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Article XXIV of GATT and regional arrangements in South Africa

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(assisted by Leora Blumberg)

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Development Bank of Southern Africa

Development Paper 92

Discussion Paper

ISSN 1022-0127

ISBN 1-874878-90-0

August 1995

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Price R10

Mission of the Development Bank of Southern Africa

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Preface

The Development Bank of Southern Africa's macroeconomic policy work has stressed the importance of export growth to economic reconstruction and development in South Africa, and of regional integration in southern Africa as a key element of this strategy. As a result, DBSA's policy programme on international economic relations and cooperation has focused mainly on regional issues.

In August 1994, the South African government acceded to the treaty establishing the Southern African Development Community (SADC). An objective of the SADC is to set up a trade regime governing trade relations among its eleven member states. South Africa is also a long-standing member of the Southern African Customs Union (SACU) whose other members are Botswana, Lesotho, Namibia and Swaziland (the BLNS states). All five SACU members are also members of the SADC. South Africa is currently engaged in renegotiating the SACU with its customs union partners. It is also actively involved in designing a new trade regime for the SADC which will take into consideration both bilateral relations and obligations existing under the SACU agreement.

In recent months, the South African government has been under pressure to join the Common Market for Eastern and Southern Africa (COMESA) — formerly known as the Preferential Trade Area for Eastern and Southern Africa or PTA. The government has declined this invitation. However, several members of the SADC, including three of the BLNS countries, are members of COMESA. As a result of a decision taken in August 1994 at the SADC summit in Gaborone, those members of SADC (nine of the eleven members) who were members of COMESA agreed to end their membership in the latter institution. This political statement has yet to be put into action.

A new concept is the Indian Ocean Region initiative. The South African government has been invited to join six other countries, namely Australia, India, Kenya, Mauritius, Oman and Singapore, in setting up an economic cooperation arrangement for the Indian Ocean rim countries. From the South African Department of Foreign Affairs perspective, however, the main focus is on trade.

All these developments raise concern about the provisions of Article XXIV of the General Agreement on Tariffs and Trade (GATT), which permits the establishment of free-trade areas and customs unions even though these are ostensibly against the objectives and purposes of the GATT Agreement. Does Article XXIV permit a member state to belong to several trading regimes at the same time? To what problems would multifarious membership of this nature give rise? If preferences are given to a particular country under one trade regime and these are perceived to be more favourable than the preferences given to another country under a different trade regime, is this a breach of Article I of the GATT on most-favoured-nation treatment and would it therefore be a matter for consideration by the World Trade Organisation? How should member states relate to each other where they are parties to more than one customs union or free-trade area? Are such multifarious relationships permitted by the GATT?

The objective of this discussion document is to provide guidance to the South African government in respect of both its current membership in extant regional trading organisations and its prospective membership in institutions being created to improve trade relations among a different set of countries. The document will examine existing relationships between the countries in southern Africa against the backdrop of their GATT/World Trade Organisation obligations and the issue of multifarious membership.

Professor Umesh Kumar of the Faculty of Law at the University of Lesotho is the author of this discussion document. He was assisted by Leora Blumberg of Webber Wentzel Bowens, Attorneys at Law, Johannesburg. The study was undertaken under the leadership of the programme manager, RH Thomas, and with the advice of GJ Richter, MA Edington, L Kritzinger-Van Niekerk and N Vink of the programme's advisory panel.

It is hoped that this discussion document will be a constructive contribution to policy formulation on South Africa's relations with the southern African subcontinent.

GJ Richter
General Manager

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Programme Manager

Contents

1. Introduction

On 1 July 1994, the World Trade Organisation (WTO) came into being as the successor to the General Agreement on Tariffs and Trade (GATT), which had regulated international trade since 1947. When the WTO became operational early in 1995 it succeeded to the institutional arrangements created for the GATT.

Through the GATT maximum tariff rates (or 'bindings') were established for particular products in accordance with the schedules of concessions negotiated by the contracting parties under Article II of the Agreement. To further liberalise trade, the GATT sponsored a series of trade negotiating 'rounds'. Including the 1947 negotiations and original drafting of GATT, eight of these rounds have been held.

After seven years of negotiations in the Uruguay Round (1986-93) a Final Act was adopted, and was ratified at Marrakesh in April 1994. This agreement, referred to as GATT 1994, incorporates several understandings on the interpretation of the GATT 1947 provisions, as well as various agreements on agriculture, textiles and clothing; trade-related aspects of investment measures; anti-dumping, subsidies and countervailing duties; trade in services; the trade-related aspects of intellectual property rights; and an escape or safeguard clause. The WTO administers and implements GATT 1994.

The participants in the GATT were contracting parties to the General Agreement, and the GATT Articles of Agreement refer to 'contracting parties'. The former 'contracting parties' to the GATT are now 'members' of the WTO. Membership of the WTO is open to all signatories of the agreement, three-quarters of whom are developing countries. The Articles of Agreement are still known as the GATT Articles.

Article I of the GATT lays down the fundamental principle that members of the WTO must extend to all other members unconditionally any advantage, favour, privilege or immunity affecting customs duties, charges, rules and procedures that they give to products originating from or destined for any other country. This is described as the 'most-favoured-nation rule' and, on joining the WTO, members assume 'multilateral GATT obligations' in terms of the most-favoured-nation principle. This ensures that commitments made in the course of GATT negotiating rounds are applied uniformly by every member to every other member. In fact, the most-favoured-nation principle is the cornerstone of the WTO.

Article XXIV of the GATT deals with regional arrangements. It is perhaps *the* most important exception to the most-favoured-nation principle. It recognises that regional arrangements can 'increase the freedom of trade' through 'closer integration between the economies' of the members to a regional arrangement. But the framers also recognised that there was a danger of a region's raising barriers to the trade of other WTO members. These two concerns are reflected in the various paragraphs of Article XXIV.

GATT provisions on regional arrangements consist of (a) Article XXIV, (b) the 'Enabling Clause' that came out of the Tokyo Round of Agreements (1973-9) and (c) Article XXV. We shall discuss them one by one.

2. Types of regional arrangements

Three types of regional arrangements are envisaged by Article XXIV:

— a customs union
— a free-trade area
— an 'interim agreement' leading to the formation of either a customs union or a free-trade area.

Each of these three arrangements is defined in Article XXIV. If an arrangement meets the specified legal requirements, it automatically qualifies for an exception to the most-favoured-nation obligation. However, Article XXIV:5, which establishes the exception, only applies when all members of a regional arrangement are WTO members. If this is not the case, the arrangement is not eligible for automatic exception and will have to secure an approval under Article XXIV:10 by two-thirds of the WTO members.

