

**THE LEGAL FRAMEWORK FOR KOREA'S  
REGIONAL TRADING ARRANGEMENTS**

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## Introduction

A challenge to any Regional Trade Agreement (RTA) is compliance with the international obligations of the international legal framework which constrains and shapes any economic cooperation among economic entities. Commentators have often focussed their analysis on the economic and political consequences of economic cooperation, largely ignoring the legal dimension of the inquiry. However, negotiations leading to the RTA will take place within the international legal framework which governs the relationships among the parties, and that framework will impose a certain structure and constraints on the parties. Perhaps the best known framework is that of the WTO.<sup>1</sup>

Korea is a member of the WTO, and therefore, in negotiating any RTA, must comply with its rules regarding the formation of any preferential trading arrangement. The WTO administers a number of agreements which regulate aspects of international trade including the General Agreement on Tariffs and Trade (GATT) and the General Agreement on Trade in Services (GATS). The “cornerstone” of the WTO framework is the MFN obligation which requires that there be no discrimination among trading partners. However, despite the fact that the aim is to do away with discrimination in international trade through the imposition of a general MFN obligation, the GATT and the GATS both have provisions which allow preferential trade to take place in certain circumstances. However, to ensure that these preferential trade areas comply with the primary objective of liberal trade, the rules impose several conditions on the creation of such trading areas. These provisions form the “legal framework”, with which such preferential trading areas must comply. However, the GATT framework is restricted to regulating trade relations, and the rules provided by the GATT are confined to regulating preferential trade in goods among participants. The GATT rules do not regulate other aspects of economic cooperation. The GATS provides rules for preferential trade in services, similar to those provided for trade in goods by the GATT, but these rules are confined to regulating preferential trade in services.

Modern economic relations have become increasingly complex. ‘... [T]rade policy is no longer [just] about trade measures at the border’.<sup>2</sup> A number of agreements go beyond the requirements of the GATT/GATS in providing for economic cooperation. A distinction is commonly made between shallow and deep integration: ‘shallow’ integration referring to the elimination of the traditional border measures, tariffs and non-tariff measures; ‘deep’ integration referring to policies that are beyond the border. These are sometimes referred to as “GATT +” (“WTO +”) agreements. As these agreements are frequently regional in nature, the broader term Regional Trading Arrangement (RTA) is often used to apply to these relationships.

One of the characteristics of recent regional trade agreements (RTAs) are (sic)

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<sup>1</sup>It must be emphasized that the role of the WTO is to establish the framework within which preferential trade unions are negotiated. The WTO does not negotiate such unions; negotiations for such unions will be conducted by the relevant government officials (usually trade officials) of the trading partners involved in such unions, who will represent their respective countries’ interests.

<sup>2</sup>M. R. Mendoza, P. Low, B. Kotschwar, eds, *Trade rules in the making : challenges in regional and multilateral negotiations* (Washington, D.C. : Organization of American States : Brookings Institution Press, 1999), at 1 (in ‘An Overview’ by editors).

their comprehensiveness. Not only do they cover the reduction or elimination of tariffs and other non-tariff barriers on the trade of goods and services, but they also cover broader elements such as investment rules, intellectual property rights and so on.<sup>3</sup>

“[A]most all of the deep integration features of recent RTAs are outside the WTO rules.”<sup>4</sup> To the extent that these activities are not regulated by an Agreement under the WTO or by some other international obligation, parties to an RTA are free to come to their own agreement for regulating these aspects of their relations. For example, most economic cooperation agreements also contain provisions regarding foreign direct investment. The GATT has very few provisions regulating investment, and these are limited to the “trade related” aspects of investment measures (TRIMs). The multilateral framework for the regulation of international investment is not very developed, so parties are much freer to come to their own arrangements in this area. Also, RTAs concentrate as much on trade facilitation (e.g., elimination of technical and regulatory obstacles) as on trade liberalisation. These are features not regulated by the WTO framework, and, to the extent that there are no other applicable international agreements, parties to an RTA are free to deal with these matters as they wish. To the extent that such measures only apply among parties to the RTA, they can be discriminatory.

The rising number of RTAs is increasing the risk of incoherent trade policy regulations being implemented through these special regimes, as well as discriminating among trade partners.

There is concern that the global rules-based system built on non-discrimination could give way to a complex web of differing regional and multilateral rules. Further, as the number of RTAs increases and overlap, the coexistence in a single country of different trade rules and provisions is a frequent feature. This lack of uniformity can severely hamper trade flows by the sheer fact of the costs involved for traders in meeting multiple sets of trade rules, and dealing with the many bureaucracies that are created. Many of these arrangements also include a dispute settlement mechanism. Thus, there is the potential for competing dispute settlement procedures.

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<sup>3</sup>A. Yanai, *Legal Frameworks for North-South RTAs under the WTO System*, IDE APEC Study Center Working Paper Series 03/04 – No. 6, (Japan: APEC Study Center Institute of Developing Economies, JETRO, March 2004), at 1.

