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# IS THE WTO QUIETLY FADING AWAY? THE NEW REGIONALISM AND GLOBAL TRADE RULES

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Trade Rules

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Abstract

While scholars and governments alike view the liberalization of international trade as a positive development, they disagree on the medium to accomplish this objective with the highest economic returns. Some experts believe that multilateralism through the 150+ Member World Trade Organization (WTO) is the only way to achieve truly open and efficient

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trade. Others view multilateralism as but an aspiration and find that regionalism offers the only viable prospect for the meaningful further opening of markets.

In light of what we label New Regionalism, our paper analyzes the positive and negative effects of regional trade arrangements (RTAs). In so doing, we necessarily pass judgment on the counterfactual of using global trading rules to increase disciplines on government restrictions on the further liberalization of trade. We begin by describing how New Regionalism affects assessment of the benefits and disadvantages of RTAs, then trace the historical and legal background of RTAs, and conclude by seeking to answer the question whether the WTO and other global institutions continue to serve a useful function.

We find that while RTAs can increase efficiency by parlaying the commonalities of neighboring countries into more cooperative trade relationships, RTAs also can undermine the benefits of multilateral consensus with provisions that, although not inconsistent, dilute that consensus through rigorous additional disciplines. We note that the marriage of developed and emerging market countries in RTAs often has positive effects on infrastructural development, but that RTAs can confuse and fragment trade through the “spaghetti bowl” effect of hundreds of different preferences that must at great cost be navigated, an especial burden for small firms. We learn that RTAs can speed trade liberalization by addressing issues such as migration, energy, and transit that the WTO has not brought to ground, but that they slow multilateral consensus on these subjects because WTO Members, especially emerging market countries, have insufficient resources to engage meaningfully on both regional and global levels.

In the end, we find surprising common cause between the WTO and its plethora of regional offspring. Proceeding from this premise, we offer to trade policy officials specific prescriptions for addressing the changing roles of global and regional instruments, including the need and means to design development strategies at different levels and the use of RTAs to activate the most efficient aspects of multilateralism.

## **I. Introduction**

While scholars and governments alike view the liberalization of international trade as a positive development, they disagree on the medium to accomplish this objective with the highest economic returns. Some experts believe that multilateralism through the 150+ Member World Trade Organization (WTO) is the

only way to achieve truly open and efficient trade. Others view multilateralism as but an aspiration and find that regionalism offers the only viable prospect for the meaningful further opening of markets.

In light of what we label the New Regionalism, our paper explores in detail the positive and negative effects of regional trade arrangements (RTAs). In so doing, we necessarily pass judgment on the counterfactual of using global trading rules to increase disciplines on government restrictions on the further liberalization of trade. In Part II, we describe the "new regionalism" and explain how it affects assessment of the benefits and disadvantages of RTAs. In Part III, we trace the historical and legal background of RTAs beginning with the 1947 General Agreement on Tariffs and Trade (GATT).

The closely-related Parts IV and V examine in detail the positive and negative benefits of regional economic arrangements, primarily from an economic perspective. Our conclusions in Part VI seek to answer the question whether the WTO and other global institutions continue to serve a useful function from an economic standpoint. We offer to policy officials dealing with regional trade treaties specific prescriptions for addressing the changing roles of global and regional instruments.

## I. The New Regionalism

Complicating our comparison of regional and global alliances is the emergence of "new regionalism."<sup>2</sup> New regionalism differs from prior efforts at regional integration in a variety of respects and most definitions share certain commonalities. Old regionalism was a Cold War phenomenon with specific objectives such as trade or security, whereas new regionalism is the result of a multidimensional, comprehensive societal approach in a context of globalization and a multi-polar world.<sup>3</sup> In addition to economic integration and trade, new regionalism includes political, social, economic, and cultural aspects, as well as security and democracy, the environment, social policy, governmental accountability, and legitimacy.

Unlike old regionalism, new regionalism is created within a region by the constituent members instead of by superpowers and is characterized by the participation of state and non-state actors.<sup>4</sup> New regionalism is structured to make economies more open, competitive, democratic, and market based<sup>5</sup> instead of being

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<sup>2</sup> This discussion is drawn in part from Stephen Joseph Powell and Patricia Camino Pérez, *Global Laws, Local Lives: Impact of the New Regionalism on Human Rights Compliance*, 17 Buffalo Hum. Rts. L. Rev. (Spring 2011).

<sup>3</sup> Björn Hettne & András Inotai, THE NEW REGIONALISM: IMPLICATIONS FOR GLOBAL DEVELOPMENT AND INTERNATIONAL SECURITY. 1-2 (Helsinki: UN Univ., World Inst. Dev. & Econ. Res 1994), available at [http://www.wider.unu.edu/publications/working-papers/previous/en\\_GB/rfa-14/](http://www.wider.unu.edu/publications/working-papers/previous/en_GB/rfa-14/) (last visited January 16, 2011).

<sup>4</sup> Id. At 1-2.

<sup>5</sup> Robert Devlin & Antoni Esteveadeordal, Working Paper 6, What's New in the New Regionalism of the Americas? 21 (2001), at <http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=35309686> (last visited January 16, 2011).

inward oriented. RTAs are used to help consolidate and prompt economic and political reforms in prospective members. New regionalism is characterized by high levels of economic interdependence and a multilateral framework.<sup>6</sup> In addition, new regionalism anticipates deeper integration, as well as linkage of developed and emerging market countries.<sup>7</sup> Deep integration involves expanding or establishing the institutional environment to facilitate trade and the location of production regardless of national borders.<sup>8</sup> New regionalism involves the achievement of full economic union and may include facilitating foreign direct investment (FDI) flows, liberalizing the movement of labor, harmonizing domestic subsidy and tax policies, harmonizing macro-economic policies, establishing institutions to facilitate and manage integration, improving transportation and communications infrastructure, and monetary union through establishment of a common currency and integrated exchange rate and monetary policy.<sup>9</sup> Features of new regionalism also include: knowledge and technology transfers and diffusion, dynamic comparative advantage, elimination of wasteful rent seeking activities, pro-competitive gains through increasing import

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6 Id.

7 Mary E. Burfisher, Sherman Robinson & Karen Thierfelder, MTID Discussion Paper No. 65, *Regionalism: Old and New, Theory and Practice* 4 (2004), at <http://www.ifpri.org/sites/default/files/publications/mtidp65.pdf>.

<sup>8</sup> Sherman Robinson, Mary Burfisher, Scott McDonald, & Karen Thierfelder, *Deep Integration and Trade Productivity Links: Tentative Lessons for CGE International Trade Models* 7 (2006), at <https://www.gtap.agecon.purdue.edu/resources/download/2707.pdf> (last visited January 16, 2011).

<sup>9</sup> See Burfisher, *supra* note 7, at 10-11.

competition, increased geographical dispersion of products, increased FDI, and increased efficiency through greater competition.<sup>10</sup>

As noted, regionalism also is characterized by its creation of linkages between developing and developed countries. For example, the United States has RTAs with Emerging Market countries: Israel, the North American Free Trade Agreement,<sup>11</sup> Jordan, Morocco, Chile, the DR-CAFTA, and Peru; the EU has 35 RTAs with Emerging Market countries.<sup>12</sup>

Because the new regionalism and its deeper integration involve elements that are not purely economic, it is difficult to evaluate RTAs formed under new regionalism using the economic techniques created to evaluate old regionalism RTAs. As discussed below, economic evaluation takes into account only trade creation and trade diversion effects. In evaluating RTAs under new regionalism, new trade theories evaluate trade-productivity links, rent-seeking behavior, and imperfect competition.<sup>13</sup>

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<sup>10</sup> Id. at 27 -28.