(a) **Customs union**

A customs union is defined in Article XXIV:8(a). It must meet three legal requirements:

— 'Duties and other restrictive trade regulations' between customs union members must be eliminated on 'substantially all the trade' or 'at least substantially on all the trade in products originating' in the territories of the customs union members. However, this requirement is not absolute. Members are free, where necessary, to exercise their right to maintain trade restrictions under GATT Articles XI (quantitative restrictions), XII (restrictions to safeguard balance of payments), XIII (non-discriminatory administration of quantitative restrictions), XIV (exceptions to the rule of non-discrimination), XV (exchange arrangements) and XX (general exceptions to GATT obligations).

— Substantially the same duties and other trade regulations must be applied on trade with non-union members.

Duties and other restrictions on trade of non-union WTO members to and from such a customs union must 'not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce ... prior to the formation of such union'. This requirement, which is provided in Article XXIV:5(a), applies to all customs unions and to interim agreements leading to a customs union.

In addition, Article XXIV:6 provides that since the process of establishing a common external tariff may involve some tariff increases and decreases by members, compensatory adjustment may become necessary if any of the increased tariffs conflict with a GATT binding. The intention is to avoid adverse effects on the trade of third countries and to provide an incentive to ensure that the rationale of the union is trade creating, rather than trade diverting.

If the common external tariff is higher than the bound tariffs of any member of the union, Article XXVIII procedures apply. Article XXVIII requires trade negotiations with members with whom the tariff binding was initially negotiated and with principal suppliers of the product involved in order to obtain agreement on a compensatory reduction in tariffs on other products. In such negotiations the intention is to 'maintain a general level of reciprocal and mutually advantageous concessions not less favourable to trade than that provided for ... prior to such negotiations'. If no agreement is reached, the adversely affected trading partners are free to withdraw previously negotiated tariff concessions, but on a most-favoured-nation basis. This makes it very difficult to target retaliation on an individual member of the union without also affecting trade interests of other WTO members. Perhaps because of this, there is no indication in Article XXIV that failure to follow the Article XXVIII procedure would affect the customs union from qualifying for the GATT exception.

Introducing a common external tariff may also affect preferences allowed under Article I. Article XXIV:9 provides that such changes in the preferences shall occur 'by means of negotiations with WTO members affected'. These negotiations too follow the same legal framework as provided in Article XXVIII.

Retaliatory action has never been taken under Article XXVIII in connection with Article XXIV:6 negotiations. This may show either that the negotiations were always successful or that it was not practicable to locate specific concessions which could be withdrawn in retaliation.

Under Article XXIV:8, a customs union results in a new 'customs territory' to which GATT obligations could apply directly. For instance, after proper notification, the Southern African Customs Union (SACU) territory could be regarded as a new 'customs territory'. The customs territory could be recognised by the WTO as a member in its own right. So far, the European Union is the only customs union which is a member of the WTO in its own right, of course in conjunction with its members.

(b) **Free-trade area**

Free-trade areas are a much simpler arrangement and are far more common than customs unions. With respect to a free-trade area, Article XXIV:8(b) merely requires the elimination of duties and restrictions on 'substantially all the trade' between the members, without the requirement of a uniform external tariff and regulations on the trade of non-members. Consequently, members could retain their external tariffs very much as they were before the free-trade area was formed. All that Article XXIV:5(b) requires is that each member's duties and regulations of commerce 'shall not be higher or more restrictive than the corresponding' ones existing prior to the formation of the free-trade area or the interim agreement leading to the formation of such an area. The Article XXIV:5(b) requirement applies only to the time of formation of the arrangement; subsequently they could be raised subject to other GATT obligations.

Rules of origin are particularly significant in respect of free trade areas, as the preferential tariff treatment only applies to products originating in the participating countries. All free-trade areas therefore provide for rules-of-origin requirements. Surprisingly, Article XXIV does not deal with them at all.

Under Article XXIV:8(b), a free-trade area is a 'group of two or more customs territories' to which GATT obligations do not apply directly.

(c) **Interim agreements**

Article XXIV:5 provides that 'an interim agreement leading to the formation' of either a customs union or a free-trade area is eligible for an most-favoured-nation exception if certain conditions are met. The provision for an interim period for the formation of a customs union or free-trade area is logical because sudden removal of trade barriers between two or more countries could greatly disturb the economies involved. In fact, substantial readjustment would almost always be needed and it therefore makes sense that the transition to such an arrangement should be gradual rather than sudden. Duties could be reduced, step by step, over a considerable period of time. It is no wonder that almost all the regional arrangements brought to what was then GATT were basically 'interim agreements'.

Article XXIV:5(c) provides that any 'interim agreement ... [submitted to the WTO] shall include a plan and a schedule for the formation of such a customs union or a free-trade area within a reasonable length of time'. This provision modifies the Article XXIV:8 requirement that 'substantially all' trade between constituent territories be freed from restrictions and, in the case of a customs union, a common external tariff be established. Article XXIV:5(c) requires (a) a 'plan and a schedule', that (b) will lead to the defined arrangement within a 'reasonable' time.

Any interim agreement must also meet the basic requirements of Article XXIV:5. Therefore, an interim agreement leading to the

formation of a customs union must not have duties which are on the whole higher than the 'general incidence' of such duties prior to the formation of the customs union. An interim agreement leading to the formation of a free-trade area must not have 'corresponding duties' higher than prior to the formation of the free-trade area.

2.1 Legal analysis of Article XXIV

Article XXIV provisions are unclear and ambiguous and have given rise to controversies. Below is a thumbnail sketch of these controversies.

(a) **'Prompt notification'**

Article XXIV:7 requires that any member deciding to enter into a customs union, free-trade area or an interim agreement leading to such union or area must notify other members 'promptly' and provide information about the arrangement so that members may make appropriate recommendations. This can be described as the transparency requirement. But what is a 'prompt' notification? Should notification be made before putting the arrangement into force or after? Article XXIV offers no guidance.

In some instances notification was made with a view to obtaining approval from members before putting the regional arrangement into force. The Treaty of Rome, the most notable example, was signed on 25 March 1957 and notified to the GATT immediately thereafter. The treaty entered into force only on 1 January 1958.

Particularly since 1980, GATT (or the WTO) has usually only been notified after the regional arrangement has obtained the approval of the domestic legislatures. The North American Free Trade Agreement (NAFTA) was ratified by Canada, Mexico and the United States in 1993 and entered into force on 1 January 1994. A GATT Working Party to examine it was set up only later. This practice of notifying what is now the WTO only after securing the approval of the members has been justified on the grounds that submitting an arrangement for approval beforehand carries the risk that it may fail to be approved by the domestic legislatures subsequently. However, this practice did not quite meet the approval of the GATT Council.