<sup>4</sup>P. J. Lloyd, ‘Implications for the Multilateral Trading System of the New Preferential Trading Arrangements in the Asia-Pacific Region’, PECC Seminar on Developing Patterns of Regional Trading Arrangements in the Asia-Pacific Region: Issues and Implications, Vancouver, BC, Canada, 11-12 November 2002. Available at [http://www.pecc.org/publications/papers/trade-papers/1\\_SII/9-lloyd.pdf](http://www.pecc.org/publications/papers/trade-papers/1_SII/9-lloyd.pdf).

Faced with a maze of differing standards, rules of origin and dispute settlement procedures, business may simply opt to ignore the trading system — preferring no rules to the tangled web we are weaving... a maze of conflicting regional regulations, standards and rules of origin risk becoming the new “walls” between blocks.<sup>5</sup>

Many of the areas outside the scope of WTO regulation have been addressed by APEC. APEC can play a role in establishing a framework providing for uniformity in these areas. The APEC framework differs from the WTO framework in that, while the WTO framework is comprised of binding rules, the APEC framework is comprised of non-binding commitments - a “soft law” approach. These voluntary, non-binding commitments are elements of the framework for governing economic relations among APEC members,<sup>6</sup> and as Korea is a member of APEC, should be taken into consideration in the formation of Korean RTAs.<sup>7</sup>

Since 2003, Korea has actively engaged in FTA negotiations with over 50 countries, and has concluded arrangements with seven partners, five of which have entered into effect.<sup>8</sup> This is part of the proliferation of preferential trade agreements in the Asia-Pacific region, which has created what has been referred to as the Asian noodle bowl effect of FTAs<sup>9</sup>.

This paper will examine the role played by the international legal framework in regulating the formation of Korean RTAs. The following Part will first briefly discuss the Role of International Law in the governance of regional economic cooperation. Part 2 will then consider the “hard law” framework of the WTO, and Part 3 will consider the “soft law” framework of APEC.

## **Part 1. The Role of International Law in the governance of regional economic cooperation**

Good economic governance is essential to facilitate international economic activity. In theory, each state is free to regulate economic transactions which take place with it or within its boundaries as it pleases. However in practice, international economic relations are governed by an international framework which provides predictability or stability to a

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<sup>5</sup>WTO News: speeches — DG Mike Moore, “Globalizing Regionalism: A New Role for Mercosur in the Multilateral Trading System”, Buenos Aires, 28 November 2000.

<sup>6</sup>See discussion in Paul J. Davidson, “Rules-Based? APEC’s Role in the Evolving International Legal Framework for Regulating International Economic Relations”, paper presented at APEC Study Centre 2002 Conference, Merida, Mexico.

<sup>7</sup>The term “RTA” emphasizes the “trade” element of the agreement; a more accurate term might be Economic Cooperation Agreement (ECA), which would encompass other areas of economic cooperation, such as investment and movement of labour. The term “FTA” refers to an area of preferential trade in goods as defined in GATT Article XXIV (see *infra*). However, as the term FTA is commonly used to describe these broader agreements, this term will be used interchangeably with the others in this paper.

<sup>8</sup> See Ministry of Foreign Affairs & Trade, Republic of Korea, website: <http://www.mofat.go.kr/english/econtrade/fta/issues/index2.jsp> (accessed April 8, 2010).

<sup>9</sup> Masahiro Kawai and Ganeshan Wignaraja, “The Asian “Noodle Bowl”: Is It Serious for Business?”, ADBI Working Paper Series, No. 136, April 2009 (available at <http://www.adbi.org/files/2009.04.14.wp136.asian.noodle.bowl.serious.business.pdf> (accessed, April 19, 2010).

potential investment or trade situation. There has been a movement internationally to rules-based governance to regulate international economic relations. 'Rules-based' governance relies on structures and their functions, and involves the negotiation of rules to govern the cooperation among the actors, and the establishment of mechanisms to achieve compliance with the rules. In a rules-based system, rules define the extent to which obligations exist and between whom, and how redress is to occur. The aim of rules-based governance is predictability and efficiency.

A legal system is an essential component of a rules-based system of governance. A legal system provides 1) rules for the orderly interchange among members of a society, and 2) provides mechanisms for the settlement of disputes that arise among members of the society, concerning the rules established by that society, and for ensuring compliance with those rules.

Although a legal system is often thought of in terms of binding rules backed up by an enforcement mechanism, rules-based governance comprises a much broader spectrum. Rules may vary from binding obligations (so-called "hard law") to non-binding commitments ("soft law"); "enforcement mechanisms" may vary from "court systems" to "managerial approaches"<sup>10 11</sup>.

The international legal system is essential to international governance. The international legal framework for regulating international trade is most often thought of in terms of the GATT/WTO framework which has taken more of a "hard law" approach, with the negotiation of increasingly detailed trade rules, and its dispute settlement mechanism to resolve disputes over the interpretation/application of the rules. However, "soft law", such as APEC rules also plays a role in regulating economic relations.<sup>12</sup>

## **Part 2. "Hard Law" - the WTO**

### **The GATT rules for Custom Unions and Free Trade Areas**

Despite the fact that the aim of the GATT was to do away with discrimination in international trade through the imposition of a general MFN obligation, the GATT still allows preferential trade to take place in certain circumstances. Of most relevance to the formation of RTAs by Korea are the exceptions to the MFN requirement provided by Article XXIV, which provides an exception for customs unions, free trade areas, and interim agreements leading to them.