<sup>11</sup> North American Free Trade Agreement, done Dec. 17, 1992, U.S. - Can. - Mex., 32 I.L.M. 289 (chs. 1-9); 32 I.L.M. 605 (chs. 10-22) [hereinafter NAFTA]

<sup>12</sup> Burfisher, *supra* note 7, at 11; David A. Gantz, REGIONAL TRADE AGREEMENTS: LAW, POLICY AND PRACTICE 207 *et seq.* (Durham: Carolina Academic Press 2009).

<sup>13</sup> See Burfisher, *supra* note 7, at 27.

## II. Regionalism under the GATT

Economic valuation of RTAs relies on two yardsticks: trade creation, the benefit that members of an RTA receive after forming the RTA; and trade diversion, the economic disadvantage that third parties and the RTA members themselves bear as a result of forming the RTA.<sup>14</sup> Trade creation means that intra-regional trade has increased, while trade diversion refers to the loss of trade from non-parties that result from lowering intra-regional trade barriers.<sup>15</sup> RTAs result in both trade creation and diversion. Therefore, the relevant question in determining the economic utility of an RTA is whether it creates more trade than it diverts.

Theories that measure the economic gains and losses from RTAs generally focus on two types: first, static gains and losses, which are created by a one-time reallocation of an existing stock of labor, capital, and other resources; and second, dynamic gains and losses, which are created from the other effects on potential output and productive capacity, including economies of scale, an improved investment climate, increased competition, an increased pace of technological change, and spill-over effects. Static gains and losses depend upon the size

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<sup>14</sup> Mohammad F. Nsour, *Regional Trade Agreements in the Era of Globalization: A Legal Analysis*, 33 N.C. J. INT'L L. & COM. REG. 359, 365 (2008).

<sup>15</sup> *Id.*



of the gains which result from trade creation and losses from trade suppression or diversion.<sup>16</sup> Trade creation is a positive consequence, while trade diversion is a negative consequence. Opponents of RTAs argue that they undermine the objectives of multilateral trade through the protection of less competitive industries.<sup>17</sup> In this view, RTAs also are discriminatory, encourage disintegration, and occur at the expense of third parties.

Proponents of RTAs contend that they increase trade and trade specialization, are a stepping stone toward a fully integrated global economy, allow countries to examine liberalization strategies on a smaller scale before applying them universally, and are not harmful to the global welfare, even if they do not provide as many benefits to world welfare as would multilateral disciplines.<sup>18</sup>

### **III. Positive Economic Effects of Regionalism**

Even conceding that that the need for multi-country cooperation to achieve the highest economic returns is great; since the Uruguay Round was concluded in 1994, multilateral talks have sputtered, victim to a true lack of international consensus on a

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<sup>16</sup> Jason R. Wolff, *Putting the Cart Before the Horse: Assessing Opportunities for Regional Integration in Latin America and the Caribbean*, 20-SPG FLETCHER F. WORLD AFF. 103,105(1996).

<sup>17</sup> See Nsour, *supra* note 14, at 365-6.

<sup>18</sup> *Id.* at 366-7.

number of critical issues, an escalation of the North-South Divide, and an obsession with multilateralism to solve the world's problems. Moises Naim, editor-in-chief of Foreign Policy Magazine, proposes a theory that he calls "minilateralism," a process that anticipates utilizing the smallest number of countries needed to have the largest possible effect on solving a particular problem. We may think of the number of countries as minilateralism's "magic number," which depends on the type and nature of the problem.<sup>19</sup>

Naim offers an example of how minilateralism could merge the best aspects of both global and regional trade governance. The Group of Twenty includes rich and poor countries from across six continents and accounts for 85% of the world's economy.<sup>20</sup> The countries in the G-20 could potentially reach a trade deal among themselves, for example, on trade in environmental products that counter global climate change, and allow other countries to join. By using minilateralism's magic number, a process to advance trade liberalization could break the multilateral gridlock and generate solutions that could provide a foundation

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<sup>19</sup> Moises Naim, *Minilateralism: The Magic Number to get Real International Action* (2009), available at <http://yaleglobal.yale.edu> (search: "Naim" and "minilateralism").

<sup>20</sup> *Id.*

upon which negotiators may build agreements that are more inclusive.<sup>21</sup>

### **A. RTAs Increase Efficiency**

In similar fashion, smaller and perhaps more realistic RTAs arguably can provide a solution to gridlock in the global trade arena and can otherwise complement the WTO trading system.<sup>22</sup> Through Article XXIV of the GATT, the original 23 Members professed the belief that RTAs can facilitate international trade.<sup>23</sup> WTO Members often resort to RTAs out of frustration with the multilateral system and its lack of progress, or their lack of progress within the WTO system.<sup>24</sup>

The fewer participants in RTAs allow members to engage in more flexible negotiations.<sup>25</sup> RTAs also focus on the interests of a specific region or group of regions, instead of on global interests.<sup>26</sup> Geographically close, regional neighbors will inevitably trade; often they speak the same language, so communication is facilitated; they share the same legal history,

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<sup>21</sup> *Id.*

<sup>22</sup> Sungjoon Cho, Defragmenting World Trade, 27 NW. J. INT'L L. & BUS. 39,41 (2006).

<sup>23</sup> General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-7, 55 U.N.T.S. 187, art. XXIV:4, (as amended by Special Protocol relating to article XXIV of the General Agreement on Tariffs and Trade, signed at Havana on 24 March 1948, GATT/1/162/, "available at" [http://www.wto.org/gatt\\_docs/English/SULPDF/90310346.pdf](http://www.wto.org/gatt_docs/English/SULPDF/90310346.pdf))

<sup>24</sup> Consultative Board to the WTO Director-General, The Future of the WTO: Addressing Institutional Challenges in the New Millennium 19 (2005), at [http://www.wto.org/english/thewto\\_e/10anniv\\_e/future\\_wto\\_e.pdf](http://www.wto.org/english/thewto_e/10anniv_e/future_wto_e.pdf) (last visited January 16, 2011).  
[hereinafter CB Report]

<sup>25</sup> See Cho, *supra* note 22, at 41.

<sup>26</sup> Rafael Leal-Arcas, The European Union and New Leading Powers, 32 FORDHAM INT'L L.J. 345, 381 (2009).

which avoids the clash of laws; and they engage in the same or similar occupations, with the result that understanding of trade needs is enhanced.<sup>27</sup>

The WTO has a consensus decision-making process in the negotiating rounds and a membership of over 150 countries.<sup>28</sup> Because of the collective decision-making process of the WTO, negotiation processes can be cumbersome, especially in new areas such as services and information technology products. In addition, each member and various coalitions have their individual agendas, making it difficult, if not impossible, to reach a consensus.<sup>29</sup> Negotiations among a smaller group of countries can produce better outcomes in a shorter amount of time. Once these agreements are adopted and implemented, countries can learn valuable lessons, which they can then use in negotiating subsequent multilateral agreements.<sup>30</sup>

## **B. RTAs Provide Solutions to Development Problems**

Trade can create economic ties and increase prosperity, thereby contributing to peace and security.<sup>31</sup> Arguably, a more open and

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<sup>27</sup> STEPHEN JOSEPH POWELL & BERTA ESPERANZA HERNÁNDEZ-TRUYOL, *JUST TRADE: A NEW COVENANT LINKING TRADE AND HUMAN RIGHTS* 41 (New York: NYU Press 2009).

<sup>28</sup> C. O'Neal Taylor, *Regionalism: The Second-Best Option?*, 28 ST. LOUIS U. PUB. L. REV. 155, 169 (2008).