The GATT Council decided in 1972 that prompt notification requires that the members, after signing a regional arrangement, should promptly notify what is now the WTO so that the arrangement would be on the agenda of the first meeting of the Council following such signature. This ruling may encourage members to enter into arrangements where the interval between signing an arrangement and its entry into force is very short.

(b) **'A plan and a schedule'**

As pointed out earlier, most of the regional arrangements are notified to the WTO as interim agreements. Article XXIV:7(b) requires that the members shall provide a 'plan and a schedule' for the formation of a customs union or a free-trade area. The requirement of a 'plan and a schedule' serves to ensure that the interim agreement is not being used as a pretext for introducing discriminatory preferences to the prejudice of other members. WTO members, acting jointly, examine the 'plan and the schedule'. If examination shows that the interim agreement is unlikely to result in a customs union or a free-trade area within the period contemplated by the members, or if the period is not reasonable, the members acting jointly may make appropriate recommendations, by a majority of the votes cast (GATT Article XXV:4). In practice, however, decisions have been taken by consensus. These recommendations must be incorporated into the interim agreement if it is to be put into force. One view is that the initiative for disapproval must come from the WTO members acting jointly, which means that, in the absence of such disapproval,

the interim agreement is deemed to be consistent with Article XXIV. Another view is that as long as it has not received the approval, its legal status remains uncertain. Recent GATT cases show that it is the latter view which is to be preferred.

The records of GATT preparatory work suggested that the 'plan and schedule' were to contain fairly definite obligations in the interim agreement on the basis of which the members could objectively conclude that it would lead to a full customs union or a free-trade area in future. But this proved to be unrealistic. When members first enter into a regional arrangement, the precise details of the plan and the schedule are unclear. It is only time and experience that fills them in. This is difficult to reconcile with Article XXIV:7(b), which requires members to determine, obviously on the basis of the plan and schedule, among others, whether the interim agreement would clearly and unambiguously lead to the establishment of a customs union or a free-trade area within a well-defined period of time. The Treaty of Rome was one such regional arrangement.

However, most of the regional arrangements presented to the then GATT fell far short of these requirements. For the customs union agreement between South Africa and Southern Rhodesia, an undertaking was initially made to submit a definite plan and schedule five years later, by 1 July 1954. This was not done and more time was allowed. (Subsequently this customs union lapsed. A new trade arrangement between South Africa and Southern Rhodesia was entered into, which secured a series of waivers under Article XXV:5. The waivers terminated on 30 June 1965 and the whole arrangement came to an end.) In the case of Turkey's association with the EEC,[1] it was contended that the 'plan and schedule' need not be detailed and complex and the Working Party members were reminded that on previous occasions members had accepted regional arrangements which were 'somewhat imprecise in this respect'.. The fact that Turkey is a developing country [2] perhaps played a role. We shall discuss this later under the Enabling Clause.

The Understanding on Article XXIV, which came out of the Uruguay Round of negotiations, requires *all* agreements notified under Article XXIV to be examined by a Working Party. These Working Parties are instituted by the Council at the request of one or several contracting parties. The terms of reference of Working Parties are generally to examine a matter in the light of the relevant provisions of the GATT and to report to the Council. Generally, working parties consist of a number of delegations varying from about five to twenty according to the importance of the question and the interests involved.

The Understanding clarifies that if an interim agreement is notified to the WTO without a plan and a schedule, the Working Party must recommend a plan and schedule. This would probably also cover a situation where the plan and the schedule that were submitted is inadequate. The Understanding does not require that the plan and schedule be very detailed or contain a set of unambiguous and clear obligations on the part of the members. But the parties must not maintain or put into force, as the case may be, any interim agreement if they are not prepared to modify it in accordance with recommendations made.

Article XXIV:7(b) requires that the interim agreement must lead to the establishment of a customs union or a free-trade area within a reasonable length of time. What is meant by 'reasonable time'? During the GATT preparatory work in 1946, the South African

[1] The expression 'EEC' is used throughout for the sake of consistency. The EEC is now the European Union.

[2] The terms 'less-developed' and 'developing' countries are used interchangeably in this report.

delegation proposed that a definite time-limit be set in Article XXIV:7(b). This was not accepted and it was decided to leave it open-ended. In recent years, however, it is common to find in the interim agreements a fixed timetable for the establishment of a customs union or a free-trade area, as the case may be. The Article XXIV Understanding makes it clear that the interim agreement must lead to the establishment of a customs union or a free-trade area in not more than ten years. Only in very exceptional circumstances may the period of ten years be extended.

The Understanding on Article XXIV requires the Working Party to submit a report to the Council for Trade in Goods on its findings. The Council may then make appropriate recommendations to the members. The Final Act reiterates the requirement of biennial reporting on progress made by the members of the regional arrangements. In the past, this was often not done. The Understanding on Article XXIV instructs the Council to implement this requirement to improve the surveillance of the customs unions and free-trade areas. However, there was no agreement on the manner in which the reporting requirement was to be implemented. For example, should there be special WTO sessions for the consideration of the biennial reports?

(c) 'Substantially all trade' requirement

Article XXIV:8 requires that, in both customs unions and free-trade areas, 'duties and other restrictive regulations of commerce' must be eliminated with respect to 'substantially all' the trade between the constituent territories. Article XXIV offers no guidance as to what is meant by 'substantially all'.

This requirement can be interpreted in both qualitative and quantitative terms. This was demonstrated in the European Free Trade Association (EFTA) negotiations. Austria, Denmark, Norway, Portugal, Sweden, Switzerland and the United Kingdom, largely in response to the creation of the EEC, signed the Stockholm Convention in 1960 which established the European Free Trade Association. The primary object was to offset any detrimental effects to their trade resulting from the progressive elimination of tariffs inside the Community by a similar reduction within EFTA. (A number of these countries have since joined the EEC.) When the EFTA agreement came up for consideration at the GATT, third parties argued that if an agreement specifically excluded a major sector of trade (such as unprocessed agricultural products), it would not qualitatively satisfy the 'substantially all trade' requirement in respect of sectors of trade, even if the total trade that was freed quantitatively amounted to 90 per cent of all trade.

On the other hand, the EEC and EFTA members argued that the words used were 'substantially all trade' and not 'trade in substantially all products or sectors', and that quantitative criteria could therefore be used to determine whether the 'substantially all trade' requirement was met. On the basis of this argument, an agreement satisfies Article XXIV:8 requirements even if a sector of economic activity such as agriculture is excluded, so long as the overall percentage of trade that has been freed of trade restrictions is substantial.

