.[129] The criterion is analogous to GATT Article XXIV:8, which requires RTA parties to eliminate duties and ORRC with respect to 'substantially all the trade' in products originating between the RTA parties. Both GATT Article XXIV and GATS Article V obligate the PTA parties to eliminate 'substantially all' intra-PTA trade barriers, albeit with 'some flexibility' in meeting the requirements.[130]

In reviewing whether the EIAs conform to the first element of the internal trade requirement, the question is whether the trade liberalization due to the EIA MFN clauses should be accounted for in assessing the 'substantial sectoral coverage' element under GATS V:1(a). The answer is that the trade liberalization based on an EIA MFN clause should not be deemed as part of the liberalization under GATS V:1(a), because it is contingent on a favourable treatment to a third party.

125 GATS Article V:1(b). It should be noted that the definition of 'a reasonable time-frame' under GATS Article V, in contrast to the term 'reasonable length of time' under GATT Article XXIV, has not been explicitly provided under the WTO Agreement.

126 See Panel Report, *US–Line Pipe*, above n. 46, para. 7.141, n. 128.

127 GATS Article V:1(a) and GATS Article V:1(b).

128 Footnote 1 of GATS Article V:1(a).

129 Note that GATS Article V:6 requires that the EIA parties should accord national treatment to a service supplier of any other WTO member if it is 'engaging in substantial business operations in the territories' of the EIA parties. The provision expands the scope of the 'nationality' of service suppliers that are qualified to receive preferential treatment. It is analogous to less-restrictive forms of preferential rules of origin in RTAs.

130 Appellate Body Report, *Turkey–Textiles*, above n. 38, para. 48. However, some scholars claim that GATS Article V appears to set a looser standard than GATT Article XXIV. See M. Matsushita, T. J. Schoenbaum, and P. C. Mavroidis, *The World Trade Organization: Law, Practice, and Policy* (Oxford: Oxford University Press, 2002), p. 364.

The trade liberalization may not be realized 'either at the entry into force of that agreement or on the basis of a reasonable time-frame'.[131] Therefore, the inclusion of additional services sectors for trade liberalization through an EIA MFN clause should not be taken into account in assessing whether the EIAs fulfils the 'substantial sectoral coverage' element under GATS V:1(a).

Similarly, under the second element of the internal trade requirement under GATS V:1(b), the question is whether the trade liberalization based on an EIA MFN clause can be characterized as trade liberalization in the sense of national treatment as required under GATS Article XVII. Two aspects of an EIA MFN clause lead to a negative conclusion. First, the trade liberalization that is based on an EIA MFN clause is contingent in nature; it takes place only when the EIA parties accord more favourable treatment to services and service suppliers from third parties. Second, the measures based on the MFN clause often may not amount to 'national treatment' within the meaning of GATS Article XVII, as is the case if the treatment to services and services suppliers of a third party is less trade-liberalizing than the national treatment under GATS Article XVII. This may well be the case if the preferential trade liberalization to a third party is based on the Annex on Article II Exemptions of the GATS instead of another EIA under GATS Article V with a third party. Since the trade liberalization based on an EIA MFN clause cannot be considered part of the trade liberalization to eliminate discrimination in the sense of GATS Article XVII (national treatment), the EIAs must meet the internal trade requirement irrespective of the intra-EIA trade liberalization resulting from the EIA MFN clause.

Next, under the external trade barrier requirement of the first-prong of *Turkey–Textiles*, the EIAs must not 'raise the overall level of barriers to trade in services' with respect to third parties as compared to the level applicable prior to the agreement. This is an economic test to examine the effect to third parties arising from the challenged measures that are adopted in the course of forming EIAs.[132] In contrast to GATT Article XXIV:5, the external trade barrier requirement under GATS Article V:4 is not provided as a separate operational criterion but is stated in combination with the other aim of an EIA, which is to 'facilitate trade between the parties to the agreement'.[133] The aim of facilitating the intra-EIA trade liberalization should be considered as the context for interpreting the external trade barrier requirement. In view of this context, the measures to enact intra-EIA trade liberalization required by GATS Article V:1 do not fail GATS Article V:4 requirements.

131 GATS Article V:1(b).

132 See Panel Report, *Turkey–Textiles*, above n. 53, para. 9.121.

133 GATS Article V does not provide the operational criteria that elaborate the external trade barrier requirement. Under GATS Article V, the challenged measure does not have to be 'in respect of' trade or 'applicable' to trade with third parties.

However, the trade liberalization based on an EIA MFN clause at issue is not required by GATS Article V:1. The trade liberalization based the EIA MFN clause provides durable advantages to the service providers from the EIA parties and excludes the service providers from third countries from the EIA party's market.[134] Since the EIA MFN clause 'raise the overall level of barriers to trade in services' with third countries compared to the level applicable prior to the formation of an EIA through the exclusionary effect, the EIA MFN clause infringe on the external trade barrier requirement. Therefore, the EIA with MFN clauses do not accord with GATS Article V:4 requirements.