<sup>29</sup> Sungjoon Cho, *Breaking the Barrier Between Regionalism and Multilateralism: A New Perspective on Trade Regionalism*, 42 HARV. INT'L L.J. 419, 432-3 (2001).

<sup>30</sup> Phillip E. Koehnke, *North American Free Trade: Mexico, Canada and the United States*, 12 CHICANO-LATINO L. REV. 67, 68 (1992).

<sup>31</sup> See Leal-Arcas, *supra* note 26, at 346.

equitable trading system can bring peace<sup>32</sup> and prosperity to the world. Regionalism can provide solutions to development problems.<sup>33</sup> There appears to be a consensus that expanded trade plays a key role in a successful development strategy. Emerging market countries often form RTAs with developed countries to compete with non-member states for the developed country's FDI, which includes the prospect of increased productivity and the transfer of technology. The potential for attracting FDI may be great enough to induce countries to introduce reforms. It may also encourage non-members to introduce reforms<sup>34</sup> in order to compete to receive FDI. Because RTAs can encourage both members and non-members to initiate reforms, RTAs have a positive influence on infrastructural and other development.

Regional cooperation for development reduces levels of discord and facilitates development cooperation, thereby turning trade relations into an effective form of conflict prevention.<sup>35</sup> By increasing contact among producers, consumers, and traders across neighboring borders, trade stimulates more harmonious relations<sup>36</sup> by giving these parties an economic incentive to work together and maintain relationships. This can be especially

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<sup>32</sup> Id.

<sup>33</sup> Chun Hung Lin, *Regionalism or Globalism? The Process of Telecommunication Cooperation Within the OAS and NAFTA*, 11-WTR Currents: INT'L TRADE L.J. 30, 33 (2002).

<sup>34</sup> Id.

<sup>35</sup> Id.

<sup>36</sup> Id.

important where the parties have a history of conflict. It gives them a mutual goal toward which each may work. RTAs provide poorer countries with mutual development gains through expanded markets, pooled resources, greater economic diversification, and increased regional investment and trade.<sup>37</sup>

RTAs can also reduce trade in small arms and conflict resources such as illegal timber and blood diamonds.<sup>38</sup> For example, in 1998 the Economic Community of West African States (ECOWAS) established the world's first moratorium on light weapons and placed a ban on the import of new weapons without the approval of ECOWAS members.<sup>39</sup>

In addition, trade creates economic interdependence, making political disputes and military conflict more costly. Countries have to determine whether engaging in a conflict with a trading partner creates enough gains to justify the action. By engaging in a dispute with another country, both countries potentially lose the benefits gained through their trading relations, and are arguably worse off. This could deter many conflicts from occurring. RTAs provide an institution and forum for negotiating

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<sup>37</sup> Oli Brown, Faisal Haq Shaheen, Shaheen Rafi Khan & Moeed Yusuf, *Regional Trade Agreements: Promoting Conflict or Building Peace?* 9, Int'l Inst. Sust. Dev. Oct. 2005; available at [http://www.iisd.org/pdf/2005/security\\_rta\\_conflict.pdf](http://www.iisd.org/pdf/2005/security_rta_conflict.pdf).

<sup>38</sup> *Id.*

<sup>39</sup> "ECOWAS Adopts Curriculum to Control The Flow Of Small Arms" ECOWAS Press Release No. 65/2000,(2000), at [http://www.smallarmssurvey.org/files/portal/issueareas/measures/Measur\\_pdf/r\\_%20measur\\_pdf/Africa/20000831\\_ecowas\\_pressrelaese.pdf](http://www.smallarmssurvey.org/files/portal/issueareas/measures/Measur_pdf/r_%20measur_pdf/Africa/20000831_ecowas_pressrelaese.pdf).

and bargaining, thereby addressing tensions before they become full blown conflicts.<sup>40</sup> Conflicts also have potential consequences for a country's RTAs with other countries or regions. Conflict or disputes may disrupt a country's ability to fulfill its obligations under an RTA or its dispute with one country may alienate its trading partners, thus, multiplying the costs of conflict. New York Times columnist and author Thomas Friedman calls this concept the "Golden Arches Theory of Conflict Prevention:" "no two countries that both had McDonalds had fought a war against each other since each got its McDonalds."<sup>41</sup>

Every rule has its exception; in this case, the Russia-Georgia and Israel-Lebanon conflicts, but Friedman's seemingly facetious notion continues to have purchase. Trading partners bring huge financial losses to their global industries when they go to war, and this fact will not be lost in the strategic discussions of conflict resolution.<sup>42</sup>

RTAs can also influence growth through technology transfers.<sup>43</sup> Trade increases productivity by providing access to a greater

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<sup>40</sup> Id.

<sup>41</sup> Thomas L. Friedman, *THE LEXUS AND THE OLIVE TREE* 239 (New York: Farrar Straus Giroux 2000).

<sup>42</sup> See also Richard N. Haass, *The Geopolitics of Golf*, *NEWSWEEK* Sept. 14, 2009, at 19.

<sup>43</sup> The World Bank, Report No. 34437, *Global Economic Prospects 2005: Trade, Regionalism, and Development* 64 (2005), <http://www-wds.worldbank.org> (search: "global economic prospects" and "regionalism") [hereinafter *GEP*].

and more advanced range of technologies.<sup>44</sup> By importing goods, which are either new or of a higher quality than existing products, a country can increase its productivity and can benefit from the research and development activities of the exporting country<sup>45</sup> without having to actually invest in the research and development. Therefore, signing RTAs with technological leaders can increase the productivity of a country by providing them access to technologies they would not otherwise possess.

### **C. RTAs Create a Level Playing Field**

Globalization has created an economic interdependence among countries. Emerging Market countries can no longer pursue economic growth and development by remaining aloof from the global trading system. Emerging market countries wish to develop trade relationships that are more easily achievable on a global scale.<sup>46</sup> Accession to the WTO takes years and is not an immediate solution to the problem of increasing an emerging market country's participation in trade.<sup>47</sup> RTAs involve a smaller number

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<sup>44</sup> Id.

<sup>45</sup> Id.

<sup>46</sup> See CB Report, *supra* note 24, at 19.

<sup>47</sup> Susan L. Sakmar, Globalization and Trade Initiatives in the Arab World: Historical Context, Progress to Date, and Prospects for the Future, 42 U.S.F. L. Rev. 919, 929 (2008).



of participants and interests, thereby reducing the costs of negotiation and making it easier to reach an agreement.<sup>48</sup>

Regionalism can also “level the playing field” for emerging market countries.<sup>49</sup> Countries more fully integrated into the global economy often show higher rates of economic growth; however, many emerging market countries have experienced low economic growth.<sup>50</sup> In addition, countries with better access to world markets have a higher per capita income as compared with countries with lesser access. RTAs provide emerging market countries an opportunity to access world markets and integrate into the global economy on at least a regional scale. This allows them to increase their rates of economic growth and per capita income.

In addition, a country’s communication and transport infrastructures and the quality of its institutions have a strong impact on the likelihood that the country will participate meaningfully in the global market. For example, African firms export less than their counterparts in other

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<sup>48</sup> Chris Brummer, *The Ties That Bind? Regionalism, Commercial Treaties, and the Future of Global Economic Integration*, 60 *Vand. L. Rev.* 1349, 1361 (2007).

<sup>49</sup> See Lin, *supra* note 33, at 33.

