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ANALYSIS OF SOUTH-SOUTH COOPERATION IN TRADE

MERCOSUR in South-South Agreements: in the middle of two models of regionalism

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List of abbreviations

ACE	Economic Complementation Agreement
ACP	African, Caribbean and Pacific
ALADI/LAIA	Latin American Integration Association
ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Agreement
CACM	Central American Common Market
CAN/ACN	Andean Community of Nations
CET	Common External Tariff
CMC	Common Market Council
CRTA	Committee of Regional Trade Agreement
CTD	Committee on Trade and Development
CTG	Council for Trade in Goods
CTS	Council for Trade in Services
CU	Customs Union
ECLAC	Economic Commission for Latin America and the Caribbean
EIA	Economic Integration Area
EU	European Union
FAF	Family Agriculture Fund
FDI	Foreign Direct Investment
FOCEM/ FSCIS	Fund for Structural Convergence and Institutional Strengthening
FTA	Free Trade Area
GATS	General Agreement on Trade in Services
GATT	General Agreement on Trade and Tariffs
GDP	Gross Domestic Product
GSP	Generalized System of Preferences
GSTP	Global System of Trade Preferences
ISM	MERCOSUR Social Institute
LDC	Least Developed Countries
MERCOSUR	Southern Common Market
MFN	Most Favoured Nation
NAFTA	North American Free Trade Area
NAMA	Non-Agriculture Market Access
PTA	Preferential Trade Agreement
RTA	Regional Trade Agreement
S&D	Special and Differential Treatment
SACU	Southern African Customs Union
TRIMS	Agreement on Trade Related Investment Measures
TRIPS	Trade-Related Aspects of Intellectual Property Rights
UNCTAD	United Nations Conference for Trade and Development
UR	Uruguay Round
US/USA	United States of America
WTO	World Trade Organization

Introduction

The objective of this paper is to analyse the MERCOSUR as a case of a regional integration process in transition between different moments: the nineties' neoliberal moment (which concentrated solely on trade liberalisation) and the present neo-developmental phase, which now includes structural policies as a new pillar for integration. The pull of each contrasting mindset leads to tensions in both the internal and external agendas. In this analysis, we will focus on three specific issues: trade in services, investments, and asymmetries. All three have loomed large in the North-South agenda, but as regional agreements make progress and a new mindset emerges they now cast a shadow on South-South relations.

In the case of asymmetries, the internal agenda has shown significant changes towards the new regionalism mindset. In the external agenda, however, the treatment of asymmetries still does not reflect much coherence with the regional political context.

In the case of services and investments little progress was noted. As regards services, although MERCOSUR correctly adopted the GATS model, MERCOSUR negotiations have barely advanced. As far as investments are concerned, MERCOSUR does not yet have common rules, neither for intra-regional investments nor harmonized rules for extra-regional flows.

In the first and second parts, RTAs proliferation and their legal framework are analysed in order to provide a context for the following sections. In the third section, we deal with the legal framework for the management of asymmetries with the purpose of better understanding the dilemmas MERCOSUR has to face in its transition period. In the fourth part, we address the reconfiguration of regionalism in South America, and then proceed to assess the internal agenda of MERCOSUR in the case of services, investments and asymmetries in order to identify challenges the regional bloc faces in this regard. In the last part, we switch to the external agenda. We focus on trade relations between MERCOSUR and specific trade partners (India, SACU and Israel) to reveal a new set of challenges.

Both sets of challenges, those faced by the internal and the external agenda, stem from the tensions between the original neoliberal orientation and the new neo-developmentist mindset, which goes beyond trade as the sole policy for regional integration.

1. The Proliferation of Regional Trade Agreements: causes and consequences

RTAs involving two or more nations to reduce or eliminate barriers between or among countries, while maintaining barriers against imports from other nations, are not a new phenomenon. In fact, RTAs flourished in the first half of the twentieth century, with agreements among European, African and South American states, and a large number of agreements were forged between countries with colonial ties, such as the Commonwealth Preference.[1]

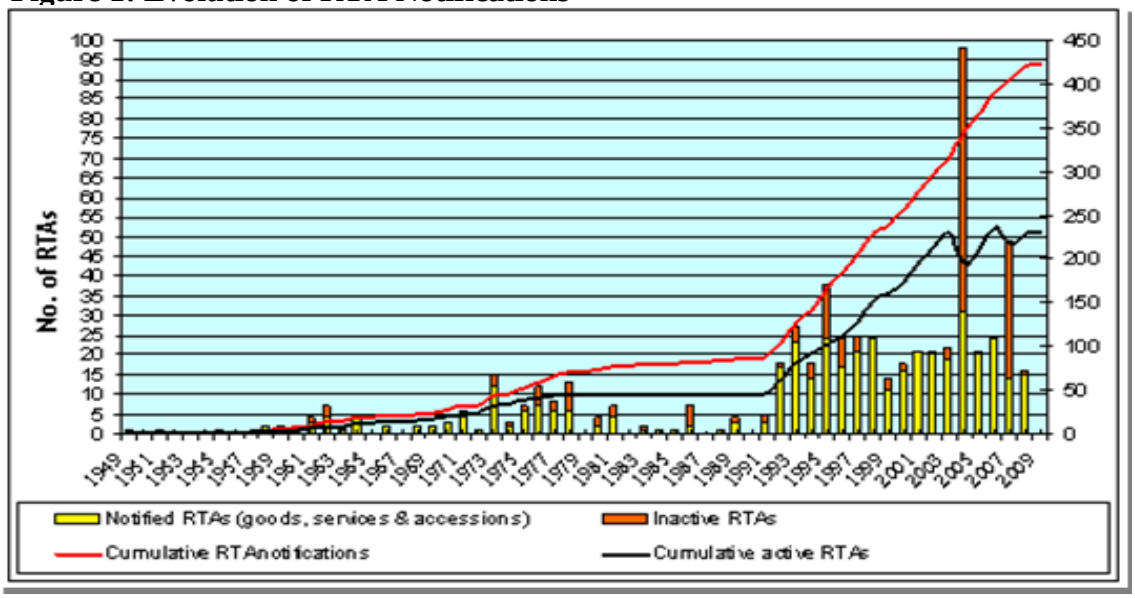
[1] The Commonwealth Preference, formerly known as Imperial Preference, was a proposed system of reciprocally-levelled tariffs or free trade agreements between different Dominions and Colonies within the British Commonwealth of Nations. For more details, see FRAM, N. (2006). "Decolonization, the Commonwealth and British Trade (1945-2004)". Stanford: Public Policy Forum.

During the negotiations of the General Agreement on Trade and Tariffs (GATT 47)[2], from 1944 to 1946, some agreements similar to RTAs were also under negotiation, such as the Benelux, which later became the embryo of the European Union.[3] The framers of the GATT felt therefore that it was necessary to allow room for preferential arrangements while imposing disciplines on the formation of RTAs. To deal with such situations, Article XXIV was incorporated in to the GATT.[4] This provision will be analysed in the following sections.