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<sup>10</sup> 'Managerial approaches suppose that states comply with rules in regulatory regimes out of enlightened self-interest and respond to non-coercive tools such as reporting and monitoring.' : Shelton, Dinah, 'Law, Non-Law and the Problem of "Soft Law"', Introduction in Shelton, Dinah, ed., *Commitment and Compliance: The Role of Non-Binding Norms in the International Legal System*, (Oxford and New York: Oxford University Press, 2000).

<sup>11</sup> See, e.g., Abbott, Keohane, *et al.*, 'The Concept of Legalization', (2000) 54 (3) *Intl Organization*, 401-419, and discussion in Paul J. Davidson, "The Role of Law in Governing Regionalism in Asia", Chapter 9 in Nicholas Thomas, ed., Governance and Regionalism in Asia (Oxon: Routledge, 2009).

<sup>12</sup> Paul J. Davidson, "The Role of Soft Law in The Governance of International Economic Relations in Asia", Volume 24 (2006) *Chinese (Taiwan) Yearbook of International Law and Affairs*, pp.1-18.

A Customs Union is defined in Article XXIV, paragraph 8(a):

(a) A customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that

(i) duties and other restrictive regulations of commerce ... are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and,

(ii) ... substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union.

A Free Trade Area is defined in Article XXIV, paragraph 8(b):

(b) A free-trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce ... are eliminated on substantially all the trade between the constituent territories in products originating in such territories.

One justification which is given for this exception to the rule of non-preferential trade is the argument that totally eliminating restrictions on trade among several customs territories creates a wider trading area and removes obstacles to competition, and thus makes possible a more economic allocation of resources which operates to increase production and raise standards of living within the trading area. Provided that the creation of such trading areas is not to the detriment of other customs territories' trade, this in turn enhances total world welfare which is the objective of the GATT system.

In order to ensure that customs unions and free trade areas meet the desired objectives, Article XXIV imposes several conditions on the creation of such trading areas. In particular, the arrangements should help trade flow more freely among the territories in the group without barriers being raised on trade with those outside the group. In other words, integration among trading parties should complement the multilateral trading system and not threaten it. The GATT rules provide criteria for the formation of customs unions and free trade areas to achieve these ends. The criteria are fundamentally three: (a) commitment to deep intra-region trade liberalization, (b) neutrality *vis-à-vis* non-parties' trade, and (c) transparency.

To meet the first criteria liberalization is required on "substantially all" the trade involved (as can be seen from the above definitions of a customs union and a free trade area). Parties are not free to grant preferential trade only in certain sectors.

Sub-paragraph 8(a)(i) of Article XXIV establishes the standard for the *internal trade* between constituent members in order to satisfy the definition of a "customs union". It requires the constituent members of a customs union to eliminate "duties and other restrictive regulations of commerce" with respect to "substantially all the trade" between them.

However,

Neither the GATT Contracting Parties nor the WTO Members have ever reached

an agreement on the interpretation of the term "substantially" in this provision. It is clear, though, that "substantially all the trade" is not the same as *all* the trade, and also that "substantially all the trade" is something considerably more than merely *some* of the trade. (Emphasis in original)<sup>13</sup>

It has been said that the question of what exactly is meant by “substantially all the trade” is notoriously imprecise.

GATT Article XXIV sets out a notoriously imprecise set of conditions under which free trade areas and customs unions are to be accepted as consistent with members’ obligations under the WTO Agreements. One of the most disputed elements is the phrase “substantially all trade” (SAT) which appears in the requirement that “duties and other restrictive regulations of commerce....are eliminated on substantially all the trade in products originating” in the partners.<sup>14</sup>

It is open to discussion whether the meaning of "substantially " should be interpreted quantitatively, qualitatively, or both.<sup>15</sup> There is no agreement among members, and in practice many agreements leave out large and sensitive areas such as agriculture and financial services. What is regarded as “substantially all” has changed over time.

since the conclusion of the first free-trade agreements in the 1950s and the negotiation of agreements now the gap between “substantially all” and “all” has narrowed considerably. Economies are now much more aware of the benefits of trade liberalisation, and on the whole they have become more ambitious. Coverage of about 70% of trade would have seemed reasonable to many in the 1960s. Today a widely accepted view is that an agreement covering less [than] 90% of trade is flawed. There is less agreement, however, on how this should be calculated.<sup>16</sup>

As regards neutrality, Article XXIV, paragraph 5 provides that the creation of a customs union or a free trade area should not lead to higher barriers to third country trade with the customs union or constituent territories of a free trade area:

5. ...the provisions of this Agreement shall not prevent, as between the territories of contracting parties, the formation of a customs union or of a free trade area or

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<sup>13</sup>World Trade Organization Appellate Body Report on Turkey - Textiles, WT/DS34/AB/R, 22 October 1999 para. 48.