<sup>50</sup> *Id.*

regions because of governmental infrastructure needs and adverse geographical conditions.<sup>51</sup>

Moreover, the use of non-reciprocal preferences has grown over the past decade, especially among emerging market countries. Because firms in emerging market countries often need positive discrimination to compete in the global arena, non-reciprocal preferences can positively affect the commercial value to these firms.<sup>52</sup> RTAs have the ability to focus on the specific needs of the member countries. Small countries have an incentive to participate in RTAs because such blocs enable them to exert increased market power as a group.<sup>53</sup> In addition, it allows them market access.<sup>54</sup> RTAs provide a certain measure of insurance against future protectionist policies and an incentive against being left out of future agreements.<sup>55</sup> RTAs provide a stepping stone for emerging market countries to participate in the global arena on a wider basis.<sup>56</sup> For example, the Asian and Pacific countries formed the Asia-Pacific Economic Cooperation to counter NAFTA's protectionist effects.<sup>57</sup> The Southern Cone Common

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<sup>51</sup> *Id.*

<sup>52</sup> See CB Report, *supra* note 24, at 20.

<sup>53</sup> See Burfisher, *supra* note 7, at 14.

<sup>54</sup> See GEP, *supra* note 43, at 36.

<sup>55</sup> *Id.*

<sup>56</sup> See CB Report, *supra* note 24, at 20.

<sup>57</sup> See Nsour, *supra* note 14, at 365.

Market (MERCOSUR) among Argentina, Brazil, Paraguay, and Uruguay is another example of this response to other regional blocs.<sup>58</sup>

#### **D. RTAs Increase Liberalization**

RTAs provide flexibility in terms of their design and content.<sup>59</sup> Countries often have a number of non-economic considerations in approaching RTAs such as national security and regional stability.<sup>60</sup> RTAs in Latin American and the Caribbean have occurred for various reasons including economic complementarity, geographical proximity, and political affinity.<sup>61</sup> They can address issues on a regional level that multilateral agreements cannot, such as migration, energy, transit, water, customs, labor, and standards.<sup>62</sup> The specific problems related to each issue differ based upon the country and region. Therefore, it is not feasible for multilateral agreements to encompass each of these issues in a way that is favorable to all countries involved. It would make multilateral agreements far too complicated and cumbersome. RTAs provide a framework for making progress on these issues.<sup>63</sup> In addition, many governments are more familiar with the governments of neighboring countries and

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<sup>58</sup> *Id.*

<sup>59</sup> See Taylor, *supra* note 28 at 159.

<sup>60</sup> Jiangyu Wang, China's Regional Trade Agreements: The Law, Geopolitics, and Impact on the Multilateral Trading System, 8 S.Y.B.I.L. 119 (2004).

<sup>61</sup> See Wolff, *supra* note 16, at 124.

<sup>62</sup> See CB Report, *supra* note 24, at 37. D.

<sup>63</sup> *Id.*

RTAs provide a forum for promoting liberalization in a manner that is consistent with their national interests.<sup>64</sup> For example, MERCOSUR was established to decrease tensions between Brazil and Argentina.<sup>65</sup> "It also helped avert a coup in Paraguay following reaffirmation by the presidents of the MERCOSUR member countries that democracy was a condition for membership."<sup>66</sup> While MERCOSUR was established to become a customs union, it also provides member countries a platform to discuss other issues such as security and drug trafficking.<sup>67</sup>

Trade liberalization increases competition in domestic markets.<sup>68</sup> For some countries it is not politically feasible to open its internal market to trade from all countries.<sup>69</sup> Therefore, RTAs provide a stepping stone toward liberalization.<sup>70</sup> RTAs condition states for liberalization, while making states more amenable to true multilateral trade.<sup>71</sup> RTAs may also encourage countries to liberalize by presenting a non-member country with a "carrot" if

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<sup>64</sup> See Brummer, *supra* note 48, at 1357.

<sup>65</sup> See Brown, *supra* note 37, at 9.

<sup>66</sup> *Id.*

<sup>67</sup> *Id.* at 6.

<sup>68</sup> See GEP, *supra* note 43, at 67.

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*

<sup>71</sup> See Brummer, *supra* note 48, at 1360-61.

it liberalizes.<sup>72</sup> Under the “carrot” approach, RTAs can merge and expand to encompass more economies as a bridge to global trade.<sup>73</sup>

RTAs can increase liberalization through new trade rules in the area of market regulations and investment rules.<sup>74</sup> By eliminating internal barriers and creating larger internal markets, these new trade rules can raise the return on investments and create an incentive for members and third countries to invest.<sup>75</sup> Firms investing in the RTA countries can achieve economies of scale by serving a larger market of potential buyers, decrease their transaction costs, and if services are included, can benefit from more efficient telecommunications, financial, and other services.<sup>76</sup> New trade rules may also induce greater efficiency in transactions with the global economy. Investments to reach the local market may include utilizing lower cost production sites within the RTA to serve the wealthier customers.<sup>77</sup>

For example, one study done in 2004 showed that firms in the businesses of electronics, textiles, and autos moved their production to Mexico to serve the US market.<sup>78</sup>

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<sup>72</sup> John P. Byrley, *Regional Arrangements, the GATT, and the Quest for Free Trade*, 6 FLA. J. INT'L L. 323, 333 (1991).

<sup>73</sup> *Id.* at 334.

<sup>74</sup> See CB Report, *supra* note 24, at 23.

<sup>75</sup> See GEP, *supra* note 43, at 105.

<sup>76</sup> *Id.*

<sup>77</sup> *Id.* at 106.

<sup>78</sup> *Id.*

Some scholars argue that removal by RTAs of trade barriers among partners can create economies of scope at the individual firm level and economies of scale at the industry level.<sup>79</sup> Economies of scope and economies of scale allow for the increased rationalization of production, leading to the efficient use of resources and resulting in a greater volume of global trade.<sup>80</sup> This benefits members and non-members and the benefits which spill over to outsiders may outweigh the costs of the original trade diversion.<sup>81</sup>

Larger markets can increase competition between suppliers and take advantage of differing regional factor prices in order to increase productivity and cause more rapid growth.<sup>82</sup> Increased competition forces firms to develop more efficient methods of production and can decrease the cost of the product. Firms have an incentive to create goods that are cheaper and more improved than similar goods from similar firms, thereby benefitting the global welfare. This rapid growth attracts intra-bloc and extra-bloc investments.<sup>83</sup>

RTAs may also include new investment rules designed to increase market access, thereby creating an opportunity for investors and

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<sup>79</sup> See Byrley, *supra* note 72, at 332.

<sup>80</sup> *Id.*

<sup>81</sup> *Id.* at 333.

<sup>82</sup> See GEP, *supra* note 43, at 106.

<sup>83</sup> *Id.*

new investment.<sup>84</sup> These investor protections can include provisions against expropriation, nondiscrimination among all investors, independent arbitration and dispute settlement with eligibility for investor-state suits.<sup>85</sup> This provides firms and investors with confidence to invest in a country governed by an RTA and lower their risks because they know what legal protections they can expect to receive.

#### **IV. Negative Economic Effects of Regionalism**

##### **A. The Spaghetti Bowl Crisis**

Many scholars contend that the proliferation of RTAs has disrupted the equilibrium between multilateralism and regionalism established under the GATT. They argue that this disruption in equilibrium has caused world trade to become fragmented.<sup>86</sup> As of July 2010, WTO Members had notified 474 RTAs to GATT/WTO, 283 of which had entered into force.<sup>87</sup> It would appear that RTAs have become the norm and may not necessarily complement the global regional trading system.<sup>88</sup> They may undermine the purpose of the WTO, which is to help trade flow as freely as possible by removing obstacles and providing

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<sup>84</sup> *Id.*

<sup>85</sup> *Id.*

<sup>86</sup> See Cho, *supra* note 22, at 40.