Up until the 1980s, regional and bilateral arrangements were extensively used in Western Europe among countries with close geographical proximity, in a great range of developing countries with close geographical proximity, and in the format of preferences granted between developed countries and from developed to developing countries. By the conclusion of the Uruguay Round, all but three WTO Members – Hong Kong, Korea and Japan – were party to at least one of the 62 RTAs in force.[5]

Since the establishment of the WTO, however, the number of RTAs has grown rapidly. During the GATT years, there were only 124 agreements notified.[6] The succeeding years have seen this number rise to 474 notifications, of which 285 are in force, as of August 2010.[7] More importantly, the rate at which RTAs are being negotiated has accelerated since the failed Seattle (1999) and Cancun (2003) Ministerials, as can be seen in Figure 1:

Figure 1: Evolution of RTA Notifications



Source: WTO (2010)

[2] Signed in Geneva on October, 30th, 1947.

[3] The Benelux is an economic union that comprises three neighbouring countries, Belgium, the Netherlands, and Luxembourg. In 1944, the three countries established the Benelux Customs Union, until being supplanted by the Benelux Economic Union in 1960. For more details, see Manin, P. (1997). *Les Communautés Européennes*. Paris: Pedone.

[4] Jackson, J.H. (1997). *The World Trading System: Law and Policy of International Economic Relations*. MIT Press.

[5] For more about the history of RTAs, see Lester, S. and Mercurio, B. (2008), *World Trade Law. Oxford: Hart.*

[6] See Fiorentino, R.; Verdeja, L. and Toqueboef, C. (2006). "The Changing Landscape of Regional Trade Agreements: 2006 Update". Discussion Paper no 12, Geneva: WTO.

[7] See WTO RTA Database in http://www.wto.org/english/tratop_e/region_e/region_e.htm. Access in 08/10/2010.

There are several reasons for the expansion of RTAs. First, RTAs liberalise trade between natural trading partners, thereby encouraging trade of goods and services, and stimulate investment in both developed and developing countries. Moreover, it has been argued that RTAs can be negotiated much faster than the multilateral process, enabling parties to liberalise more quickly than they would through multilateral consensus, in addition to addressing specific issues, such as investment, competition, labour standards, movement of natural persons, and others that have not yet been subject to multilateral agreements. From this perspective, the resulting achievements in trade liberalisation would substantially complement the WTO and could be seen as an important *building block* for future multilateral liberalisation.[8] On the other hand, it has also been sustained that the proliferation of RTAs would be a negative phenomenon for the multilateral scenario. RTAs would accordingly constitute *stumbling blocks* instead of *building blocks*. From a developing countries' standpoint, this subject is even more controversial.

The purpose of this section is to contextualise the current phenomenon of the expansion of RTAs in a multilateral trading system scenario and analyse the main arguments that are being presented by the international trade literature for the rise of RTAs. To this effect, first, we analyse some economic, geopolitical and institutional causes for such an expansion; second, we make an evaluation of the possible impacts of such proliferation of RTAs for the multilateral trading system and, finally, we examine their potential impacts on the developing countries.

1.1. Multilateral impasses and dissatisfactions

In the post Uruguay Round era, the concerns about the multilateral trading system have intensified. A number of WTO Members, particularly developing countries, are dissatisfied with the effects of world trade liberalisation. In this regard, the degree of liberalisation in the agriculture market has not met their expectations. Continuing subsidies provided by certain developed countries to their domestic farmers have been a major obstacle for certain developing countries to gain market access in the more advanced economies.[9] The concentration of wealth has increased: 20% of the world population is now in possession of more than 82% of world's GDP.[10] Additionally, crucial objectives listed in the preamble to the WTO Agreement, such as raising standards of living, ensuring full employment and promoting sustainable development, have not been achieved yet.

In turn, following the collapse of the WTO Ministerial Conferences in Seattle (1999) and Cancun (2003), several developed and high-income developing countries realized that protectionist elements in many countries were slowing the multilateral liberalisation process and that, in the current climate, their interests would be better

[8] Lester, S. and Mercurio, B. (2008). *Op. cit.*.

[9] World famine has even increased in numerous developing countries. See data available in FAO Annual Report "The State of Food and Agriculture 2009". In http://www.fao.org/docrep/012/i0680e/i0680e00.htm . Access in 08/08/2010. The subsidies granted by the U.S. government to its cotton producers is emblematic of the limited benefits brought so far by the WTO Agriculture Agreement.

[10] Data available in IMF Annual Report "World Economic Outlook Update July 2010". In http://www.imf.org/external/pubs/ft/weo/2010/update/02/index.htm Access on 08/08/2010.

served by bypassing the multilateral negotiations and instead focusing their attention on and pursuing their own initiatives in regional and bilateral RTAs.[11]

At the same time, due to the difficulties in negotiating direct investment issues in the WTO, these countries are also entering into many bilateral investment agreements (BITs). According to UNCTAD, in 2005, there were almost 2,500 BITs in force around the world.[12] BITs are seen by some trade experts as a major economic factor fostering the propagation of regionalism today. In view of the fact that some countries condition negotiations of RTAs on the existence of investment rules, BITs became a key element for trading states (both developed and developing countries) to gain preferential trade access to large regional markets.[13]

Currently, the big four RTAs (the EU, NAFTA, the MERCOSUR and the ASEAN) account for close to 65 % of the total export trade and 70% of the total import trade of the world.[14] In other words, the share of MFN regulated global trade is around a third. While it is not clear in the economic literature whether RTAs promote global trade integration or vice-versa, it is certain that this relation exists and it is increasingly turning into a strategic political decision for developed and developing countries.[15]

1.2. Economic advantages

To explain this rapid growth of RTAs since the 1990s, economists have tried to identify the reasons that are pushing countries towards regionalism – especially through the traditional explanation of the welfare effects of trade liberalisation and the consequent gains from trade at a regional level.

The traditional theory of gains from regional economic integration differentiates the concepts of trade creation and trade diversion to show the net effects of trade liberalisation on a regional basis.[16] Basically, RTAs can lead to trade creation if, due to the formation of the RTA, its members switch from inefficient domestic producers and import more from efficient producers from other members of the RTA. In theory, this situation generates welfare from production efficiency and consumption efficiency. On the other hand, trade diversion happens if, because of the RTA, members switch imports from low-cost production in the rest of the world and import more from higher-cost producers in the partner countries. In this case, on the

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[11] Pal, P. (2004). Regional Trade Agreements in a Multilateral Trade Regime: an overview. In http://www.networkideas.org/feathm/may2004/survey_paper_RTA.pdf.

[12] UNCTAD Report. *The Entry into Force of Bilateral Investment Treaties (BITs*). At http://www.unctad.org/en/ docs/webiteiia20069_en.pdf Access in 09/02/2010.

[13] See OECD Trade Policy Working Paper No. 55 "the interaction between investment and services chapters in selected regional trade agreements". In http://www.oecd.org/officialdocuments/displaydocumentpdf/?cote=COM/DAF/INV/TD(2006)40/FINAL&doclanguage=en. Access in 12/05/2009. Brazil is one of the greatest exceptions to this trend, as, despite having signed a number of BITs, neither of them has been ratified. Yet, foreign direct investment (FDI) in Brazil is one of the world's highest.