The GATT Working Party failed to reach a definite conclusion.

The EEC once argued that if 80 per cent of total trade was liberalised in a free-trade area, this should be regarded as satisfying the 'substantially all trade' requirement. That case concerned the EEC's overseas territories' arrangements and involved setting up 18 bilateral free-trade areas, one with each of 18 developing countries in Africa, by the

eliminated duties and other restrictive trade regulations on substantially all products originating from the 18 overseas territories, which in turn removed customs tariffs on most imports from the EEC. The EEC argued that the liberalisation was in respect of 98,6 per cent of total trade. This position was justified by totalling the intra-European trade among EEC countries (at that time, the original six members) with the trade with each of the 18 overseas territories. The EEC refused to supply figures concerning the percentage of trade liberalised between the EEC territories on the one hand and the 18 overseas territories on the other. Despite this, the Working Party did not disapprove the arrangement, which it considered to be no more than a continuation of the colonial preferences that were specifically embodied in Article I and annexes B and C of GATT.

In sum, there has not been any progress, so far, in deciding what proportion of trade could be regarded as 'substantially all' in terms of Article XXIV:8 requirements. The Uruguay Round not only failed to resolve the ambiguity, but used the same language in the agreement on trade in services! However, the preamble to the Understanding on Article XXIV does mention that contribution to the expansion of world trade by customs unions and free-trade areas may be 'diminished if any major sector of trade is excluded'. Words in a preamble do not have the force of law, however, and only the future will tell if these words would swing the interpretation the way the preamble intends.

(d) **Customs unions: 'Not on the whole ... higher or more restrictive than the general incidence' requirement**

Article XXIV:5(a) requires that while a customs union must have a common external tariff and other restrictive trade regulations, on the whole these must not be higher or more restrictive than the general incidence applicable in the constituent territories before the formation. The phrase 'on the whole' is ambiguous. How does one determine the overall level of customs tariffs?

In theory there are three alternatives. One is the simple averaging of tariff rates. The second is to compute a trade-weighted average tariff using the volume of trade for each product as the weights. And the third is to choose the lowest tariff rate on a product applicable in any of the constituent territories as the common external tariff. The three alternatives may have different consequences for the third country exporters. Moreover, no matter which alternative is chosen, the question remains as to whether the exercise would require a systematic comparison on a country-by-country and product-by-product basis to determine if the incidence is higher 'on the whole' and thus prejudicial to other member states.

These questions were considered in the EEC case, when the Treaty of Rome was examined. A substantial number of third countries felt that 'an automatic application of a formula, whether arithmetic average or otherwise, could not be accepted, and agreed that the matter should be approached by examining individual commodities on a country-by-country basis'. This meant that the third countries were against the EEC raising barriers to the trade of any individual third country. This approach was rejected by the EEC member states, who argued that 'the common tariff has to be judged as an entirety', as the wording of Article XXIV:5 is that the duties and other trade restrictions should not 'on the whole' be higher or more restrictive. The EEC used simple arithmetic averaging and justified this by arguing that Article XXIV:5 did not exclude any method of calculation. The EEC further argued that third countries should be considered as a group, for the purpose of the Article. Therefore it should not matter if the market access of an individual third country were adversely affected so long as 'on the whole' market access was not more restrictive. In sum, the EEC insisted that

Article XXIV:5 did not preclude raising barriers to trade in a specific sector or subsector of trade so long as other sectors of trade were liberalised. The Understanding on the Interpretation of Article XXIV provides that the assessment shall be based on a weighted average of tariff rates and of customs duties collected. For this purpose, import statistics for a previous representative period shall be supplied by the customs union, on a tariff line basis and in value and quantities broken down by the WTO country of origin. The WTO secretariat will then compute the weighted average tariff rates and customs duties collected.

Another issue that has given rise to difficulties concerns the meaning of the expression 'applicable' in Article XXIV:5. It requires that a comparison be made between the 'general incidence' of duties and other regulations of the common external tariff or a customs union with those 'applicable in the constituent territories prior to the formation of such union'. The legal question is which duties should be regarded as applicable: duties sanctioned by the law or duties that are factually being applied on goods? When the Treaty of Rome was being examined, the EEC presented data on the basis of the 'legal or bound tariff rates' and on that basis there was no doubt that the common external tariff would be lower than the previous national rates. When the Working Party members asked the EEC to supply data concerning the tariff rates that were actually applied by the individual countries, the EEC refused, saying that Article XXIV:5 did not require it. Some of the individual third countries then produced data based on their own experience of trade with the individual countries of the EEC. These data were not comprehensive, but on the basis of this the Working Party concluded that the 'general incidence of Common Tariff seemed to be higher than the ... tariff rates actually applied ... on January 1, 1957'. There was an inconclusive debate at the end of which all members asked the then Executive Secretary of GATT to provide the correct legal interpretation. The Executive Secretary reported that the drafting history of Article XXIV:5 did not offer any guidance and either of the two interpretations was possible. The Understanding on Article XXIV that emerged from the Uruguay Round makes it clear that the expression 'applicable' means the 'applied rates of duty', that is, factually applied rates.

The third problem concerns the interpretation of the expressions 'at the formation' or 'at the institution'. Article XXIV:5 provides that 'at the institution' or 'at the formation' of a regional arrangement, the applicable duties and other trade restrictions should not on the whole be higher. Does this mean that once the WTO Working Party has approved the regional arrangement, it should be possible for the members to raise the level of tariff and other trade restrictions? This has never been settled. We would answer in the affirmative on the basis of literal interpretation, but presumably subject to all other GATT requirements and obligations. Otherwise a WTO Working Party would be able to impose obligations in perpetuity on a customs union, a free-trade area or an interim agreement.

Fourthly, Article XXIV:5 mentions 'duties and other regulations'. The question is whether the expression 'regulations' also includes 'non-tariff regulations and restrictions'. The Treaty of Rome permitted EEC members to impose quantitative restrictions even when these were not justified by the country's own balance-of-payments position. The EEC defended the provision on the grounds that regional arrangements were an exception not only to the most-favoured-nation provision but also to all other GATT provisions, and that the Working Party should only examine the restrictions if the regional arrangements complied with Article XXIV criteria. Most third party members thought that the expression 'regulations' did not include quantitative restrictions but only covered such things as customs procedures,

grading and marketing requirements and other similar routine controls. It would appear that the 'customs territory' which results in the formation of a customs union should be treated as an entity and be entitled to all GATT exceptions, such as an escape clause or balance of payments.