<sup>87</sup> World Trade Organization: Regional Trade Agreements, available at [http://www.wto.org/english/tratop\\_e/region\\_e/region\\_e.htm](http://www.wto.org/english/tratop_e/region_e/region_e.htm)

<sup>88</sup> See Cho, *supra* note 22, at 41-2.

predictability and transparency.<sup>89</sup> Scholar L. Alan Winters has likened RTAs to street gangs and has said "you may not like them, but if they are in the neighborhood, it is safer to be in one".<sup>90</sup>

In addition, RTAs can create a downward spiral. Some scholars argue that regional trade partners have a tendency to negotiate as a bloc in multilateral trade talks, as opposed to individual nations.<sup>91</sup> This forces other nations to develop RTAs of their own or else they risk losing bargaining power.<sup>92</sup> This leads to the creation of further RTAs, rather than true trade liberalization.

Noted economist and trade liberalization advocate, Jagdish Baghwati, of Columbia University argues that RTAs result in trade diversion and create what he terms the spaghetti bowl crisis.<sup>93</sup> The spaghetti bowl is comprised of customs unions, regional and bilateral free trade areas, common markets, preferences, and miscellaneous trade deals.<sup>94</sup> Every country negotiates different trading terms in each RTA with a different country with their own exceptions, loopholes, and regulations,

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<sup>89</sup> World Trade Organization: What Is the World Trade Organization, available at [http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/fact1\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact1_e.htm).

<sup>90</sup> Stephen Walsh. *Addressing the Abuse of the WTO's Exemption for Regional Trade Agreements*.73 (2004); at [http://www.elsa.org/fileadmin/user\\_upload/elsa\\_international/PDF/SPEL/SPEL04\\_1\\_WALSH.pdf](http://www.elsa.org/fileadmin/user_upload/elsa_international/PDF/SPEL/SPEL04_1_WALSH.pdf).

<sup>91</sup> See Byrley, *supra* note 72, at 334.

<sup>92</sup> *Id.*

<sup>93</sup> Christopher M. Bruner, *Hemispheric Integration and the Politics of Regionalism: The Free Trade Area of the Americas (FTAA)*, 33 U. MIAMI INTER-AM. L. REV. 1, 63 (2002).

<sup>94</sup> *Id.*



turning global trade into a hodge-podge of dissimilar agreements.<sup>95</sup>

The global trade system is now characterized by a crisscrossing of preferences, with different trade barriers applying to products depending on the origin of the product.<sup>96</sup> The spaghetti bowl has resulted in the Most-favored Nation principle being superseded by what some scholars term the Least-favored Nation principle.<sup>97</sup> MFN is the cornerstone of the GATT/WTO system and is a commitment of nondiscrimination whereby each WTO Member treats every other Member country equally.<sup>98</sup> RTAs facilitate intra-bloc trade, but impede global trade by providing barriers to extra-bloc trade and causing dissociation of the bloc from the rest of the world because of the preferential nature of its RTA.<sup>99</sup>

RTAs, by their very nature, lower duties and taxes for their members; however, they preserve or raise tariff barriers for the rest of the world.<sup>100</sup> For example, the U.S. agreement with the Dominican Republic and five Central American countries, the DR-CAFTA-US Agreement eliminates more than 80% of tariffs on

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<sup>95</sup> Council on Foreign Relations, *CFR's Jagdish Bhagwati Argues Against Preferential Trade Agreements in New Book; Recommends Completion of Multilateral Doha Round* (2008), <http://www.cfr.org/publication/16798/cfrs>.

<sup>96</sup> Jagdish Bhagwati, *Reshaping the WTO* (2005), available at <http://docs.google.com/gview?a=v&q=cache%3AJhLJsYFeauYJ%3Awww.columbia.edu%2F%7Ejb38%2FFEER%2520Final%2520Edited%2520by%2520Restall%2520and%2520Bhagwati.pdf+jagdish+bhagwati+spaghetti+bowl&hl=en&pli=1>.

<sup>97</sup> See Cho, *supra* note 22, at 42.

<sup>98</sup> See Koehnke, *supra* note 30, at 70.

<sup>99</sup> See Cho, *supra* note 22, at 42.

<sup>100</sup> See Brummer, *supra* note 48, at 1391.

industrial goods traded between the member countries.<sup>101</sup> In addition, intra-trade liberalization may be limited because certain sectors may be insulated from open trade, and thus excluded from coverage under the RTA or protected by rules of origin.<sup>102</sup>

## B. RTAs Create Market Confusion

RTAs can create confusion in the global trading arena because multiple preferential rates are being applied to various trading partners.<sup>103</sup> These differing rates often apply within schemes that have different timelines for reaching the preferential rates. The different RTAs may also be inconsistent and complex, making it difficult and costly to administer the schemes.<sup>104</sup> For example, tariffs on U.S.-Mexico trade were not fully eliminated until some 15 years after NAFTA's entry into force, while most tariffs were reduced to zero upon the agreement's entry into force on January 1, 2003. Other tariffs were cut at five-, ten-, or fifteen-year intervals.<sup>105</sup> Multiply the confusion engendered by this panoply of tariff changes on hundreds of traded products by the hundreds of RTAs facing exporters and the conundrum facing traders in the global market becomes clearer.

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<sup>101</sup> Christina Laun, *The Central American Free Trade Agreement and the Decline of U.S. Manufacturing*, 1 *IND. INT'L & COMP. L. REV.* 431, 435 (2007).

<sup>102</sup> See Cho, *supra* note 22, at 42.

<sup>103</sup> See CB Report, *supra* note 24, at 22.

<sup>104</sup> *Id.* B.

<sup>105</sup> See NAFTA, *supra* note 11, at arts. 302; see also *id.* at Annex 302.2, § 3.

Some scholars contend that these differences in border rules increase transaction costs involved with trading in the global arena.<sup>106</sup> These costs can be particularly burdensome for small corporations and firms, and therefore for Emerging Market countries because they are added to the formal costs of administering preferences and the potential for informal costs.<sup>107</sup> These costs must be considered when determining the usefulness of RTAs. Because these costs may be too great to permit an adequate focus on the multilateral arena<sup>108</sup>, this can cause a diversion of resources from multilateral trading agreements. Trade negotiators in Emerging Market countries are often incapable of concentrating on more than one trading negotiation at a time.<sup>109</sup>

RTAs can make it more difficult to achieve multilateral liberalization because they create a complex network of trade regimes which diminish predictability and transparency.<sup>110</sup> Contrast this result with that of the absence of discriminatory policies and taxes on imports, which maximizes competition

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<sup>106</sup> See CB Report, *supra* note 24, at 22.

<sup>107</sup> *Id.*

<sup>108</sup> *Id.* at 23.

<sup>109</sup> *Id.*

<sup>110</sup> *Id.*

world-wide and makes it possible for consumers to enjoy optimal prices and the efficient allocation of resources.<sup>111</sup>

Some scholars argue that major powers, like the United States, benefit from intra-bloc trade in a highly disproportionate manner and are able to use RTAs to gain superior terms in negotiations with less powerful states.<sup>112</sup> In this view, RTAs provide the United States a forum to export its domestic legal rules and norms into the global arena.<sup>113</sup> Because the United States is a dominant economic player, they have little difficulty in furthering their interests in the agreement and thus, the agreements could be considered business contracts.<sup>114</sup> These RTAs are negotiated from positions based on extreme power disequilibrium, thereby enforcing the disequilibrium between the dominant and less dominant countries.<sup>115</sup> Because RTAs can exploit Emerging Market countries through unequal provisions, RTAs can exacerbate the developmental differences between the developed and Emerging Market countries. RTAs may also aggravate the developmental disparity of countries because of the uneven distribution of benefits from free trade.<sup>116</sup>

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<sup>111</sup> See Brummer, *supra* note 48, at 1355.

<sup>112</sup> See Cho, *supra* note 29, at 432-3.