[14] ITC Annual Report 2008. At http://www.intracen.org/Corporate/En/Annual_report.htm. Access in 10/02/2010.

[15] See the economic debate in Frankel, J. and Romer, D. (1999). "Does Trade Cause Growth?". The American Economic Review 89 (3); Rodriguez, F. and Rodrik, D. (1999). "Trade Policy and Economic Growth: A sceptic's guide to the cross-national evidence". National Bureau of Economic Research working paper 7081; Sachs, J. and Warner, A. (1995). "Economic Reform and the Process of Global Integration". Brookings Papers on Economic Activity 95.

[16] Viner, J. (1950). *The Customs Union Issue*, Carnegie Endowment of International Peace. New York.

contrary, trade diversion is supposed to lower welfare from not only the partner's countries but also from the rest of the world.[17]

A group of economists[18] challenged such assumptions and argued that RTAs are likely to be more welfare enhancing because trade diversion can have a benign effect on the member countries, especially if the members are "natural trading partners"; that is, if they are geographically close and have very high trade dependence among each other.

In this debate, Latin-American scholars played a prominent role in the Economic Commission for Latin America and the Caribbean (ECLAC). These scholars sustained that trade diversion was the only way to break through an international structure of commercial dependency of developing RTA members in relation to more advanced economies of developed countries. For Prebisch and Furtado, trade diversion was imperative and had several beneficial effects for developing countries which engaged in RTAs: increases in GDP, employment and tax income, among others. [19]

In sum, throughout the years the economic arguments regarding the welfare benefits of RTAs have led to a significant increase in RTAs and they are becoming a geopolitical strategy for both developed and developing countries.

1.3. Geopolitical strategy

RTAs may be a viable substitute for a difficult multilateral arrangement. Often nations in close geographical proximity share common interests. There may be common elements in culture, religion, language, history, social and economic systems among such nations. But often these common elements do not exist in RTAs such as USA-Jordan, Mexico-Japan and US-Korea, among others.

In addition, bilateral/regional opportunities may help developing countries to gain from regional integration and stronger economic ties to developed countries, thereby improving both the trading regimes and the rule of law and implementing structural reforms necessary to further their integration into the world economy. This could help further to open and liberalise developing countries' economies on the multilateral stage. This perspective, which sees regionalism as a pre-stage to multilateralism, is known as *open regionalism:* RTAs are the building blocks of the multilateral trading system.[20]

This geopolitical debate could be seen from another angle. According to Ghosh[21], developed countries, such as USA and EU, are pushing through RTAs to

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[17] See ECLALC Report "Desvio de comércio provocado pelos acordos bilaterais de países latino-americanos com os Estados Unidos" LC/BRS/R.150. March 2005.

[18] See Summers, L (1991). *Regionalism and the World Trading System*. Wyoming: Federal Reserve Bank of Kansas City; Krugman, P. (1991), "Is Bilateralism Bad?" in E. Helpman and A. Razin (eds.), *International Trade and Trade Policy*, Cambridge, Mass.: MIT Press.; Frankel, J. (1997): *Regional Trading Blocks in the World Economic System.* Washington DC: Institute for International Economics.

[19] See Prebisch, R. (1973). *Transformações e desenvolvimento: a grande tarefa da América Latina*. Rio de Janeiro: Fundação Getúlio Vargas; Furtado, C. (2007). *A economia latino-americana: formação histórica e problemas contemporâneos*. São Paulo: Companhia das Letras. Wionczek, M. (1966). *Integração Econômica da América Latina: experiências e perspectivas*. Rio de Janeiro: Cruzeiro. Bielschowsky, R. (Org.) (2000). *Cinqüentas anos de pensamento na Cepal*. Rio de Janeiro: Record.

[20] Correa (2001). *O Mercosul e a OMC: Regionalismo e Multilateralismo*. São Paulo: LTr.

[21] Ghosh, J. (2004). "Regionalism, Foreign Investment and Control: the new rules of the game outside the WTO". In http://www.networkideas.org/feathm/may2004/ft05_RFI_Control.htm

persuade developing countries to make deeper trade and investment commitments than is now possible in the WTO. On the other hand, certain emerging economies, such as Brazil and India, are stimulating South/South agreements under the UNCTAD General Preferences System among Developing Countries (SGPC) to further strengthen the already significant trade flow among them[22] and possibly to consolidate the idea that trade liberalisation mechanisms and commitments among developing countries need to observe certain flexibilities, which ultimately would not be make them fully compliant with the MFN clause.[23]

1.4. WTO Plus agreements

The scope and geographical reach of RTAs have expanded significantly in recent years. Apart from merely removing tariffs on intra-bloc trade in goods, the newer agreements tend to have deeper coverage. This new generation of RTAs, especially those comprising developed countries, include more regional rules on investment, competition and standards, as well as provisions on environment and labour. Most of these new agreements also include preferential regulatory frameworks for mutual trade in services.[24]

RTAs often also require negotiations in several areas not fully covered by the multilateral system, such as environment, labour, investment, and competition policy, among others. Because of their broader range, RTAs trade-related rules are known as *WTO Plus agreements*.[25] In this sense, RTAs are considered laboratories for experimentation. When RTAs supply rules in areas not successfully addressed by the WTO, RTAs fills in the lacuna.[26]

For example, if the USA and the UE succeed in including environmental and labour standards in the RTAs with both developed and developing countries, such provisions may become commonplace and eventually be eased into multilateral agreements. If a certain number of WTO Members agree to abide by environmental and labour standards in bilateral and regional levels, it will be easier to achieve consensus at the multilateral level on such issues.[27]

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[22] From 1996 to 2006, the South/South trade triplicate and totaled US$ 3 trillion (Pontes, Vol. 4, No. 20, 2010, Geneva, ICTSD.

[23] With the purpose of fostering the South/South trade, a group of developing countries (twenty-two developing countries, including Brazil, India, Indonesia, among others), during a negotiating round under the SGPC auspices, in Geneva, reached an agreement, on November 25, 2009, aimed at eliminating duties and other barriers to exports among them. Participants shall reduce import duties on approximately 70% of manufactured and agricultural products of each of them. After the effective adoption of the agreement, each of the Participants shall establish a list of products eligible to duty reduction and submit them to other Participants for negotiation and assessment. This tariff cut shall not be extended to other countries. As pointed out by Pontes, "the "preferential margin" seems to be at least 20% lower than the tariffs level applied in accordance with the WTO MFN. As a practical matter, this means that if India's import tariff on spare car parts from the United States is 10%, same spare parts imported from Brazil will be 8%". Pontes, Vol. 4, No. 20, 2010, Geneva, ICTSD.

[24] Pal, P (2004). Op. cit..

[25] Although there are some WTO rules and agreements in matters of environment – such as the General Exception in GATT's article XX – and investment – through TRIMS -, the level of regulation of these topics in some RTAs is much deeper.

[26] Matsushita, M.; Lee, Y.S. (2008). "Proliferation of Free Trade Agreements and Some Systemic Issues – In relation to the WTO disciplines and Development Perspectives". The Law and Development Review. Vol. 1, issue 1.