Fifthly, Article XXIV:6 provides that if a member wishes to increase a bound tariff on a product on joining a customs union, Article XXVIII applies and compensatory adjustment may have to be provided. But in doing so, due account must be taken of the compensation already afforded by the reductions brought about in the corresponding duties of the other members of the union. These words are ambiguous. The Understanding on the Interpretation of Article XXVIII elaborates on the provision in four ways. Firstly, it requires that the negotiations must be entered into in good faith. Secondly, the third countries with whom negotiations may begin must include the country with the highest share in *its exports* of the product affected by the withdrawal or modification. This should help small and medium-sized countries, in particular. Thirdly, negotiating partners are *required* to take due account of reduction of duties only on the same tariff line products. They are not precluded from considering offers of other reductions but cannot be forced to accept them as sufficient. Fourthly, if negotiations on compensatory adjustments do not succeed within a reasonable period, the customs union shall be free to modify or withdraw the concessions.

In that case, the affected third countries shall be free to retaliate and withdraw substantially equivalent concessions in accordance with Article XXVIII.

Another difficult legal question is when should negotiation under Article XXVIII begin: before or after the establishment of the customs union? The Understanding makes it clear that negotiations under Article XXVIII must begin *before* tariff concessions are modified or withdrawn upon the formation of a customs union or an interim agreement leading to the formation of such a union.

While these provisions in the Understanding should remove a major source of potential conflict that was inherent in Article XXIV, the whole issue of the nature of compensation and the modalities that should be adopted under Article XXVIII are still not clear. In the EEC case, the negotiations were extremely complex and rather disappointing for the third country exporters. In fact, at one stage, the Working Party refused to consider the accession of Denmark, Ireland and the United Kingdom to the EEC because of Article XXVIII problems and threatened retaliation by the third party exporters.

Lastly, as discussed above, free-trade areas typically require rules of origin. When the EEC submitted its free-trade arrangement with the individual EFTA countries to the GATT Working Party in 1973, it was argued by the third countries that the rules of origin had been designed in such a manner as to raise barriers to their trade in intermediate products. Not much could be done as GATT did not give any guidelines as to the kind of rules of origin a regional integration arrangement could have. This has now been taken care of by the Agreement on Rules of Origin which came out of the Uruguay Round. While this Agreement does not cater to Article XXIV needs, it does set in a mechanism which would harmonise rules of origin within a three-year period. On account of such harmonisation, the future free-trade areas may be constrained to design the rules in accordance with a set multilateral standard.

3. Regional arrangements: Part IV of GATT and the 'Enabling Clause'

Part IV of the GATT Agreement, comprising Articles XXXVI to XXXVIII, is entitled 'Trade and Development'. It was not part of the original Agreement, but was added by an amending protocol in 1965. Article XXXVI:8 of Part IV provides that the developed member countries do not expect reciprocity in trade negotiations to reduce or to remove tariffs and other barriers to trade of less-developed member countries. Part IV also obliges developed countries to adopt special measures and policies with a view to increasing the imports from the less developed member countries.

The Yaoundé Convention of 1963 (see above) was replaced in 1975 by the Lomé Convention between the EEC and 46 less-developed African, Caribbean and Pacific Island (ACP) States. The Lomé Convention has been reconstructed three times since then. The 1975 Lomé Convention allowed ACP states certain trade preferences for their products in the EEC on the principle of non-reciprocity. The EEC claimed that the regional arrangement was consistent with Article XXIV and Part IV, as well as Article I:2 and Article XXXVI.

Third countries, however, argued that Part IV provided for special treatment for *all* less-developed countries and the Lomé Convention, in effect, would discriminate against less-developed countries which were not members of the Convention. These arguments were repeated again and again when the compatibility of Lomé II, III and IV with Article XXIV read with Part IV of GATT was considered.

In 1994, during the examination of the Lomé IV Convention, the GATT Working Party observed that the Convention would remain inconsistent with GATT so long as the parties to the Convention were not granted a waiver of their contractual obligations under Article XXV. On 9 December 1994, the WTO members, acting jointly, granted a waiver to the Convention countries under Article XXV:3 from most-favoured-nation obligations under Article I:1 until 29 February 2000 to the extent necessary to enable the European Union to provide preferential treatment for products originating in the ACP member states as required by the Convention.

Part of the rationale for this can be found in the Agreement on the Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries, dated 28 November 1979, which was negotiated at the Tokyo Round. It incorporates an 'enabling clause' which provides that, notwithstanding the most-favoured-nation requirements of Article I of GATT, WTO member countries may grant differential and more favourable treatment to developing countries. Paragraph 2(c) of the Agreement applies such treatment to regional and global arrangements entered into among less-developed member countries for the 'mutual reduction or elimination' of tariffs and non-tariff measures. Paragraph 2(d) authorises 'special treatment for the least developed among the developing countries'.

Paragraph 3 of the Agreement imposes certain conditions. The first is that any such arrangement must 'be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade' of other WTO member countries. The second, given in Paragraph 2(c), is that the mutual reduction or elimination of non-tariff measures must be 'in accordance with criteria or conditions' prescribed by the WTO member countries. The third condition is that 'such agreements must not constitute an impediment to the reduction or elimination of tariffs and other restrictions to trade on a most-favoured-nation basis'. The fourth condition is provided in Paragraph 4: such agreements must be notified

to the WTO when introduced, modified or withdrawn, and, on request, the third countries must be given an adequate opportunity to consult with the members of the regional arrangements.

By 1 January 1995, eleven agreements had been notified to the WTO under the Enabling Clause. None of them was from Africa. The only African country party to any of these agreements is Egypt, which entered into a preferential trade arrangement with India and what used to be Yugoslavia, an arrangement which came into force on 1 April 1968. This was the first regional arrangement notified under the Enabling Clause.

There is an unresolved controversy surrounding the application of the Enabling Clause. Since the clause does not make any reference to Article XXIV, the legal question is whether the Enabling Clause provides developing countries with an alternative to form regional arrangements outside Article XXIV. This question is likely to be debated by the WTO Working Party when it meets towards the end of 1995 to examine the Southern Common Market (MERCOSUR), which was notified in 1992 and whose members are Argentina, Brazil, Paraguay and Uruguay. Developing countries believe they do have this option.