<sup>113</sup> Mark B. Baker, No Country Left Behind: The Exporting of U.S. Legal Norms Under the Guise of Economic Integration, 19 EMORY INT'L L. REV. 1321, 1324 (2005).

<sup>114</sup> *Id.*

<sup>115</sup> *Id.* at 1330.

<sup>116</sup> See Cho, *supra* note 22, at 70.

Members of large blocs can enhance their economic wellbeing through internal integration and the resulting economies of scale; however, the exports of non-member states may be threatened by the gains made by larger bloc members.<sup>117</sup> In addition, even though RTA members may enjoy positive benefits from the RTA, they do not benefit equally.<sup>118</sup> RTAs generally produce winners and losers.<sup>119</sup> For example, if two countries with different levels of domestic infrastructure enter into a RTA, the country with the superior infrastructure will attract more industrial activities.<sup>120</sup> This causes an uneven spread of economic activities, which will only increase.<sup>121</sup>

Another form of this is called “hub and spoke” regionalism, in which the economically powerful “hub” country establishes bilateral trade agreements with economically inferior “spoke” countries.<sup>122</sup> The hub benefits disproportionately because it has access to agreements with multiple spokes and often enjoy economies of scale which spokes do not.<sup>123</sup>

### C. RTAs Create Regulatory Failure

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<sup>117</sup> Id.

<sup>118</sup> See Brummer, *supra* note 48, at 1390.

<sup>119</sup> Souleymane Coulibaly, *On the Complementarity of Regional and Global Trade* (2008), available at <http://siteresources.worldbank.org/INTWDR2009/Resources/4231006-1204741572978/Coulibaly.pdf>.

<sup>120</sup> Id.

<sup>121</sup> Id.

<sup>122</sup> See Cho, *supra* note 29, at 432.

<sup>123</sup> Id.

RTAs can also create regulatory failure.<sup>124</sup> Recently, RTAs have been designed to cover more than just the liberalization of tariffs and quotas.<sup>125</sup> They contain chapters involving social regulations such as labor, the environment, and human health.<sup>126</sup> However, many social charters contained within RTAs are often inconsistent with WTO norms,<sup>127</sup> thereby undermining efforts to establish a regulatory norm on a multilateral basis. Some bilateral agreements have diluted multilateral disciplines on public health because they include provisions on trade and intellectual property rights.<sup>128</sup> The US-Jordan RTA includes provisions linking trade and labor.<sup>129</sup> This may be inconsistent with the regulatory consensus achieved by WTO members through the International Labor Organization.<sup>130</sup>

In addition, the US-Jordan RTA explicitly overrides the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) by stating that any marketing approval of pharmaceutical products should be in conformity with the RTA and not TRIPS.<sup>131</sup> This undermines the WTO's multilateral consensus on the subject. Such inconsistency with WTO policies and rules

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<sup>124</sup> See Cho, *supra* note 22, at 42.

<sup>125</sup> See GEP, *supra* note 43, at 35.

<sup>126</sup> See Cho, *supra* note 22, at 67. For example, the US-Singapore FTA and the Japan-Singapore Economic Agreement for a New Age Partnership contain environmental provisions. See CB Report, *supra* note 24, at 37.

<sup>127</sup> *Id.* at 42.

<sup>128</sup> *Id.*

<sup>129</sup> *Id.* at 69.

<sup>130</sup> *Id.*

<sup>131</sup> *Id.*

impedes global regulatory harmonization for the benefit of companies engaged in the international market.<sup>132</sup> For example, the text of NAFTA does not resolve the issue of the relationship between NAFTA and the WTO.<sup>133</sup> NAFTA states that in the event of an inconsistency or conflict with another agreement, NAFTA prevails unless otherwise provided.<sup>134</sup> This results in a diversion of resources, political capital, public attention, and other resources from the multilateral process.<sup>135</sup> These resources are already scarce in emerging market countries which cannot afford their diversion. The more time an emerging market country spends on RTAs, the less time the country has to employ these resources in pursuit of multilateralism.

Multiple regulations involving the same subject confuse the issues on a global scale and can increase transaction costs for global businesses.<sup>136</sup> Producers in non-member countries have to bear additional compliance costs when it exports goods to RTA countries with disparate regulations.<sup>137</sup> In addition, these trade barriers may entirely block products from non-member countries if the products do not conform to the RTA.s unique rules.<sup>138</sup> Firms often produce goods based on a particular method;

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<sup>132</sup> *Id.*

<sup>133</sup> *See* NAFTA, *supra* note 11, art. 103(2), 32 I.L.M. at 297.

<sup>134</sup> *Id.*

<sup>135</sup> *See* Cho, *supra* note 22, at 69.

<sup>136</sup> *Id.*

<sup>137</sup> *Id.*

<sup>138</sup> *Id.*

manufacturing the product by a different method that conforms to one particular RTA's regulations could prove costly. Therefore, multiple regulations only serve to hinder global trade and undermine multilateral harmonization of regulatory issues.

#### **D. FTAs Divert Trade**

Economists generally believe that RTAs are inferior to multilateral agreements when it comes to trade creation.<sup>139</sup> Countries excluded from RTAs almost always lose because member states have preferred access to the markets of included countries, thereby reducing the demand for exports of excluded states into the markets of the RTA.<sup>140</sup>

According to Professor Harrison of the University of Central Florida, because of the trade diversion effects on both included and excluded countries, multilateral trade liberalization provides larger gains to the world than an elaborate network of RTAs.<sup>141</sup> The RTAs studied in the article only produced small gains or losses to the world.<sup>142</sup> RTAs are obstacles because they decrease the aggregate global welfare by competing with non-member countries and other RTAs to increase the tariffs against

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<sup>139</sup> *Id.* at 62.

<sup>140</sup> Glenn W. Harrison *et al.*, *Rules of Thumb for Evaluating Preferential Trading Arrangements: Evidence from Computable General Equilibrium Assessments 2* (2003), available at <http://www-wds.worldbank.org/> (search: "Harrison" and "rule").

<sup>141</sup> *Id.*

<sup>142</sup> *Id.* at 3.



other blocs to shift the terms of trade in each bloc's favor.<sup>143</sup> The global welfare is diminished because RTA member products are protected, regardless of whether they are of equal quality of non-member products or even equal efficiency.<sup>144</sup> Protecting infant industries against imports tends to be indiscriminate and creates incentives for infant producers to remain inefficient and continue demanding protections which become politically difficult to remove.<sup>145</sup> These infant industries never learn, grow or develop.<sup>146</sup> Some scholars argue that poor countries, infant industries need a certain measure of protection in order to grow.<sup>147</sup> However, India managed to develop industries such as shipping, steel and textiles without protection.<sup>148</sup>

Discriminatory trade barriers contained within RTAs may cause sales by member countries to displace sales from more efficient countries, which deny producers and consumers access to superior quality and lower cost goods.<sup>149</sup> According to a study on MERCOSUR's trade impact by Yeats, principal economist at the World Bank, he noted that RTA members often trade in goods in

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<sup>143</sup> See Cho, *supra* note 29, at 430.

<sup>144</sup> *Id.*

<sup>145</sup> See Bhagwati, *supra* note 95.