[27] Baldwin, R. and Low, P. (2009). *Multilateralizing Regionalism: challenges for the world trading system*. Geneva: WTO.

Another important and critical reason compelling Members to negotiate RTAs is the fear of exclusion and hence the ensuing impact on market access, especially in a post-crisis scenario. As a result of the increased bilateralism and regionalism in recent years, countries that remain relatively inactive on the bilateral front face *de facto* discrimination in many key markets. The result is that world trade is being intensified through RTAs rather than based on WTO's MFN principle.

This has been commonplace in the world trading system. It is clear that certain countries have become disadvantaged worldwide and are losing commercial space due to an initial scepticism towards RTAs.[28] With the number of RTAs rapidly increasing and with every major world trading nation negotiating RTAs with multiple countries, the phenomenon will only increase.[29]

In 1999, before the explosion of RTAs which followed the failure of the Seattle and Cancun Ministerial, the WTO estimated that 57% of world trade in goods was covered by RTAs; therefore, less than half of trade in goods was governed by the MFN principle, the cornerstone of the WTO system.[30]

It now seems unlikely for any country to take a stand against bilateralism; there are simply too many RTAs in force or under negotiation. Refusing to negotiate RTAs would only serve to distance this country from the contemporary dynamics of international trade.[31]

Some economists believe that this exclusion from markets, or disadvantage as against competitor nations, is the main reason driving the growth of RTAs. This reasoning is commonly called the "domino effect" of regionalism: the more nations join RTAs, the greater the need for non-Members to negotiate RTAs just to keep up with their international trade competitiveness.[32]

On the other hand, it has also been highlighted that RTAs have the potential to threaten the sustainability of the multilateral trading system. RTAs, by their very nature, are inimical to the MFN principle of the WTO and weaken the predictability of the entire multilateral trading system.

If the number of RTAs continues to multiply, critics contend that the entire foundation of the multilateral system could be weakened. The dividing line between the positive aspects of RTAs and the negative ones is fuzzy indeed.

1.5. The "spaghetti bowl" of rules

From the multilateral trading system point of view, another major problem created by the expansion of RTAs is the complexity resulting from the multiplicity of trade agreements in force. Each RTA contains different conditions and obligations

[28] Although MERCOSUR's policy, especially driven by Brazil and Argentina, has until recently placed much more emphasis on the multilateral negotiations, members now seem to be willing to embark on RTA negotiations to regain access to markets of countries, including in South America, that have entered into RTAs with the US, EU and China, among others.

[29] For more about the influence of RTA expansion over non-members, see Estevadeordal, A.; Freund, C. and Ornelas, E. "Does Regionalism Affect Trade Liberalization Towards Non-Members?". In CEP Discussion Paper No 868, London; LSE.

[30] Fiorentino, R.; Verdeja, L.; Toqueboef, C. (2006), "The Changing Landscape of Regional Trade Agreements: 2006 Update". Discussion Paper no 12, Geneva: WTO.

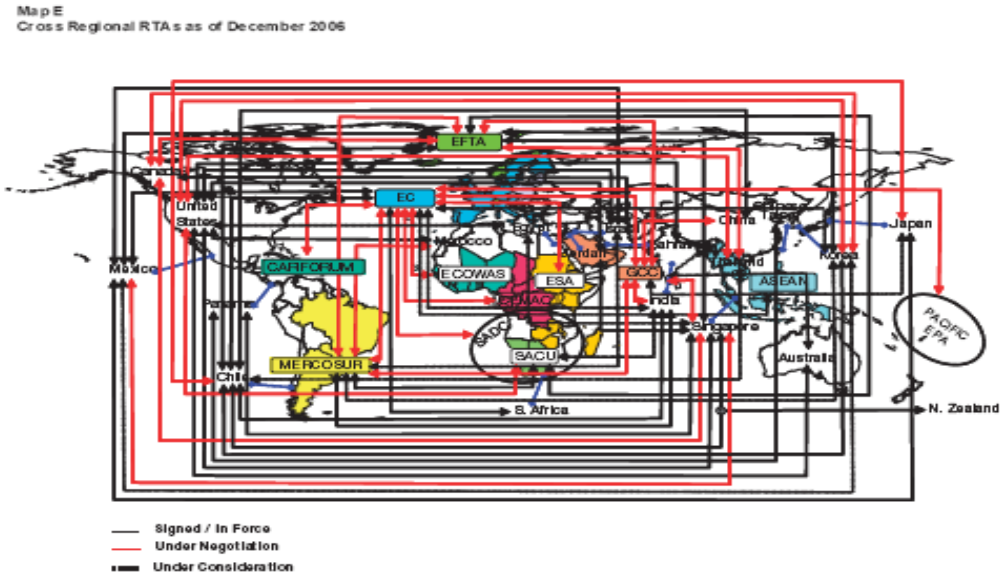
[31] Estevadeordal, A.; Freund, C.; Ornelas, E. "Does Regionalism Affect Trade Liberalization Towards Non-Members?". Discussion Paper No 868, London: LSE.

[32] Baldwin, R. (1994). "A Domino Theory of Regionalism". Graduate Institute of International Studies. Geneva: University of Geneva.

which apply to different countries and situations, a situation that can lead to confusing and conflicting obligations. The variety of standards and rules may erect obstacles to trade facilitation by increasing administrative complexity and creating a "web" of different regulations arising from fragmentation of international trade law inside the countries' jurisdiction.

This is a major concern for the international trading community that was referred to by Jagdish Bhagwati as a "spaghetti bowl" given its variety of rules and standards simultaneously in force around the world.[33] The map in Figure 2 provides an interesting illustration of this scenario.

Figure 2: Cross Regional RTAs



Source: WTO 2006

A question inevitably arises: is the world trading system moving away from non-discriminatory multilateralism towards a more fractured, fragmented system, founded in bilateralism and regionalism? From what is emerging, the answer could be "yes". In any event, that begs the question of whether the growth of discrimination is a fixed end game or a phase during which trade negotiations are carried out elsewhere but ultimately feed back into the WTO, as the work of Richard Baldwin suggests.[34]

Compared with multilateral trade negotiations, bilateral and regional trade negotiations for RTAs are generally easier. However, the proliferation of RTAs presents a serious systemic problem for the WTO regime. A RTA is a preferential trading system in which each participant provides concessions to other participants in one way or another. In this sense, a RTA is essentially a discriminatory system *vis-à-vis* outside parties.[35]

The number of RTAs makes one wonder whether in fact the multilateral trading system is the principle and the RTAs are the exceptions. In any event, uncontrolled proliferation of bilateral and regional agreements may cause erosion of the WTO disciplines and place the effectiveness of the multilateral trading system in

[33] Bhagwati, J. (2000), *The Wind of the Hundred Days: how Washington mismanaged globalization*. Boston: MIT Press.
[34] Baldwin, R. and Low, P. (2009). *Op. cit.*.
[35] Jackson, J. H. (2002). *Op. cit.*.

jeopardy. In other words, the proliferation of RTAs is a challenge for the future role of multilateral governance. Faced with the fact that there are so many RTAs (and therefore a fragmentation of trade rules) and that multilateral trade negotiations are becoming increasingly difficult, the WTO must learn to live with RTAs. In this regard, an important task for Members of the WTO is to ensure that WTO disciplines are effectively applied to prevent RTAs from being too exclusive and discriminatory in relation to outside parties.