<sup>14</sup>Robert Scollay and Roman Grynberg, ““Substantially All Trade”: Which Definitions Are Fulfilled in Practice? An Empirical Investigation”, A Report for the Commonwealth Secretariat, 15 August 2005, available at: [http://www.acp-eu-trade.org/library/files/Scollay-Grynberg\\_EN\\_150805\\_Commonwealth\\_Substantially-all-trade.pdf](http://www.acp-eu-trade.org/library/files/Scollay-Grynberg_EN_150805_Commonwealth_Substantially-all-trade.pdf) (accessed April 18, 2010).

<sup>15</sup>See, e.g., the discussion in Lo Chang-fa, On the Discretion and Limitations of Adopting Trade Remedies Provisions in RTAs”, paper presented at Asian International Economic Law (AIELN) Inaugural Conference, 30 June, 2009, available at: [http://aieln1.web.fc2.com/Lo\\_panel2.pdf](http://aieln1.web.fc2.com/Lo_panel2.pdf) (accessed April 18, 2010).

<sup>16</sup>Walter Goode, *Negotiating free-trade agreements: a guide*, (Canberra: Commonwealth of Australia, 2005), available on the website of the Australian Department of Foreign Affairs and Trade, [http://www.dfat.gov.au/publications/negotiating\\_ftas/negotiating\\_ftas.pdf](http://www.dfat.gov.au/publications/negotiating_ftas/negotiating_ftas.pdf) (accessed April 18, 2010).

the adoption of an interim agreement necessary for the formation of a customs union or free trade area; Provided that:

(a) with respect to a customs union, or an interim agreement leading to the formation of a customs union, the duties and other regulations of commerce imposed at the institution of any such union or interim agreement in respect of trade with contracting parties not parties to such union or agreement shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union or the adoption of such interim agreement, as the case may be;

(b) with respect to a free-trade area, or an interim agreement leading to the formation of a free-trade area, the duties and other regulations of commerce maintained in each of the constituent territories and applicable at the formation of such free-trade area or the adoption of such interim agreement to the trade of contracting parties not included in such area or not parties to such agreement shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the same constituent territories prior to the formation of the free-trade area, or interim agreement, as the case may be;

As regards transparency, Article XXIV, paragraph 7(a) requires any parties deciding to enter into a customs union or free trade area to notify other parties and provide them with details of the proposed arrangement. This would include plans and schedules for removing internal barriers and establishing common external barriers in the case of a customs union, within a reasonable time. Parties seek to obtain information on legal and procedural aspects of the implementation of the agreement, and on the economic/trade magnitudes involved, and to gauge the agreement's conformity *vis-à-vis* the relevant rules. In the GATT years, these examinations were conducted in individual working parties. On the 6<sup>th</sup> of February 1996, the WTO General Council created the Committee on Regional Trade Agreements<sup>17</sup>. Its two principal duties are to examine individual regional agreements; and to consider the systemic implications of the agreements for the multilateral trading system and the relationship between them. With regard to negotiations on procedural issues relating to RTAs, on 14 December 2006, the General Council of the WTO established, on a provisional basis, a new transparency mechanism for all RTAs.<sup>18</sup> This provides that:

Without prejudging the substance and the timing of the notification required under Article XXIV of the GATT 1994, ... nor affecting Members' rights and obligations under the WTO agreements in any way:

(a) Members participating in new negotiations aimed at the conclusion of an RTA shall endeavour to so inform the WTO.

(b) Members parties to a newly signed RTA shall convey to the WTO, in so far as

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<sup>17</sup>The CRTA's terms of reference can be found in WT/L/127. See the WTO Website: Regional Trade Agreements: Committee, Work of the Committee on Regional Trade Agreements (CRTA), <[http://www.wto.org/english/tratop\\_e/region\\_e/regcom\\_e.htm](http://www.wto.org/english/tratop_e/region_e/regcom_e.htm)> (accessed April 18, 2010).

<sup>18</sup>Transparency Mechanism for regional trade agreements, Decision of 14 December 2006, WT/L/671.



and when it is publicly available, information on the RTA, including its official name, scope and date of signature, any foreseen timetable for its entry into force or provisional application, relevant contact points and/or website addresses, and any other relevant unrestricted information.<sup>19</sup>

Upon notification, the RTA is to be considered by Members under the procedures established in the mechanism. Members may ask to have the proposal modified if they think it is inconsistent with the GATT or that it may damage their trading interests.