4. Regional groupings between developed and developing countries

There has been some debate as to regional groupings between developed and developing countries in the context of Article XXIV. In the 1966 Working Party Report 'EEC — Association Agreements with African and Malagasy States and Overseas Countries and Territories' (in the Yaoundé Convention, discussed above) reference is made to the view of some members of the Working Party that, in a free-trade area consisting of industrialised and less-developed countries, the industrialised countries should not require reciprocal advantage from their less-developed parties, and, in this connection, referred to the principles established in the new Part IV of the General Agreement. In the view of these members, Article XXIV had never been meant to apply to free-trade areas between developed and less-developed countries. The view of the Community and Associated States was that the question of reciprocity was not dealt with in Article XXIV, which only required that restrictions on substantially all the trade between member countries of a customs union or a free-trade area should be removed. It was felt that part IV of the General Agreement did not aim to modify the provisions of Article XXIV. The only test the contracting parties to GATT (now referred to as WTO members) could apply to a free-trade area was whether it satisfied the requirements of Article XXIV, and there was no reason to believe that the authors of Article XXIV had overlooked the possibility of free-trade areas between countries at different stages of development. It was pointed out that the contracting parties had moreover already examined free-trade areas where there had been a greater difference between the stages of development of the constituent territories.

However, the 1976 Report of the Working Party on the ACP-EEC Convention of Lomé noted that the Convention was compatible with parties' obligations under the General Agreement, in particular the provisions of Articles I:2, XXIV and XXXVI, 'which had to be considered side by side and in conjunction with one another...since the objective of the Convention was to implement actions and measures aimed at improving standards of living and the economic development of less-developed countries, it could not but be in line with the objectives pursued by the GATT particularly those of Part IV.'

A report on the Working Party entitled 'Agreement between the European Communities and Israel' records that a member of the Working Party noted the parties' viewpoint that there was nothing in Article XXIV to prevent the timetable for the fulfilment of the reciprocal obligations being phased differently if the parties so agreed. It was felt that such a different phasing could be a legitimate matter for concern especially if the difference was substantial. The representative of Israel did not share this view, especially in the light of the Tokyo Declaration and the need for differential measures providing special and more favourable treatment for developing countries. He said that, in that instance, the parties' different stages of economic development made the phasing appropriate and compatible with the letter and spirit of the General Agreement. It seems that this is the view that prevails at present, in the light of a number of regional groupings of members at vastly differing stages of development, for example NAFTA.

5. Article XXV (Waiver)

Article XXV:5 provides that 'in exceptional circumstances' WTO member countries 'may waive an obligation' imposed on any WTO member country under GATT by a two-thirds majority of the votes cast, provided that such majority consists of more than half the WTO member countries. So far, 28 waivers from Article I have been granted under this provision by the developed countries to the developing countries mostly to promote imports from such countries. However, the total number of waivers granted to regional arrangements has been rather few. The waiver granted to the ACP countries under the Lomé IV Convention in December 1994 is the most recent example.

6. Article XXIV and dispute settlement

The Understanding on Article XXIV clarifies that any matter arising from the examination of any regional arrangement under Article XXIV may invoke the new dispute settlement provisions of GATT 1994. This puts to rest any doubt there may have been concerning the jurisdictional question on issues arising from the working of a regional arrangement already examined by a Working Party. Some thought that only a Working Party had jurisdiction to examine them.

Between 1947 and 1 January 1995, as many as 98 regional integration agreements were notified to the WTO. Of these, 33 were notified between 1990 and 1994 alone. This shows a rapidly growing trend to form such arrangements. It was pointed out earlier that Article XXIV requires their notification and subsequent examination by a Working Party. By the end of December 1994, 69 Working Parties had completed the examination of most of these arrangements. Surprisingly, only in six cases was consensus reached that the regional arrangement conformed to the conditions laid down in Article XXIV. Failure to reach a consensus has therefore been the norm. The most serious case was that of the EEC, where the Working Party failed to reach a consensus as to whether the Treaty of Rome was compatible with Article XXIV. Because of the ambiguities in Article XXIV, the EEC and third parties did not see eye to eye on a number of crucial provisions of the Treaty. As a result, it was concluded that the 'examination and the discussion of the legal questions involved in it could not be usefully pursued at the present time'. The examination was supposed to be taken up later but this never happened.

This sent a wrong signal. Indeed it led to the setting of a pattern which has plagued all subsequent examinations at the WTO. The depth of frustration is clearly visible in the following statement of the Chairman of the Working Party established in the Canada-United States Free Trade Agreement, who observed in 1991:

Over 50 Working Parties on individual customs union or free-trade areas were unable to reach consensus whether they were consistent with Article XXIV. On the other hand, no such agreement had been disapproved explicitly. One might question the wisdom of establishing a Working Party if none expected it to reach consensus findings in respect of specific provisions of such arrangements, or to recommend to their members how to meet certain benchmarks. There is a risk that the regional arrangements would be treated increasingly superficially by the Working Parties and the WTO member countries would lose — if they had not already — their ability to distinguish between agreements of greater or lesser GATT consistency.

These were very strong words. They prompted a review of the way in which the Working Parties examined regional arrangements. The issue has not yet been taken up and is likely to be on the WTO agenda in 1995.

What is perhaps more surprising is that in spite of so many lack-of-consensus findings, so few have been submitted to the dispute settlement proceedings. In fact, there have been only three and they all concerned EEC regional arrangements.

In the first case, the EEC had set up a regional arrangement with certain Mediterranean countries such as Algeria, Cyprus, Egypt, Israel, Jordan, Lebanon, Malta, Morocco, Spain (at that time not an EEC member), Tunisia and Turkey concerning the import of citrus products on preferential terms into the EEC territories. The arrangement could not obtain a consensus finding from the GATT Working Party that it conformed to Article XXIV. The United States initiated dispute settlement proceedings in 1982 that the preferences granted under the arrangement violated the most-favoured-nation rule embodied in Article I:1 and affected adversely its citrus exporters. The GATT Panel that was set up reported that in the absence of a consensus finding the legal status of the arrangement remained open and consequently, the EEC could not take legal cover under Article XXIV to justify its trade preferences with the Mediterranean countries. Therefore, the EEC was asked to begin Article XXVIII negotiations with a view to making necessary compensatory adjustments to the United States. The EEC and the Mediterranean members of the regional arrangement refused to do so on the grounds that this would disrupt the basis and the balance of the arrangement and, therefore, was not a politically viable option.

In the second case, the EEC had proposed to import bananas from the ACP countries on preferential terms under its regional arrangement with them. In February 1993, Colombia, Costa Rica, Guatemala, Nicaragua and Venezuela asked that GATT should set up a dispute settlement panel. The EEC justified the preference on the basis that the ACP countries were less-developed countries and entitled to special treatment under Part IV of GATT read with Article XXIV. But the Panel reported that Part IV did not permit the EEC to discriminate in favour of the ACP group of developing countries with regard to bananas in a manner which would cause substantial prejudice to another group of developing countries. Part IV endorsed special treatment in favour of *all* developing countries. The Panel asked the WTO members to put pressure on the EEC to bring its measures into conformity with GATT.