While RTAs set forth new rules not covered in the WTO and, in this way, contribute something toward the liberalisation of trade, this liberalisation is partial and preferential in that it applies only to the RTA participants. This is a mixed impact for the multilateral trading order. It liberalises trade at least partially where the WTO cannot accomplish it and, in this sense, the total liberalisation of the world trade may be greater than otherwise. However, due to the inequality of conditions among WTO Members arising from the formation of RTA, trade may be diverted from its most natural flow. Whether advantages engendered by RTAs outweigh its disadvantages depends on the particular conditions of RTAs.

Can increased bilateralism and regionalism coexist indefinitely with the multilateral system? The answer to this question is likely to be provided, in part, by the Committee of Regional Trade Agreement (CRTA) and by the Dispute Settlement Body (DSB). It is expected that both will be more active in monitoring and enforcing the WTO rules on RTAs. As we will see below, the problem is that the meaning of the relevant provisions is far from clear.

1.6. Consequences for developing countries

Over and above these systemic implications, the core question is whether liberalisation through RTA opens windows for development.

Generally, developing countries may be disadvantaged in negotiating RTAs with developed countries in view of differences in economic and human[36] resources and political influence. In multilateral trade negotiations, developing countries can form coalitions in which many of them participate and present a united front *vis-à-vis* developed countries. While negotiating RTAs, however, developing countries, generally speaking, may not be able to rely on such a "collective approach". Consequently, developing countries may be subject to the overwhelming bargaining power of their major trading partners. Another risk for developing countries when negotiating bilateral RTAs with developed countries is that the former may impose a high standard on the developing country counterpart with respect to such matters as environmental protection and foreign direct investment.

Additionally, powerful developed countries may engage in a "divide and conquer" strategy when negotiating RTAs with developing countries. The position of developing countries is especially vulnerable in bilateral trade negotiations since, in bilateral negotiations, the difference in bargaining power between developed and developing countries may be exploited by developed countries to impose conditions favourable to them and unfavourable to developing countries. One of these unfavourable conditions would be to further reduce their manoeuvring room (or

[36] The lack of human resources in terms of adequately trained negotiators sufficient in number to handle RTAs and WTO negotiations simultaneously is indeed a great disadvantage of and a major challenge for developing countries.

policy space), already substantially diminished by the WTO Agreement on Subsidies and Countervailing Measures, to stimulate through the concession of subsidies the competitiveness of their domestic industries.

On the other hand, it must also be noted that the goal of expanding RTAs is not to dismantle the multilateral trading system. Instead, the reason is more pragmatic. Nations realized that RTAs will shield them against future protectionist incursions into their particular trading relations because their partners will be legally bound to the commitments expressed in the RTAs. Thus, even if their trading partners later are tempted to succumb to political pressure to increase protectionism, they will be legally prohibited from doing so. This reasoning is particularly persuasive for developing countries to the extent that such agreements guarantee access to large markets and protect the small nations against any future protectionist action of the larger nation seeking to reverse liberalisation.

In a nutshell, RTAs should be considered in the overall context of the economic development objectives of developing countries – RTAs should be regarded as a means to improve the economic conditions of developing countries and not an end in itself. The ability of developing countries to adopt trade-related development policies should be preserved even after signing RTAs.[37]

Although MERCOSUR is not necessarily a consequence of the last 10-year period of unprecedented proliferation of RTAs, it has been strongly influenced by the new rules, issues and subjects brought about by such a phenomenon. This South American regional integration process has undergone several changes to its institutional and legal structure, liberalisation mechanisms and objectives. Instruments and mechanisms aimed at reducing asymmetries among its members were also incorporated into its legal framework. The question arises as to whether MERCOSUR complies with relevant WTO rules.

On the other hand, the lack of a consolidated and consistent pattern and or model to negotiate RTAs, as evidenced by the RTAs recently negotiated between MERCOSUR and Israel and MERCOSUR and India, seems to be one of the major challenges for the bloc in the second decade of the 21st century. The question arises as to whether MERCOSUR will evolve to become a south-south trade cooperation paradigm.

The above two questions are addressed in the following sections.

2. The WTO Legal Framework of Regional Trade Agreements

The purpose of this section is to describe and analyse the WTO legal framework regulating RTAs. First, we address the legal status of RTAs as an exception to GATT's cornerstone provision - the Most Favoured Nation Rule (MFN). Second, we assess several RTAs' modalities according to WTO classification, their main aspects and definitions. Third, we analyse the legal requirements for RTAs under WTO rules, specifically GATT Article XXIV, the Enabling Clause, and GATS Article V. Finally, we discuss the surveillance mechanism of the RTAs notified to WTO, focusing on MERCOSUR's evaluation under such mechanism, as well as some relevant DSB views in this respect concerning MERCOSUR.

[37] Matsushita, M. and Lee, Y.S. (2008). *Op. cit.*.

2.1. Regional Trade and the MFN Rule

The MFN rule is one of the oldest and most important obligations in the area of international economic law. It means that a country must treat other countries at least as well as it treats any "most favoured" country. This rule has been the cornerstone of the multilateral trading system since its early days.[38] It is regulated by GATT Article I:1:

> Article I:1, GATT: With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 and 4 of Article III, any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.

One of the most relevant and increasingly controversial exceptions to the MFN rule is GATT Article XXIV and its equivalent for services: GATS Article V.[39] These provisions authorize the concession of trade preferences – in terms of goods and services respectively - through the formation of customs unions and free trade areas.

The concept of a trading 'preference' is instrumental for understanding the relationship either between RTAs and MFN or between the General System of Preferences (GSP) and other unilateral, non-generalized preferential schemes and MFN.

By definition, a ´positive´ preference is a trading advantage being offered to one or more territories. It is ´preferential´ and therefore conflicts with MFN because the treatment is not being likewise accorded to *all other* WTO Members. The same conflict occurs with a ´negative´ preference, under which the MFN treatment being accorded to all other parties is denied to one or more of them.

Historically, MFN has been viewed as a means of protecting the interests of smaller and weaker territories in the trading system, since their lack of commercial policy power would otherwise invite less preferential treatment when they could not impose reciprocal conditions on their larger trading partners, or be included in preferential systems that larger and more powerful GATT Contracting Parties could establish. At the same time, MFN has also been viewed as an instrument favouring larger producing territories, since it guarantees a right of access to other territories' resources, including in smaller and weaker territories in the trading system. Both elements are present in the historical justifications for MFN.[40]

With MFN established in the GATT, the question of its practical scope of application in global commercial policy depends upon how broadly or how narrowly the exceptions to MFN are drafted and subsequently how they are applied in commercial practice. The overall impact of MFN in the system depends upon the resulting legal architecture that is established between this principle and the exceptions that are allowed to derogate from it for the establishment of RTAs and other preferential systems. This relationship between MFN and RTAs is understood

[38] Lester, S. and Mercurio, B. (2008). *Op. cit.*.