Article XXIV was discussed at the Uruguay Round and the parties signed an Understanding on the Interpretation of Article XXIV.<sup>20</sup> The text of this Understanding attempts to clarify and reinforce the criteria and procedures for the review of new or enlarged customs unions or free-trade areas and for the evaluation of their effects on third parties. The obligations of contracting parties in regard to measures taken by regional or local governments or authorities within their territories are also clarified. WTO Members have further agreed at the Doha Round of negotiations to initiate negotiations aimed at further clarifying and improving disciplines and procedures under the existing WTO provisions applying to regional trade agreements.<sup>21</sup>

There are controversies about the interpretation of the GATT provisions against which custom unions and free trade areas are assessed and questions about the effectiveness of the controls.<sup>22</sup> In only one case<sup>23</sup> was consensus reached in an examination of an agreement under Article XXIV provisions. However, this does not mean that the GATT has been ineffective in regulating the growth of preferential trading regions.

The GATT rules, however imperfectly observed, served as a model ... while they permitted the development of regional arrangements ... they have served to provide some measure of international supervision and control over the process. ... the existence of the GATT rules may be judged to have a restraining influence on members of regional trade groups.<sup>24</sup>

In fact the GATT has played an important role in this area of trade regulation. Many economic cooperation agreements contain a statement similar to that in the preamble to the Canada - US Free Trade Agreement (1989). Canada and the United States stated that they were “Resolved to build on their mutual rights and obligations under the General Agreement on Tariffs and Trade and other multilateral and bilateral instruments of cooperation”.

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<sup>19</sup>Article 1.

<sup>20</sup>Understanding on the Interpretation of Article XXIV of the General Agreement on Tariffs and Trade 1994.

<sup>21</sup>For information on the issues under discussion, see the Secretariat's study entitled Compendium of Issues related to Regional Trade Agreements TN/RL/W/8/Rev.1, 1 August 2002.

<sup>22</sup>“GATT Article XXIV has proven inadequate in several respects ... it never worked in a “legal” way because it lacked legal discipline.” - Sungjoon Cho, “Breaking the Barrier Between Regionalism and Multilateralism: A New Perspective on Trade Regionalism”, (2001) 42 Harv. Int'l L.J. 419, at 421.

<sup>23</sup>The customs union between the Czech Republic and the Slovak Republic after the breakup of Czechoslovakia.

<sup>24</sup>Frank Stone, Canada, the GATT and the International Trade System, (Montreal: The Institute for Research on Public Policy, 1984), p.79.

A major drawback to Article XXIV is that it was designed to address the formation, as opposed to the operation of unions. While the text of Article XXIV provides discipline for the establishment of groups, it is silent on important issues pertaining to operational relationships between customs unions or free trade areas and the GATT, or among such groupings after their formation.

A problem peculiar to a free trade area is that, in order to avoid the creation of a de facto customs union, members of a free trade area must ensure that the volume of trade that is freed among themselves is limited to products originating in their territories. If products from outside the area were to enjoy equal freedom of movement, then the independent tariffs of member states would be undermined by the lowest tariff in the area, as goods would simply be brought into the area through the lowest tariff point (assuming transportation costs within the area are not a significant factor). This problem is avoided by the inclusion of rules of origin in the agreement establishing the free trade area. Although the WTO Rules of Origin Agreement has certain requirements for WTO members as regards rules of origin, and aims for common (“harmonized”) rules of origin among all WTO members, it does not restrict rules of origin in preferential trade agreements. Countries setting up a free trade area are allowed to use different rules of origin for products traded under their free trade agreement.

### **The GATS rules for Trade in Services**

The above provisions only apply to preferential trade in goods, as the GATT only regulates trade in goods. Similar rules to allow integration with regard to services are included in the General Agreement on Trade in Services (GATS) which was concluded at the Uruguay Round. Prior to the GATS, services were not regulated by the international legal framework.

Article V of the GATS provides an exception to the MFN obligation of GATS for bilateral or plurilateral agreements to liberalise services trade - “economic integration agreements”. This Article is similar in structure and intent to Article XXIV of the GATT. Article V provides, in part:

This Agreement shall not prevent any of its Members from being a party to or entering into an agreement liberalizing trade in services between or among the parties to such an agreement, provided that such an agreement:

- (a) has substantial sectoral coverage<sup>25</sup>, and
- (b) provides for the absence or elimination of substantially all discrimination, in the sense of Article XVII, between or among the parties, in the sectors covered under subparagraph (a), through:
  - (i) elimination of existing discriminatory measures, and/or
  - (ii) prohibition of new or more discriminatory measures,either at the entry into force of that agreement or on the basis of a reasonable time-frame..

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<sup>25</sup> The requirement in GATS Article 5 for a “substantial sectoral coverage” and “elimination of substantially all discrimination” in services raises problems similar to those discussed above regarding the requirement of GATT Article 24 that a regional trade agreement should cover “substantially all the trade” in goods between its members.