Last, under the second prong of *Turkey–Textiles*, EIA MFN clauses should satisfy the 'necessity' requirement.[135] With respect to the necessity test, the Appellate Body's reasoning in *Turkey–Textiles* should again inform our interpretation of EIA MFN clauses, as the objectives of an RTA under GATT Article XXIV and an EIA under GATS Article V are identical.[136] According to *Turkey–Textiles*, if a reasonable alternative to the challenged measure exists, the challenged measure will not be deemed necessary for the formation of an EIA.[137] If this standard is applied here, reasonable alternatives to the challenged EIA MFN clauses can be found. Instead of providing an EIA MFN clause, the EIA parties can choose the reasonable alternative of incorporating the anticipated future trade liberalization to a third party as intra-EIA market access commitments. The reasonable alternative is no longer contingent upon the EIA parties' treatment of third parties. Therefore, it will be considered an inherent part of the market access commitments required by GATS Article V:1, thus conforming to the external trade barrier requirement under the first-prong of *Turkey–Textiles*. Another reasonable alternative is to provide an MFN-consultation clause that is effective only within 'a reasonable time-frame' after the enactment of the EIA and that results in trade liberalization during that time-frame.[138] In view of the availability of these reasonable alternatives, the EIA MFN clauses fail the *Turkey–Textiles* necessity test. In sum, the measures based on EIA MFN clauses cannot be exempted from the obligation under GATS Article II, because they fail to meet the requirements of legal defence under GATS Article V, in particular, the external trade barrier requirement and the necessity test as laid out in *Turkey–Textiles*.

134 See Aaditya Mattoo and Pierre Sauve, 'Regionalism in Services Trade', in Aaditya Mattoo, Robert M. Stern, and Gianni Zanini (eds.), *A Handbook of International Trade in Services* (New York: Oxford University Press, 2008), pp. 245–286, at 223.

135 Pauwelyn proposes an alternative criterion that the challenged measure should be 'part of' the RTA rather than being 'necessary' for the formation of the RTA. See Joost Pauwelyn, 'The Puzzle of WTO Safeguards and Regional Trade Agreement', 7 Journal of International Economic law (2004), at 141.

136 See Article 31:1 of the VCLT, above n. 121.

137 Appellate Body Report, *Turkey–Textiles*, above n. 38, para. 58.

138 GATS Article V:1(b).

4. Conclusion

The world trading system today forebodingly exhibits some resemblance to the trading system before the establishment of the GATT in 1948.[139] The MFN clauses in PTAs – similar to MFN clauses in bilateral FCN treaties during the pre-GATT years – illustrate the erosion of multilateralism under the WTO. The MFN clauses in PTAs fail to conform to WTO law, because they do not satisfy the requirements for legal defence under GATT Article XXIV or GATS Article V for their violations of the general MFN clauses under GATT Article I or GATS Article II. The measures based on the PTA MFN clauses increase the burden on the trade with third parties.[140] As a result, the PTA MFN clauses do not satisfy the necessity test under *Turkey–Textiles*, as reasonable alternatives to the PTA MFN clauses are available. One reasonable alternative is for the PTA parties to replace the PTA MFN clauses with unconditional market access commitments, which will substitute for the conditional market access that may result from the PTA MFN clauses. Another reasonable alternative is to replace the PTA MFN clauses with MFN-consultation clauses that would result in increased market access for the duration of the interim agreements for RTAs or within 'a reasonable time-frame' for EIAs.[141]

The MFN clauses in PTAs entrench the preferential trade liberalization between the PTA parties, as the trade liberalization in future PTAs with third parties is constrained by the extent of trade liberalization in the existing PTAs with MFN clauses.[142] Thus, PTA MFN clauses detract from the WTO's aim of expanding the trade in goods and services in the world through the elimination of discriminatory treatment in international trade relations.[143]

To bring PTAs into conformity with the world trading system, PTAs under the WTO should not include PTA MFN clauses. For those products or services subject to the existing PTA MFN clauses, any preferential liberalization based on the PTA MFN clauses should be accorded non-discriminatorily to all WTO members in accordance with the general MFN principles under GATT Article I and GATS Article II.

139 The erosion of the WTO's central role 'runs the risk that global trade governance drifts back towards a 19th century Great Powers world.' See Richard Baldwin, '21st century regionalism and global trade governance', Vox, 23 May 2011, available at http://www.voxeu.org/article/21st-century-regionalism-and-global-trade-governance (visited 3 July 2013).

140 In the case of the MFN clauses in EIAs, the external trade barrier requirement under GATS Article V is infringed.

141 GATT Article XXIV:5 (c) and GATS Article V:1(b).

142 In the case of EIAs, the entrenchment occurs in the EIAs with MFN clauses that do not exclude the measures under GATS Article V within the scope of the MFN clauses.

143 See the preamble of the WTO Agreement, above n. 4.