[39] Apart from the exception for RTAs, there are also exceptions referring to heath, environment, public morals, as well as exception treatment for developing and least-developed countries.

[40] Tenier, J. (2003). *Intégrations regionales et mondialisation : complementarieté ou contradiction*. Paris: Documentation Française.

by examining both the substantive rules, as well as the institutional controls that are provided to ensure compliance.[41]

While the GATT RTA exception in Article XXIV for customs unions and free-trade areas is not the only exception to MFN, it is probably the most important 'rule and exception' relationship in the multilateral trading system, since it serves to define the role and functioning of the system itself in international trade.

The rise of RTAs, with their inherent discriminatory qualities, led many to question whether they might undermine the multilateral trading system. This growing discontent led to the formation of the WTO Committee on Regional Trade Agreements (CRTA), which was established in 1996 to examine individual RTAs and to consider whether they were systematically compatible with multilateralism.[42]

Not all RTAs are alike. The literature has varied over time and has been very imprecise in describing and differentiating them.[43] According to WTO official documents and reports[44], RTAs can be classified as a Free Trade Area, a Customs Union, Preferential Trade Agreement and an Economic Integration Area. Under this typology, the status of notifications to WTO in August 2010 is the following:

Table 1: Number of RTAs in force by legal basis

Legal Basis	Grand total
GATT Art. XXIV (FTA)	158
GATT Art. XXIV (CU)	15
Enabling Clause	30
GATS Art. V	82
Grand total	*285*

Source: WTO RTA Database 2010

Table 2: Number of RTAs in force by modality

	Enabling clause	GATS Art. V	GATT Art. XXIV	Grand total
Customs Union	6		15	21
Economic Integration Agreement		78		82
Free Trade Agreement	9		154	167
Preferential Trade Agreement	14			15
Total	*29*	*78*	*169*	*285*

Source: WTO RTA Database 2010

[41] The GATT *rationale* in commercial policy practice was to generally prohibit the use of quantitative restrictions in international trade (GATT Article XI) in favor of the use of tariff duties (import taxes) as the permitted form of ´legal economic protection´ (GATT Article II). The GATT then established that the tariff duties of the contracting parties would operate according to MFN (GATT Article I). Thus, any benefit or privilege that is accorded by any GATT party to any other state or territory would be required to immediately and unconditionally extend that same benefit to all other GATT contracting parties. In Jackson, J. H. (2002), *The World Trading System: law and policy of international economic relations*. Boston: MIT.

[42] Baldwin, R; Low, P. (2009). *Multilateralizing Regionalism: challenges for the world trading system*. Geneva: WTO.

[43] See, for example, the classic taxonomy of Bela Balassa for the stages of regional integration in Balassa, B. (1961). *The Theory of Economic Integration.* Illinois: Richard Irwin Press.

[44] See RTA Database for classification, criteria and reports. In http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx

2.2. GATT Article XXIV

Article XXIV of the GATT establishes the basis for allowing RTAs as an exception to the MFN requirement. Under article XXIV, there are two types of RTAs: Free Trade Areas and Customs Unions.

A Free Trade Area (FTA) is an arrangement through which members establish the obligation to eliminate tariffs and non-tariff barriers for products imported from other FTA members. In short, a FTA is an area in which there are no tariffs or non-tariff barriers on "substantially all the trade" among the constituent countries, but each country is free to establish its own tariff and non-tariff barriers with respect to the rest of the world. Approximately 70 per cent of the RTAs that have been notified to the WTO are FTAs.[45]

An FTA is defined by Article XXIV, 8.b. of GATT:

> Article XXIV, 8.b. GATT - 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 (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.

In a Customs Union (CU), there are again no tariffs on trade within the participating countries, but for each product category there is a common tariff applied by each country *vis-à-vis* the rest of the world. This is usually referred to as the Common External Tariff (CET). About 8 per cent of RTAs currently in force are customs unions, including MERCOSUR, the Andean Pact, the Central American Common Market (CACM) and the Southern African Customs Union (SACU).

A CU is defined by Article XXIV, 8.a. of GATT:

> Article XXIV, 8.a. GATT - 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 (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) 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) subject to the provisions of paragraph 9, 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;

Article XXIV establishes four basic rules with which WTO Members must comply in order to establish a RTA as regards trade in goods. The first is a procedural requirement: (1) to *notify the WTO* of the RTA for a subsequent review by the CRTA. The second and third rule are substantive in nature: (2) *an external trade requirement*, which obliges RTA members not to raise the overall protection and make access for products more onerous than before the RTA, and; (3) *an internal trade requirement*, that establishes the obligation to liberalize substantially all trade among members of the RTA. The last rule, (4) *reasonable period of time*, determines the maximum length of time for finalizing the implementation of the RTA.

During the Uruguay Round, negotiators agreed to consolidate their understanding on the interpretation of Article XXIV provisions on a document entitled "The Understanding on the Interpretation of Article XXIV of the GATT

[45] Neumann, V.T. (2009). *Regional Trade Agreements and the WTO*. 7th International Conference on Managment, Enterprise and Benchmarking, Budapest: MEB.

1994" (Understanding). The "Understanding" forms the basis for interpreting Article XXIV and its provisions need to be read side by side with Article XXIV paragraphs, due to the details it provides. In this paper, reference to the Understanding will be made where appropriate.[46]

Rule number 1: Obligation to notify

WTO Members desiring to enter into a RTA covering trade in goods must notify the Council of Trade in Goods of their intention, which transfers the notification to the CRTA to examine the RTA for its compatibility with WTO Rules. The dynamics of these examinations will be further analyzed below.

The question arises as to whether the notification must be presented before or after the formation of a RTA: must it be *ex ante* or *ex post*? The majority of RTAs have been notified to GATT/WTO after their successful completion. This seems to violate the spirit of Article XXIV: 7(a) of the GATT. What was originally intended to be an *ex ante* review has become an *ex post* review.[47]

Rule number 2: External trade requirement

The second rule – a demand in terms of external trade requirement – changes under article XXIV: 5 depending on whether the RTA is a FTA or a CU.

According to Article XXIV: 5 (b), when entering into a FTA, parties may not alter their external protection in such a manner as to adversely affect non-FTA parties. The *rationale* for this rule is simple: FTAs are meant to facilitate trade liberalization; therefore, an FTA must be structured in terms of removing trade barriers among FTA participants instead of increasing trade barriers with non-participants.

This same requirement is more complicated when it comes to a CU. According to Article XXIV: 5 (a) two main requirements must be fulfilled: (i) not to raise the overall level of external protection above certain threshold; and (ii) to make compensatory adjustments when the customs duties in some CU participants have been raised to create harmonized external tariffs.

Rule number 3: Internal trade requirement

One of the most controversial provisions of Article XXIV is unquestionably the internal trade requirements. Paragraphs 8 (a) and (b) provide for the elimination of duties and other restrictive regulations of commerce with respect to "substantially all the trade" between Members of RTAs.