Article V further provides that “in evaluating whether the conditions under paragraph 1(b) are met, consideration may be given to the relationship of the agreement to a wider process of economic integration or trade liberalization among the countries concerned.”<sup>26</sup>

Paragraph 7 of Article V requires Members which are parties to any agreement referred to in paragraph 1 to promptly notify any such agreement and any enlargement or any significant modification of that agreement to the Council for Trade in Services. The Transparency Mechanism for regional trade agreements<sup>27</sup> applies to such reviews, and WTO Members participating in new negotiations aimed at the conclusion of an RTA must endeavour to so inform The Committee on Regional Trade Agreements. Also, to ensure transparency, GATS Members are required to publish all measures of general application and establish national enquiry points mandated to respond to other Member's information requests on matters related to GATS obligations.<sup>28</sup>

The WTO rules for creating free-trade agreements for services follow the pattern developed for trade in goods, but with important differences. In relation to tariffs on goods, Article XXIV speaks of their elimination. It does not mention “reduction”. However, in the case of liberalizing trade in services, there is no mention of eliminating regulatory measures altogether. Instead, Article V requires the elimination of existing discriminatory measures and a prohibition of new or more discriminatory ones, i.e., national treatment is required. But the regulation itself can remain. In other words, this Article also recognises that governments have the right to regulate their economies.

### **Part 3. “Soft Law” - APEC**

As has been discussed above, a number of economic cooperation agreements go beyond the requirements of the WTO agreements in providing for economic cooperation. To the extent that these deal with activities that are not regulated by an agreement under the WTO or by some other international obligation, parties to them are free to come to their own agreement for regulating these aspects of their relations. However, new rules are needed to ensure that these new issues are also included within the multilateral framework, and do not become a form of discrimination or lead to incoherent trade policy regulations. A number of the areas of economic activity of concern in negotiating ‘modern’ economic arrangements, which are not regulated by the WTO or other international agreements, deal with contentious issues, which may be difficult to resolve by conventional “binding” agreements, but could be dealt with by a ‘softer’ approach. This brings us to consider the role of APEC.

*APEC plays a role in establishing a framework providing for uniformity in several of the areas not regulated by the WTO. The APEC framework differs from the WTO framework in that, while the WTO framework is comprised of binding rules the APEC framework is comprised of non-binding commitments. - a “soft” legal framework. From the beginning, APEC has advanced cooperation through voluntary, non-binding commitments (a “soft law” approach) rather than binding rules. These voluntary, non-binding commitments are elements of the framework for governing economic relations among APEC members.*<sup>29</sup> The

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<sup>26</sup>Article V, para. 2.

<sup>27</sup>*Supra.*

<sup>28</sup>GATS, Article III

<sup>29</sup>See discussion in Paul J. Davidson, “Rules-Based? APEC’s Role in the Evolving International Legal Framework for Regulating International Economic Relations”, paper presented at APEC Study Centre 2002 Conference, Merida, Mexico.

fact that “soft law” commitments are “non-binding” does not mean that they are complied with any less than “hard law”.<sup>30</sup> A soft law approach to governance may in fact offer a number of advantages.<sup>31</sup>

Although APEC’s approach is to formulate voluntary, non-binding principles, these form part of the international framework which regulates conduct among its members.<sup>32</sup> They have an effect on the evolving legal framework for economic cooperation in the region and will contribute to it. These commitments, while “non-binding”, are nevertheless intended to be statements of serious intent, and do have an effect on the conduct of APEC members.

Two elements of APEC’s voluntary framework which are particularly relevant to Economic Cooperation Agreements are the Non-Binding Investment Principles<sup>33</sup> and the agreement on a set of best practice principles for regional trade agreements and free trade agreements (APEC Model Measures for RTAs/FTAs<sup>34</sup>).

### The Non-Binding Investment Principles

While the WTO sets the legal framework for trade relations, it does not generally govern international investment (aside from the TRIMs Agreement and some provisions in the GATS). Very little exists in the form of an international legal framework to regulate this activity. The general rules of international law afford at present little protection to the private investor and although various attempts have been made to create an international investments code in the form of a multilateral convention, the signatories of which would undertake definite obligations protecting foreign private investment in their countries, these plans have not yet materialized in the form of an international convention.

Steps have been taken towards creating a more structured approach to investment liberalisation in the Asia Pacific region. The impetus was provided by the draft of a trade and investment framework agreement which was prepared by the United States and circulated to APEC members for consideration at the APEC Ministerial Meeting in Seattle in November, 1993. The draft dealt with measures to liberalise trade and investment rules to reduce protectionism and lower other kinds of trade impediments. At the meeting in Indonesia in November, 1994, APEC members agreed on a set of non-binding investment principles designed to remove obstacles to foreign investment.

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<sup>30</sup>Douglas M. Johnston, ‘Commitment and Compliance: The Role of Non-Binding Norms in the International Legal System,’ 95 *The American Journal of International Law* (2001), 710.

<sup>31</sup>Paul J. Davidson, “The Role of Soft Law in The Governance of International Economic Relations in Asia”, Volume 24 (2006) *Chinese (Taiwan) Yearbook of International Law and Affairs*, pp.1-18.

<sup>32</sup>See, Davidson, Paul J. “Rules-Based? - APEC’s Role in the Evolving International Legal Framework for Regulating International Economic Relations”, paper presented at the APEC Study Centre 2002 Conference, Merida, Mexico, 22-24 May, 2002.