In the third case, the EEC established a common market organisation for bananas. While the traditional ACP countries were allowed duty-free access for their bananas, non-traditional ACP countries and others were given a combined quota of 2 million tonnes only. Colombia, Costa Rica, Guatemala, Nicaragua and Venezuela began dispute settlement proceedings against such measures, which led to the establishment of a panel in June 1993. The Panel ruled in favour of the Latin American claimants that the EEC measures infringed several GATT obligations. Following negotiations, the EEC set up a quota of 2.2 million tonnes of bananas for Colombia, Costa Rica, Nicaragua and Venezuela. Guatemala's quota has not yet been finally agreed to.

In each of these three cases, the EEC was able to block the adoption of the panel rulings by the Council. Under the new dispute settlement procedure, this would no longer be possible. Under the new system, claimants are entitled to have a dispute settlement panel set up to obtain a ruling on any of the measures applied by another WTO member or members. Once the ruling has been given, it will have to be adopted by the Dispute Settlement Body (DSB) of the WTO within the prescribed period unless one of the parties notifies its decision to appeal or the DSB decides by consensus not to adopt the report. The appellate body is bound to give its report within the prescribed period. It would go to the DSB for adoption. Once the DSB adopts the report, parties are bound to implement it. If it is not implemented, the DSB may authorise retaliatory measures.

The implications of the new dispute settlement procedure for regional arrangements are far-reaching. It may become very difficult to ignore a lack-of-consensus finding on a regional arrangement regarding its Article XXIV conformity. Future regional arrangements are likely to be designed with a great deal of care and sensitivity for the trade rights of the third parties.

7. SACU, SADC and the proposed Indian Ocean Region (IOR)

South Africa is a long-standing member of the Southern African Customs Union (SACU), whose other members are Botswana, Lesotho, Namibia and Swaziland. All of the members of the SACU are also members of the South African Development Community (SADC). Recently, the South African government was invited to join Australia, India, Kenya, Mauritius, Oman and Singapore to establish a trade and security region. This raises an interesting question, namely, whether Article XXIV permits a member of one regional arrangement (like SACU) to join another arrangement (like the IOR).

To begin with, Article XXIV does not prohibit a WTO member country from being a member of more than one regional arrangement. Neither does it put any upper limit on the number of regional arrangements to which a country may become member to. The EEC, for example, is a member of more than 40 regional arrangements of one kind or another. South Africa, therefore, can become a member of SACU, SADC and IOR at the same time without infringing any of its GATT obligations.

South Africa is classified as a developed country, and therefore the SACU Agreement does not fall within the ambit of the Enabling Clause, although the other SACU members are all developing or least developed countries.

The SACU Agreement has never been formally notified to GATT, nor has it undergone a review under Article XXIV, the apparent reason being that the original

agreement predates GATT. There has, however, been some recent pressure, particularly from the United States, for compliance with Article XXIV, on the basis that the SACU Agreement has undergone substantial changes since 1948. While the SACU Agreement would in all probability satisfy the third requirement of Article XXIV, there is some uncertainty as to whether the second requirement would be satisfied.

The SACU is not a 'customs territory' for the purposes of Article XXIV:8 and members of the SACU remain contracting parties to GATT in their own right. While the SACU states have a common customs tariff, their individual rights and obligations in respect of other issues of GATT appear to remain in tact.

In its present form, SADC embodies a number of objectives, including the co-operation in trade matters, without any specific obligations at this stage. It has therefore not been necessary (certainly at this stage) to notify SADC in terms of Article XXIV. SADC is, however, at present negotiating a trade protocol, in which it aims to give practical effect to the trade co-operation objective. We assume that both the proposed IOR and SADC trade regimes would be essentially free-trade areas to begin with. In that case, the question will be the relationship between SACU and such proposed free-trade areas and the legal problems to which this relationship may give rise. A good precedent to consider in this context is the way the EEC, a customs union, widened itself by creating and joining free-trade areas, most notably the European Free Trade Association. The EEC, a customs union, joined EFTA, a free-trade area. Since then, the EEC, and its successor organisations the EC and EU, has joined many other free-trade areas.

If SACU, after it has been reconstituted, becomes a legal entity and has power to enter into and form regional arrangements with other countries either individually or as a group, then there should not be any difficulty for SACU to participate in free-trade areas like SADC and the IOR. There are enough precedents it could rely on. The EEC, for instance, has formed free-trade areas with single countries (such as Sweden, Portugal, Egypt and Cyprus) and a group of countries, such as EFTA. To meet such an objective, it would be advisable for SACU to provide conditions for such association in the SACU Agreement itself.

Could one member of SACU, for example South Africa, enter into a free-trade area type regional arrangement? To begin with, conditions for such an association would have to be provided in the SACU Agreement itself. Until recently, some members of SACU, such as Lesotho and Swaziland, were members of the Preferential Trade Area (PTA). At present, they are members of COMESA, which is clearly incompatible with the SACU Agreement. It is also known that some members of SACU have entered into bilateral trade treaties. But this has all been done in a rather unsystematic manner primarily because the present SACU Agreement does not fully regulate such associations.

Article 19(1) of the SACU Agreement prohibits a contracting party, without the prior concurrence of the other contracting parties, from entering into a trade agreement with a country outside the common customs area in terms of which concessions on the duties in force in the common customs area are granted to that country. This has not proved to be a problem in respect of SADC up until now as joining SADC has not meant granting any concessions on duties to any country, and therefore there has been no contravention of Article 19(1). In any event, all SACU countries are now SADC members.

It would appear, however, that the SACU countries would need to act in concert, and be treated as one, in the SADC negotiations for the reduction of tariffs.

Article 24 of the SADC Treaty provides that subject to Article 6(1), member states and SADC shall maintain good working relations and other forms of cooperation, and may enter into agreements with other states, regional and international organisations, whose objectives are compatible with the objectives of SADC and the provisions of the Treaty. Section 6(1) provides for member states to refrain from taking any measure likely to jeopardise the sustenance of its principles, the achievements of its objectives and the implementation of the provisions of the Treaty. No reference is made to existing agreements between SADC members and third countries.

A number of the countries with whom South Africa has existing trade arrangements are members of SADC, that is, Malawi, Mozambique and Zimbabwe. While at this stage there is no direct conflict with SADC, it could be argued that all the trade agreements or arrangements with South Africa granting tariff preferences are not compatible with the ultimate objectives of SADC, particularly those relating to the elimination of obstacles to the free movement of goods among member states. It is likely, however, that these arrangements will be accommodated within SADC.