Throughout the years, Members could not agree on the meaning of "substantially all the trade" or of "other restrictive regulations of commerce". Historically, since the 1960s, defining operationally the rule of liberalising substantially all the trade has been very difficult, both for working groups and the Appellate Body and during Ministerial negotiations.[48]

Rule number 4: Reasonable period of time

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[46] According to its Preamble, the Understanding on the Interpretation of Article XXIV was required, *inter alia*, to "reinforce the effectiveness of the role of the Council for Trade in Goods in reviewing agreements notified under Article XXIV, by clarifying the criteria and procedures for the assessment of the new or enlarged agreements, and improving the transparency of all Article XXIV agreements, and "the need for a common understanding of the obligations of Members of paragraph 12 of Article XXIV." Paragraph 12 of Article XXIV establishes that each "contracting party shall take such reasonable measures as may be available to it to ensure observance of the provisions of this Agreement by the regional and local governments and authorities within its territories."

[47] Thortensen, V. (2002). *Os acordos regionais e as regras da OMC*, *in* Amaral Júnior, A. (Org.), *A OMC e o Comércio Internacional*. São Paulo: Aduaneiras.

[48] Most recently, Australia submitted a proposal in the Doha Round negotiations to conceptualize "substantially all the trade" as a quantitative component and proposed that 95 per cent of all six-line tariff lines listed in the Harmonized System. See Lester, S. and Mercurio, B. (2008). *Op. cit.*.

The forth rule is settled in Article XXIV:5(c) of GATT and its Understanding. In GATT there is a term requirement that any interim agreement referred to in subparagraphs (*a*) – customs union - and (*b*) – free trade area - shall include a plan and schedule for the formation of such a customs union or of such a free-trade area within a reasonable length of time. To clarify this article, the Understanding established that a "reasonable period of time" shall be construed as not more than 10 (ten) years.

2.3. Regional Trade and Development: The Enabling Clause

The relation between RTAs and development was never clear in the early GATT days. In fact, the relation between trade and development as a whole was only formed in legal terms in the multilateral trading system in 1965, with the insertion of Part IV of GATT, entitled Trade and Development.[49]

Under Part IV, a fundamental principle of the multilateral trading system was created: the principle of non-reciprocity. It was just a matter of time until this principle was extended to RTAs involving developing countries.

Until 1979, the year in which the Enabling Clause was established, several developing countries resorted to Part IV of GATT to justify RTAs that were not consistent with Article XXIV. The main rule not observed by these RTAs among developing countries, due to the high asymmetries in the intra-trade area, was Article XXIV: 8 (a) and (b), which demanded the liberalization of "substantially all the trade". The non-reciprocity principle provided the basis for RTAs involving developing countries liberalization to be carried out in "substantially part of the trade" – the part that benefits developing countries.[50]

The Enabling Clause, formally known as "Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries" was adopted in 28 November 1979 as part of the Tokyo Round, which began in 1973, represented the systematic legalization of commercial preferences, under the principle of Special and Differential Treatment (S&D). The Enabling Clause comprises: a) the Generalized System of Preferences; b) Non-tariff measures in GATT instruments; c) Global or regional arrangements among developing countries, and (d) Special treatment to LDCs.

According to the WTO's official classification, a RTA notified under the Enabling Clause is defined as a Preferential Trade Agreement (PTA). A PTA is a type of RTA in which countries offer preferential access to goods and possibly services to their partners. The preferential access need not necessarily cover all goods, and need

[49] The integration of Part IV to GATT was the result of a worldwide movement of developing countries which had identified that the continued dependence of a number of less-developed countries on the exportation of a limited range of primary products would maintain these countries in a condition of under-development. Under this perspective – known as Dependency Theory - there was a need to provide in the largest possible measure more favourable and acceptable conditions of access to world markets for these countries, thus permitting an expansion of world trade and demand and a dynamic and steady growth of the real export earnings of these countries so as to provide them with expanding resources for their economic development.

[50] Feuer, G.; Cassan, H. (1985), *Droit international du développment*. Paris: Dalloz.

not necessarily entail the complete removal of tariffs where preferences are granted. PTAs therefore need not offer symmetric access across the partner countries.[51]

PTAs have two main characteristics: (i) they are based on the principle of non-reciprocity, which allows developing countries not to reduce tariffs to the same extent as the developed countries; (ii) according to the principle of special and differential treatment, the concessions granted by developed countries to developing countries in a PTA are not automatically extended to other WTO Members.

A PTA is defined by Paragraph 2 of the Enabling Clause:

> Paragraph 2, Enabling Clause - Regional or global arrangements entered into amongst less-developed contracting parties for the mutual reduction or elimination of tariffs and, in accordance with criteria or conditions which may be prescribed by the CONTRACTING PARTIES, for the mutual reduction or elimination of non-tariff measures, on products imported from one another.

As highlighted by Manin (1997), a paradigmatic example of a PTA can be seen in the European Union's (EU's) trading relationships with the African, Caribbean and Pacific (ACP) States under the Lomé and Cotonou agreements. Under these agreements, the EU granted preferential access on most exports by the ACP states, while the ACP states retained their tariffs on EU exports.[52]

Paragraph 3 of the Enabling Clause defines the conditions for these RTAs to be considered in compliance with GATT/WTO rules:

> Any differential and more favourable treatment provided under this clause:
> *(a)* shall be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade of any other contracting parties;
> *(b)* shall not constitute an impediment to the reduction or elimination of tariffs and other restrictions to trade on a most-favoured-nation basis;
> *(c)* shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries.

Finally, according to the general GATT principle of transparency, Paragraph 4 establishes the obligation to notify the agreement to the CRTA.

2.4. Integration beyond trade of goods: GATS Article V

The General Agreement on Trade in Services (GATS) also established rules for RTAs which refer to trade in services. According to the GATS, these RTAs are called Economic Integration Areas (EIA).

An EIA is defined by GATS Article V (b) as an agreement which has substantial sectoral coverage, and 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 by GATS, through the elimination of existing discriminatory measures, and/or prohibition of new or more discriminatory measures.

Essentially similar to Article XXIV of GATT, Article V of GATS establishes four basic rules that WTO Members must comply in order to establish an EIA:

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[51] The term PTA is sometimes used erroneously to include the more ambitious Free Trade Area and Customs Union concepts. Article XXIV of the GATT in principle forbids PTAs that fall short of being Free Trade Areas or Customs Unions.

[52] For more about EU's external trading relations, see MANIN, P. (1997). For the complete text of the Lomé and Cotonou agreements, access http://ec.europa.eu/development/geographical/regionscountries_en.cfm.

Rule number 1: Obligation to notify

WTO Members that wish to celebrate or modify an EIA shall notify the CRTA, through the Council for Trade in Services (CTS), to whom the Members of the agreement shall make available any information the CTS finds relevant in the process of examining its compliance with GATS rules.

The controversy about when this notification must occur is similar to the interpretation of Article XXIV of the GATT: shall the notification be *ex ante* or *ex post*? The rule in Article V:7(a) sets forth that the notification be done promptly. There is no precise definition of this term. Some sustain that it should respect the term of 90 days - the same term that is established in Article XXVIII of GATT for notifying any modification of schedules. The issue has still not been resolved by the CTS and the WTO Members.[53]

Rule number 2: Intra RTA trade requirements

Article V:1 defines the obligations that must be observed in terms of intra RTA trade to be considered an EIA in compliance with the WTO rules. The article regulates internal trade on services through two basic concepts: *substantial sectoral coverage*, in Article V:1 (a) and *elimination of substantially all discrimination*, in Article V: 1 (b).