<sup>33</sup>Reproduced in Paul J. Davidson, ed., *Trading Arrangements in the Pacific Rim*, looseleaf (New York: Oxford University Press, 1995-) [TAPR] at Document II.B.3.a.

<sup>34</sup>TAPR, Document III.AA.1.

The Non-binding Investment Principles (NBIP) of 1994<sup>35</sup> are principles for strengthening the efficiency of investment administration, eliminating investment obstacles, and establishing a free and open investment environment in the region. The NBIP are to be used as a guideline by members to achieve the APEC goal of free and open investment in the region, and may be a useful “tool” in the role of creating uniform investment provisions to be included in individual Economic Cooperation Agreements (ECAs). Although non-binding, APEC’s Non-Binding Investment Principles are thus an important component of the “soft law” framework for managing this area of economic cooperation.

#### APEC Model Measures for RTAs/FTAs

APEC Economic Leaders adopted a set of best-practice principles for free-trade and regional trade agreements at their meeting in Santiago on 20 and 21 November 2004. The APEC Best Practices for RTAs/FTAs.<sup>36</sup> are intended to achieve high standard agreements in the APEC region. Although not ‘binding’ on the APEC members, these guidelines are influential, and serve as a guide to some of the issues that need to be addressed by ‘new’ economic cooperation agreements, which are much broader in scope than provided for by the rules of the WTO.<sup>37</sup>

At their meeting in Jeju on 2 and 3 June 2005, APEC Ministers Responsible for Trade instructed Senior Officials to develop possible model measures on trade facilitation for RTAs/FTAs. The Model Measures build on the Best Practices for RTAs/FTAs adopted by APEC members in 2004. They are not exhaustive, but they are designed to help members give effect to the Best Practices by identifying RTA/FTA provisions that can facilitate trade and reduce transaction costs for business, bearing in mind the general APEC principle of voluntarism.

The APEC Ministers Responsible for Trade have stated,

A key aspect of [promoting high quality RTAs/FTAs] is the development of model measures for RTA/FTA chapters as capacity-building tools and non-binding references to assist APEC economies in achieving such comprehensive and high-quality agreements, and to promote greater consistency and coherence among the RTAs/FTAs within the region.<sup>38</sup>

In 2008 the Committee on Trade and Investment (CTI) completed its work on model measures by concluding five chapters, including a chapter on Customs Administration and Trade Facilitation that was developed by the APEC Business Advisory Council (ABAC).

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<sup>35</sup>See Appendix 2.

<sup>36</sup>Although the title only refers to RTAs/FTAs, this is expanded in the footnote to the title to “Regional Trade Arrangements (RTAs), Free Trade Agreements (FTAs), and other Preferential Arrangements”. (Emphasis added)

<sup>37</sup>The Best Practices have been included in Walter Goode, *Negotiating free-trade agreements: a guide*, (Canberra: Commonwealth of Australia, 2005) which has been prepared as a practical introduction to the negotiation of free-trade agreements, available on the website of the Australian Department of Foreign Affairs and Trade, [http://www.dfat.gov.au/publications/negotiating\\_ftas/negotiating\\_ftas.pdf](http://www.dfat.gov.au/publications/negotiating_ftas/negotiating_ftas.pdf) (accessed April 16, 2010).

<sup>38</sup>Meeting of APEC Ministers Responsible for Trade, Arequipa, Peru, 31 May - 1 June, 2008, Statement of the Chair.

This brings the total number of chapters to 15 plus a chapeau.<sup>39</sup>

The Chapeau states:

These model measures are ... intended to encourage a coherent and consistent approach to the design and content of [RTAs/FTAs].

The model measures reflect the general APEC principle of voluntarism. They are neither mandatory nor exhaustive....The model measures are indicative examples to provide members with useful reference in negotiating RTA/FTA chapters. They are a guide to the kind of provisions that might be included in a free-trade agreement.

While not binding, these model measures must nevertheless be given consideration by APEC Members entering into negotiations for a regional trading arrangement. Although a rules-based framework for regulating economic cooperation is often thought of from the perspective of a legal framework based in 'hard law', it is also important to consider the role of 'softer' legalization, through 'non-binding' commitments. 'Non-binding norms have a complex and potentially large impact in the development of international law.'<sup>40</sup>

## Conclusion

Good economic governance is essential to facilitate international economic activity. International law plays an important role in rules-based governance. International economic law provides the framework for regulating economic activity among the members of the international community, and provides the international legal framework for rules-based governance. Such a framework is necessary in order to promote increased order and predictability in international transactions. Nations create international rules and institutions to capture the gains available from cooperation. These institutions provide a framework for mutually beneficial decision-making and serve to guide and constrain behaviour.

*Although a legal system is often thought of in terms of binding rules backed up by an enforcement mechanism - "hard law", rules-based governance comprises a much broader spectrum. Rules may vary from binding obligations (so-called "hard law") to non-binding commitments ("soft law").* This paper has considered the legal framework that governs the formation of "regional trading arrangements" by Korea. As a member of both the WTO and APEC, Korea must consider both the "hard law" rules of the WTO and the "soft law" guidelines of APEC.