<sup>146</sup> *Id.*

<sup>147</sup> *Id.*

<sup>148</sup> *Id.*

<sup>149</sup> Caroline Freund and Emanuel Ornelas, Policy Research Working Paper 5314, *Regional Trade Agreements 5* (May 2010), available at [http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2010/05/19/000158349\\_20100519101328/Rendered/PDF/WPS5314.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2010/05/19/000158349_20100519101328/Rendered/PDF/WPS5314.pdf)

which they have no comparative advantage.<sup>150</sup> This impacts both members and non-members. The study determined that MERCOSUR is becoming less competitive internationally in products where trade is re-orienting towards the region.<sup>151</sup> Yeats suggests that MERCOSUR's own trade barriers are the problem because certain goods are protected by higher than average discriminatory trade barriers, providing local producers an incentive to seek the higher prices which are available on the sale of the products to MERCOSUR markets.<sup>152</sup> By diverting exports from more competitive foreign markets, its comparative advantage decreases in products which are growing fast in the intra-trade market and it reduces the ability of non-member countries to export goods to MERCOSUR members.<sup>153</sup>

In addition, intra-trade liberalization may be limited because certain sectors may be insulated from open trade by being excluded from coverage under the RTA or protected by rules of origin.<sup>154</sup> RTAs may provide a global loss to welfare by excluding major products from its coverage.<sup>155</sup> RTAs generally do not address the tariff peaks in major products or provide a

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<sup>150</sup> Alexander J. Yeats, *Does MERCOSUR's Trade Performance Raise Concerns about the Effects of Regional Trade Arrangements?* 1 (1998), <http://www-wds.worldbank.org/>(search "Yeats" and "MERCOSUR").

<sup>151</sup> *Id.* at 18.

<sup>152</sup> *Id.*

<sup>153</sup> *Id.* at 30.

<sup>154</sup> *Id.*

<sup>155</sup> See Cho, *supra* note 22, at 62.

comprehensive means for liberalizing the products.<sup>156</sup> For example, under the E.C., trade creation outweighs trade diversion in the manufactured products; however, under its common agricultural policy, European farmers are sheltered from foreign competition.<sup>157</sup> In addition, the U.S. and other developing country preferences exclude commodities which are linked to U.S. domestic support programs, including processed foods with sugar and dairy content, such as confectionary items.<sup>158</sup> Therefore, its benefits might be outweighed by the trade it diverts.

RTAs also provide an opportunity for local interest groups to manipulate the design and operation of RTAs, which can distort the efficient flow of interstate commerce. For example, some RTAs utilize rules of origin matrices which safeguard "originating goods" from member countries with preferential treatment.<sup>159</sup> Rules of origin are a reference to domestic regulations which determine an imported goods country of origin.<sup>160</sup> For example, Mexican apparel can only receive tariff-free treatment within NAFTA only if it is produced with North American yarn and textiles.<sup>161</sup> In addition, CAFTA eliminates

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<sup>156</sup> *Id.*

<sup>157</sup> *Id.* at 63.

<sup>158</sup> See Burfisher, *supra* note 7, at 16.

<sup>159</sup> See Cho, *supra* note 29, at 430.

<sup>160</sup> See Freund, *supra* note 149, at 4.

<sup>161</sup> See Nsour, *supra* note 14, at 366.

tariffs and quotas on apparel and textiles if the countries meet CAFTA's provisions on the rules of origin and gives duty free benefits to some apparel made in Central America if it contains certain fabrics from NAFTA partners Canada and Mexico.<sup>162</sup> Rules of origin are inherent in RTAs because RTAs by their very nature provide preferential treatment to goods from a member state. These rules also negatively affect international commerce by discriminating against non-member states.<sup>163</sup> Therefore, RTAs may be seen as institutionalizing protectionism.<sup>164</sup> The benefits created by increasing intra-bloc trade may be outweighed by the bloc in trade they may cause.<sup>165</sup> In addition, it can be extremely difficult to determine a product's country of origin given that several countries may be involved in the manufacturing process of one good.<sup>166</sup> These rules can be extremely burdensome and complicated and therefore impose large transaction costs and burdens to the businesses and firms manufacturing these goods.<sup>167</sup> For example, NAFTA has rules to ensure that exporters, importers and manufacturers comply with the certificate of origin requirements.<sup>168</sup> All three parties must maintain records relating

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<sup>162</sup> See Laun, *supra* note, at 101.

<sup>163</sup> See Cho, *supra* note 29, at 431.

<sup>164</sup> See Cho, *supra* note 22, at 42.

<sup>165</sup> *Id.*

<sup>166</sup> *Id.*

<sup>167</sup> See Freund, *supra* note 149, at 36.

<sup>168</sup> William W. Kovatch, Jr., The NAFTA's Rules of Origin, Certificate of Origin, and Record-Keeping Requirements: The Disadvantage to Small Businesses, 12 *Transnat'l Law.* 403, 414 (1999).

to the good's origin for a period of five years.<sup>169</sup> NAFTA parties are allowed to verify the origin of goods through questionnaires or visits.<sup>170</sup> Firms face an additional cost to establish procedures to ensure compliance with NAFTA's certificate of origin and record-keeping requirements.<sup>171</sup> It also requires an expert to be trained or hired to determine compliance with NAFTA's rules of origin and various classification rules.<sup>172</sup> All of this can be quite costly and detrimental to some businesses.

## **V. Conclusions**

RTAs have become a common feature in the global trade arena. In determining their utility it is important to employ theories both economic and political that take into account the nuances of the new regionalism. Whereas old regionalism RTAs were usually single-objective pacts to increase trade or security, New regionalism results in multi dimensional comprehensive societal agreements. These differences must be considered when evaluating their efficacy. The trend in the last decade has been the growth and utilization of RTAs and this trend is unlikely to reverse itself. In fact, we are likely to see the number of RTAs increase dramatically as emerging market

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<sup>169</sup> *Id.*

<sup>170</sup> *Id.*

<sup>171</sup> *Id.* at 415.

<sup>172</sup> *Id.* VI.

countries seek more promising entrée to the riches of the global market than they have enjoyed under the WTO/GATT system.

Developed and emerging market countries alike also have sought trade liberalization in regionalism in the face of repeated failure to reach closure in the Doha Round.

Therefore, it is simply not plausible to evaluate RTAs based solely on their trade creation and diversion aspects. It is important to take a more holistic view to determine not only their impact on trade, but also their impact on non-economic aspects such as human rights compliance<sup>173</sup> and conflict-decreasing abilities. Beyond the static effects of trade liberalization, new regionalism creates dynamic effects through trade interconnectedness and investment, such as transformation of production structures, economies of scale, greater levels of competition, and changes in company performance, which should also be taken into account. Moreover, regionalism can no longer be seen solely as an economic phenomenon; its political dimension must be considered as well. As the World Bank (2000) stresses: "Security, bargaining power, cooperation, and lock-in are probably the main political motors for regional integration. Sometimes these motives receive a veneer of economic

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<sup>173</sup> Powell & Pérez, *supra* note 2.

rationalization.”<sup>174</sup> This increasingly complex regionalism can be well evidenced in Latin America, where trade is intimately linked to political and geo-political aspects. Latin American regionalism finds itself in a critical moment where the dynamic composition of coalitions of power and the lack of social consensus within the different countries have created uncertainty.<sup>175</sup> Generally, open trade is considered an instrument that contributes to peace and security through the creation of economic ties and increased prosperity. Despite the fact that regional agreements tend to reduce conflict levels, and facilitate development cooperation—serving as a conflict prevention tool—trade also has been utilized to aggravate conflict levels. This is the case of the relationship between Colombia and both Venezuela and Ecuador. Even though Colombia, Venezuela, and Ecuador have long been commercial partners and members of the Andean Community (Colombia and Ecuador) and the G3 Group (Colombia and Venezuela), and despite their geographical proximity, trade among these countries has been diminished significantly as a result of political disagreements. This conflict has created a difficult financial situation for consumers and the productive sectors of these countries, deepening the economic crisis in which the world has been

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<sup>174</sup> TRADE BLOCS (World Bank 2000), quoted in Philippe De Lombaerde and Luis Jorge Garay, *The New Regionalism in Latin America and the Role of the US* 6, UNU-CRIS Occasional Papers O-2006/10, available at <http://www.cris.unu.edu/fileadmin/workingpapers/20060421120114.O-2006-10.pdf> (last visited Dec. 22, 2010).