What has been the position in the WTO notified customs unions? The WTO notified customs unions between 1947 and 1 January 1995 number only eight out of a total of 95 notified regional arrangements. Among these eight, there has not been a single instance where a member of a customs union has joined another free-trade area. The problem may not be with the members of the customs union but with the free-trade area. A customs union does not have rules of origin; a free-trade area does. Consequently, the PTA Treaty had to have special exemptions for SACU members when they joined PTA. They proved to be far from satisfactory.

Generally speaking, free-trade areas hesitate to take in a single member of a customs union. The inherent conflict between the obligations of a single member under a customs union and its obligations towards the members of a free-trade area makes the whole exercise an extremely complex one. In theory, it can be done and South Africa can join the IOR, for example, on its own rather than as part of SACU. But it would be problematic both at the SACU level and, when the arrangement comes up for a consensus finding under Article XXIV, at the WTO level.

If SACU joined a regional arrangement as a customs territory, it would be treading familiar territory. This has been done many times. The most famous is the EEC/EFTA example. The GATT Working Party examined the relevant provisions of the Stockholm Convention, which set it up, and their practical implications for the third parties. It also examined its consistency with Article XXIV.

The Rules of Origin under the Stockholm Convention came under a great deal of scrutiny. The third parties found the design of these rules to be technically complex, which made it difficult for them to see clearly in advance the effects they could have on trade. The third parties were also not sure how these rules would be administered and interpreted.

As pointed out earlier, henceforth the Rules of Origin would have to consider the 1994 Agreement on Rules of Origin that emerged from the Uruguay Round. It is envisaged that in three years' time (that is by 1997), a multilateral standard for the Rules of Origin may be established. In the interim period, nevertheless, a WTO Working Party is likely to examine the Rules of Origin of any free-trade area against the provisions of the 1994 Agreement. This has obvious implications for South Africa or the SACU joining any proposed free-trade area like SADC or the IOR.

Another issue that the Working Party debated at length in the EFTA case related to a fundamental question: Whether the combined effects of the Stockholm Convention and the regimes applicable to trade between the EEC and other European and overseas territories to which the EEC extended preferences would, in effect, serve to enlarge the area in which the preferences would be effective and if so, whether it would not affect the trade interests of the third parties adversely.

This is a question that third parties often pose when a customs union proposes to join a free-trade area. If SACU joins the proposed SADC or IOR free-trade areas, for example, a large area of trade preferences would certainly be created. The members of SACU, SADC and the IOR would enjoy certain trade preferences which would be denied to non-members. To an extent, this is bound to affect them adversely. Regarding the SADC free-trade area, legal cover could not necessarily be taken in terms of Part IV of GATT and the Enabling Clause as South Africa is considered to be a developed country, although all the other SADC members are developing countries. Unless South Africa could negotiate some sort of arrangement for the purpose of its regional groupings in Southern Africa, that it be regarded as a developing country, Article XXIV would apply to all its regional groupings. (This may not be out of the question bearing in mind that South Africa has been granted Generalised System of Preferences benefits by a number of developed countries.) Even if the regional arrangement were subject to Article XXIV requirements and found to be inconsistent, waiver could be sought under Article XXV as was done in the Lomé IV case in December 1994. WTO member countries, acting jointly, granted a waiver without much difficulty.

The proposed IOR is a little different from SADC. It has Australia and Singapore, among others, as its members. That would rule out the application of Part IV and the Enabling Clause option. The free-trade area would have to be justified in terms of Article XXIV. The usual argument that is taken when a customs union joins a proposed free-trade area emphasises that the trade-creating effects of the arrangement would substantially exceed its trade-diverting effects. For instance, it could be argued that the arrangement would not create new obstacles to trade with the third countries, but would, on the contrary, encourage trade with them by strengthening the economy of the region. The requirements of a plan and a schedule and the rules of origin may be used to buttress the arguments.

The issue of the non-discriminatory application of quantitative restrictions was raised and debated at great length. Some of the members of EFTA maintained quantitative restrictions. Third parties argued that these restrictions may be relaxed for the members of the free-trade area but not for the third parties. They argued that Article XXIV required that, with respect to quantitative restrictions, the most-favoured-nation rule must be applied. EFTA members and the EEC merely replied that they hoped to relax restrictions on a non-discriminatory basis. A related issue was whether an EFTA member could impose fresh restrictions on imports from non-EFTA and non-EEC members on the grounds of balance-of-payments difficulties? On this it was agreed that in such a case, the EFTA member would have to abide by Articles XII to XV of GATT. In sum, the issue remained unresolved. It is possible that the new Disputes Settlement Board of the WTO would have to give a ruling on it as and when it gets an opportunity.

With regard to the consistency of the Stockholm Convention with Article XXIV, the Working Party raised questions such as whether the free-trade area covered 'substantially all the trade' if the agricultural sector was largely excluded and whether the provisions on quantitative restrictions were consistent with Article XXIV. The treatment of the agricultural sector gave the most

problems as it was governed not only by the Stockholm Convention but also by several bilateral treaties, which the third parties argued could not take the legal cover under Article XXIV. In any case, the Working Party found some of their provisions inconsistent with Article XXIV. They could not be approved by the Working Party. The third parties also did not agree with the EEC and EFTA on quantitative restrictions and insisted they must be applied in a non-discriminatory manner with respect to both EFTA and EEC members and other non-members.

In conclusion, the Working Party recommended to WTO members that they were unable to approve the arrangement as being consistent with Article XXIV. As a result, the status of the regional arrangement remained open. Until a few years ago, the legal status of such open regional arrangements met only frowns; complainants did not test their validity in a dispute settlement proceeding. This is now beginning to change. Of the three cases that tested the legal validity of such open arrangements, two arose in the last two years alone. The Panel has given a ruling that open arrangements do not constitute conformity and the third parties have a right to demand compensatory adjustments under Article XXVIII. The proliferation of such open arrangements also led to a provision in the Understanding on Article XXIV that *all* arrangements notified to the WTO so far should be re-examined with respect to their consistency with Article XXIV and their progress monitored in a systematic manner.

It is likely that some of these concerns may be raised when SACU, IOR or SADC regional arrangements are notified for approval. This would require that adequate attention be paid to the legal design of the arrangement with the proposed IOR in the light of the concerns highlighted in this report.

8. Conclusion

There is growing international concern over the mushrooming of preferential trading arrangements that are inconsistent with Article XXIV and yet are operational as if they were consistent. There is a feeling that this undermines the integrity of GATT in letter and in spirit. The view has been expressed that for the future of the most-favoured-nation system of trade and viability of GATT, it is important that Article XXIV should not be used to justify departures from most-favoured-nation treatment except when it is obvious that Article XXIV criteria have been be met. The developing countries could still be treated differentially and more favourably in terms of Part IV of GATT and the Enabling Clause.