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<sup>39</sup>See Appendix 1 for a list of chapters, and see, Committee on Trade and Investment, 2008 Annual Report to Ministers, November 2008, Lima, Peru, Appendix 2, for the full text of the Model Measures, available at [http://publications.apec.org/publication-detail.php?pub\\_id=66](http://publications.apec.org/publication-detail.php?pub_id=66) (accessed April 16, 2010).

<sup>40</sup>Shelton, Dinah, 'Law, Non-Law and the Problem of "Soft Law"', Introduction in Shelton, Dinah, ed., *Commitment and Compliance: The Role of Non-Binding Norms in the International Legal System*, (Oxford and New York: Oxford University Press, 2000).

## **APPENDIX 1**

### *APEC Model Measures for RTAs/FTAs*

Safeguards (endorsed in 2008)

Competition Policy (endorsed in 2008)

Environment (endorsed in 2008)

Temporary Entry for Business Persons (endorsed in 2008)

Customs Administration and Trade Facilitation\* (endorsed in 2008)

Electronic Commerce (endorsed in 2007)

Rules of Origin and Origin Procedures (endorsed in 2007)

Sanitary and Phytosanitary Measures (endorsed in 2007)

Trade in goods (endorsed in 2006)

Technical barriers to trade (endorsed in 2006)

Transparency (endorsed in 2006)

Government procurement (endorsed in 2006)

Cooperation (endorsed in 2006)

Dispute Settlement (endorsed in 2006)

Trade facilitation (endorsed in 2005)

\* submitted by ABAC

(from Committee on Trade and Investment, 2008 Annual Report to Ministers, November 2008, Lima, Peru, Appendix 2)

## **APPENDIX 2**

### **APEC NON-BINDING INVESTMENT PRINCIPLES**

Jakarta, November 1994

In the spirit of APEC's underlying approach of open regionalism,

Recognising the importance of investment to economic development, the stimulation of growth, the creation of jobs and the flow of technology in the Asia-Pacific region,

Emphasising the importance of promoting domestic environments that are conducive to attracting foreign investment, such as stable growth with low inflation, adequate infrastructure, adequately developed human resources, and protection of intellectual property rights,

Reflecting that most APEC economies are both sources and recipients of foreign investment,

Aiming to increase investment including investment in small and medium enterprises, and to develop supporting industries,

Acknowledging the diversity in the level and pace of development of member economies as may be reflected in their investment regimes, and committed to ongoing efforts towards the improvement and further liberalisation of their investment regimes,

Without prejudice to applicable bilateral and multilateral treaties and other international instruments,

Recognising the importance of fully implementing the Uruguay Round TRIMs Agreement,

APEC members aspire to the following non-binding principles:

#### **Transparency**

\* Member economies will make all laws, regulations, administrative guidelines and policies pertaining to investment in their economies publicly available in a prompt, transparent and readily accessible manner.

#### **Non-discrimination between Source Economies**

\* Member economies will extend to investors from any economy treatment in relation to the establishment, expansion and operation of their investments that is no less favourable than that accorded to investors from any other economy in like situations, without prejudice to relevant international obligations and principles.

#### **National Treatment**

\* With exceptions as provided for in domestic laws, regulations and policies, member economies will accord to foreign investors in relation to the establishment, expansion, operation and protection of their investments, treatment no less favourable than that accorded in like situations to domestic investors.

#### **Investment Incentives**

\* Member economies will not relax health, safety, and environmental regulations as an



incentive to encourage foreign investment.

#### Performance Requirements

\* Member economies will minimise the use of performance requirements that distort or limit expansion of trade and investment.

#### Expropriation and Compensation

\* Member economies will not expropriate foreign investments or take measures that have a similar effect, except for a public purpose and on a non-discriminatory basis, in accordance with the laws of each economy and principles of international law and against the prompt payment of adequate and effective compensation.

#### Repatriation and Convertibility

\* Member economies will further liberalise towards the goal of the free and prompt transfer of funds related to foreign investment, such as profits, dividends, royalties, loan payments and liquidations, in freely convertible currency.

#### Settlement of Disputes

\* Member economies accept that disputes arising in connection with a foreign investment will be settled promptly through consultations and negotiations between the parties to the dispute or, failing this, through procedures for arbitration in accordance with members' international commitments or through other arbitration procedures acceptable to both parties.

#### Entry and Sojourn of Personnel

\* Member economies will permit the temporary entry and sojourn of key foreign technical and managerial personnel for the purpose of engaging in activities connected with foreign investment, subject to relevant laws and regulations.

#### Avoidance of Double Taxation

\* Member economies will endeavour to avoid double taxation related to foreign investment.

#### Investor Behaviour

\* Acceptance of foreign investment is facilitated when foreign investors abide by the host economy's laws, regulations, administrative guidelines and policies, just as domestic investors should.

#### Removal of Barriers to Capital Exports

\* Member economies accept that regulatory and institutional barriers to the outflow of investment will be minimised.