<sup>175</sup> *Id.* at 13.

immersed these past three years. This case shows the profound link between trade and non-economic aspects and the manner in which trade can work in ways both to mollify conflicts between trade partners and as a mechanism to exacerbate the conflict through the cessation or interruption of trade between disputing countries.

However, two questions remain: (1) Does new regionalism support multilateralism or obstruct it? (2) Does new regionalism facilitate development for emerging market countries or thwart it? Because the WTO regulatory power since 1994 has embraced a wide variety of formerly-domestic issues such as consumer protection and environmental, labor, and food safety standards, many national governments have perceived the present situation as one of "sovereignty impairment" and this view has contributed to the stalemate in multilateral negotiations. As a result, regionalism has become a more viable forum where a reduced number of countries, perhaps with closer cultural, geographic, and occupational backgrounds are more likely to agree on those sensitive issues.<sup>176</sup> Although it could be said that regionalism has been negative in the sense that it has helped developed countries to spread their policies and strengthen their economic power at the expense of emerging

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<sup>176</sup> Brigid Gavin, *Reconciling Regionalism and Multilateralism Towards Multilevel Governance*, at 10, UNU-CRIS Occasional Papers, 0-2005/20, available at <http://www.cris.unu.edu/fileadmin/workingpapers/20051206104911.O-2005-20.pdf> (last visited Oct 23, 2009).



market countries, it is undeniable that regionalism has been indispensable for emerging market countries to benefit from the opportunity of gaining access to markets that they could not otherwise have entered.

Regionalism has been proposed as an effective answer to the challenges of global competition both in developed and developing countries, allowing them to participate in regional and global economies. Countries with better access to world markets and those more fully integrated into the global economy often show higher rates of economic growth and have a higher per capita income as compared with countries with lesser access.

New regionalism is outwardly-oriented and diverse in its geographical coverage, which contributes to more open and competitive economies because it encourages integral reforms at the national level and ultimately at the multilateral level. Consequently, if RTAs attain a broader scale and regionalism continues to support internal reform processes and brings about greater geographic diversity connecting partners from different macro-regions of the world economy, new regionalism might become the appropriate tool to complement and activate multilateralism.<sup>177</sup> At a multilateral level, Article XXIV of the GATT, Article 5 of the GATS, and the Enabling Clause provide the

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<sup>177</sup> Pavel Hnát, Multilateralism and New Regionalism: Impacts on Global Economic Governance, at 7, University of Economics, Prague, available at <http://www.cceisaconf.uni.wroc.pl/wordy/papers%201%20session/hnat1.pdf> (last visited Jan. 18, 2011).

policy framework for a regional development scheme. These rules are under review in the Doha Round to determine if they take into consideration the development facet of RTAs. The Doha Round objective of lowering trade barriers throughout the world to allow countries to increase trade globally should be accompanied by definition of the fundamental criteria that would make RTAs development friendly.<sup>178</sup> The WTO provides for the concession of special rights to emerging market countries. These "special and different treatment" (SDT) provisions, which include longer time periods, special support, and lower levels of commitment to increase the integration of emerging market countries into international trade flows, allow emerging markets to be treated more favorably than other members.<sup>179</sup> Similarly, the enabling clause, officially called "Decision on differential and more favorable treatment, reciprocity and fuller participation for developing countries," is the legal basis for the Generalized System of Preferences (GSP) and also the legal basis for regional arrangements among emerging market countries.<sup>180</sup> Under the Enabling Clause, developed country WTO Members may give preferential trade concessions to this majority of WTO Members as an exception to the GATT's Most-favored Nation Clause. Thus,

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<sup>178</sup> *Id.*, at 6.

<sup>179</sup> Bob Deacon, Karel Van Hoestenbergh, Philippe De Lombaerde, and Maria Cristina Macovei, *Regional Integration, Decent Work, and Labour and Social Policies in West and Southern Africa*, at 14, UNU-CRIS Working Papers, W-2008/13, available at <http://www.cris.unu.edu/fileadmin/workingpapers/W-2008-13.pdf>.

<sup>180</sup> *Id.*

the mutual relation between regionalism and multilateralism should be seen as a matter of mutual consistency and complementarity.<sup>181</sup> As expressed in 2007 by the WTO Director General, Pascal Lamy, the future of the world trade order lies in "a strong and modern multilateral trading system coupled with RTAs which amplify rather than undermine its benefits. A strong multilateral trading system complemented - not substituted - by a new generation of regional trade agreements," which are thus like "pepper in the multilateral curry."<sup>182</sup>

Lamy's apparent comfort with the growth of RTAs reflects, in our view, not so much lack of concern with their adverse effects on multilateralism as recognition of the course of economic integration chosen by his employers, the WTO Members. In order to reconcile WTO regulation and regional agreements, the Doha Round must be able to define the principles that would allow emerging market countries effectively to exploit RTAs and to design a development strategy for their benefit while advancing multilateralism. Emerging market countries need to work toward a development strategy at different levels.<sup>183</sup> This strategy presupposes the existence, at a multilateral level, of market

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<sup>181</sup> See Hnat, *supra* note 177, at 5.

<sup>182</sup> *Id.* at 11.

<sup>183</sup> See Gavin, *supra* note 176, at 12.

access provisions that promote global trade, as well as regional integration that would also increase trade not only between rich and poor WTO Members but, most importantly, among the emerging market countries themselves.

Trade among emerging market countries has almost doubled over the past twenty years, and has expanded from trade mostly in commodities, agricultural products, to include trade in services.<sup>184</sup> As intra-regional and interregional trade grows, there will be a need for regional regulation that should be in accordance with clear multilateral rules of economic liberalization, which in turn might apply even where various levels of economic liberalization overlap, thereby solving the Spaghetti Bowl crisis.

We noted earlier that RTAs may not necessarily complement the global regional trading system.<sup>185</sup> With successful conclusion of the Doha Round stalled for many years and RTAs proliferating as fast as new leaves in the spring, some trade experts already bemoan the demise of the WTO.<sup>186</sup> At least half of world trade crosses borders without reference to MFN principles, the most basic of foundational GATT principles. Is modern trade multilateralism at an end a mere 60+ years after its birth?

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<sup>184</sup> *Id.*

<sup>185</sup> Text at note 89, *supra*.

<sup>186</sup> These final paragraphs originally appeared on Professor Powell's blog, <http://powell-on-just-trade.blogspot.com/2010/10/regional-trade-agreements-as-new-glue.html>.

Perhaps we underestimate the WTO's staying power. With the explosion of RTAs comes the exponential growth of the spaghetti bowl of inconsistent and sometimes inexplicable trade rules that confound exporters to more than one region and have eaten away at the basic premises of the multilateral trading system. In the near future, however, can we not expect these participants in the global market to demand some mechanism at minimum to compile these multifarious regulations into an easily searched location and at best to harmonize them to some standardized, business-friendly system? What other international organization is better equipped than the WTO to use its vaunted data-gathering skills to create the perfect web site to track, categorize, and explain each of the thousands of RTA rules? With every WTO Member a party to at least one and usually several RTAs, what better organization to engage its Members in the task of recommending harmonious "regional" trading rules that will return some semblance of predictability and order to the global market? What WTO Member, acting in its own interests, can possibly resist adapting its RTAs to these user-friendly standards? Can we expect that RTAs, operating under the WTO umbrella, will become the new glue of multilateralism?