According to the footnote of GATS Article V:1 (a), The concept of "substantial sectoral coverage" is understood in terms of a number of sectors, volume of trade affected and modes of supply. However, the concept "elimination of substantially all discrimination" has no clarification or official interpretation.

The central question of this paragraph is related to the meaning of "substantially all" and consequently the possibility of implementing discriminatory measures in an EIA. To what extent are these exceptions allowed? That is an open question and there is no relevant WTO jurisprudence in this regard.[54]

Finally, another important aspect referring to the internal trade aspect of an EIA refers to the observance of the principle of national treatment in terms of services. Article V:6 governs the extension of national treatment to legal entities originating in a Member other than the EIA parties. The rule is not conclusive about the national establishment conditionality and also refers to the fact that this enterprise engages in "substantial business operations", another vague concept not clarified by the CTS.

Rule number 3: Trade requirements vis-à-vis non-Members

In this regard, there are two requirements, provided under paragraphs 4 and 5 of Article V of GATS: (1) the agreement shall not increase or restrict trade with non RTA signatories in sectors or subsectors that are not original from parties of the EIA; (2) if an adjustment of a Member's list of commitments is necessary, due to the fact of joining the EIA, the Member shall notify such modification within 90 days.

Rule number 4: Reasonable length of time

As analysed above, Article V:I (b) determines that any EIA should enter into force in a reasonable time-frame. Some Members argue that the time-frame for EIAs is the same as for FTAs and CUs, established in Paragraph 3 of the Understanding of Article XXIV. Therefore, the reasonable time-frame should not be longer than ten years.

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[53] To see the actual debate on the interpretation of the RTA rules, access the documents of the Negotiating Group on Rules (NGR) in http://www.wto.org/english/tratop_e/region_e/region_negoti_e.htm.

[54] Thortensen, V. (2001). *OMC: As Regras do Comércio internacional e a Nova Rodada de Negociações Multilaterais.* 2ª Edição. São Paulo: Aduaneiras.

Rule number 5: Agreements involving developing countries

Finally, Paragraph 3 of GATS Article V contains important provisions addressing developing countries. It distinguishes between two types of agreements: the first, when there are developed and developing Members (V:3 a) and a second, when there are only developing Members involved in the agreement (V:3 b).

2.5. WTO's surveillance of RTAs

During the GATT years, examination of agreements was conducted in individual working parties. The establishment of the CRTA as the single body responsible for examining the agreements helped streamline the examination process and provided a forum for the discussion of cross-cutting systemic issues which are common to most, if not all, agreements. In February 1996, the WTO General Council established the Committee on Regional Trade Agreements. 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.

RTAs falling under Article XXIV are notified to the *Council for Trade in Goods* (CTG), which adopts the terms of reference and transfers the agreement to the CRTA for examination. The notification of agreements falling under the Enabling Clause is made to the *Committee on Trade and Development* (CTD). RTAs covering trade in services, whether concluded by developed or developing WTO Members, are notified to the *Council for Trade in Services* (CTS).

In 2006, the General Council established on a provisional basis a new Transparency Mechanism for all RTAs. The new transparency mechanism provides for early announcement of any RTA and notification to the WTO. Members will consider the notified RTAs on the basis of a factual presentation by the WTO Secretariat.

Basically, the procedures of the new Transparency Mechanism, according to the 2006 General Council Decision[55], are the following:

"Early Announcement: Members participating in new negotiations aimed at the conclusion of a RTA should inform the WTO Secretariat of such negotiations. Members which are parties to a newly signed RTA should send to the Secretariat information on the RTA, including its official name, scope, 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.
Notification: The notification of a RTA by Members should take place as early as possible, in general no later than the parties' ratification of the RTA or any party's decision on the application of the relevant parts of an agreement and before the application of preferential treatment between the parties. Parties should specify under which provision(s) of the WTO agreements the RTA is notified and provide the full text and any related schedules, annexes and protocols.
Procedures to Enhance Transparency: The consideration by Members of a notified RTA shall be normally concluded within one year after the date of notification. The WTO Secretariat will draw up a precise timetable for the consideration of the RTA in consultation with the parties at the time of the notification.

[55] WT/L/671 - Decision of 14 December 2006 of the General Council which created the Transparency Mechanism for Regional Trade Agreements.

Factual Presentation: The WTO Secretariat's factual presentation, as well as any additional information submitted by the parties, is to be circulated in all WTO official languages so that Members' written questions or comments on the RTA under consideration can be transmitted to the parties through the Secretariat.
Subsequent Notification and Reporting: Any changes affecting the implementation of a RTA, or the operation of an already implemented RTA, should be notified to the WTO as soon as possible after changes occur. The parties should provide a summary of the changes made, as well as any related texts, schedules, annexes and protocols, in one of the WTO official languages and, if available, in electronic format.
Preparation of Factual Abstracts: Article 22(b) of the Transparency Mechanism calls for a factual abstract to be prepared by the Secretariat to present the features of RTAs for which the CRTA has concluded the "factual examination".

Source: WTO Transparency Mechanism Decision (2006)

The status of examinations in August 2010 is the following:

Table 3: Status of examinations of RTA notifications

	Enabling Clause	*GATS Art. V*	*GATT Art. XXIV*	*Grand total*
Factual Presentation in preparation	7	25	63	95
Factual Presentation on hold	0	3	0	3
Factual Presentation distributed	4	33	50	87
Factual Abstract in preparation	8	5	10	23
Factual Abstract distributed	3	16	32	51
Report adopted	1	0	17	18
No report	8	0	0	8
Grand total	31	82	172	285

Source: WTO RTA Database

2.6. MERCOSUR's assessment under WTO rules

In 1992, MERCOSUR was notified to the former Committee on Trade and Development, which established a working party in 1993 with the following objective:

> "To examine the Southern Common Market agreement (MERCOSUR) in the light of the relevant provisions of the Enabling Clause and of the General Agreement, including Article XXIV and to transmit a report and recommendations to the committee for submission to the contracting parties, with a copy of the report transmitted as well to the council. The examination in the working party will be based on a complete notification and on written questions and answers."[56]

From a regional perspective, MERCOSUR was negotiated as an Economic Complementation Agreement (ACE) No. 18 under the Latin American Integration

[56] (GATT/AIR/3545/ 21 January 1994). Terms of Reference of the Working Party, established on the Seventy-Fourth Session held on 28 May, 1993.

Association's (LAIA) framework.[57] As a broader RTA, LAIA is in force since 1980 and had been notified to the GATT when the Enabling Clause came into force.[58] MERCOSUR's legal status at the time of its notification in 1992 was of a sub-regional RTA falling under article XXIV to the extent that its purpose was to form a Customs Union and under the Enabling Clause (LAIA's legal basis under GATT). [59]

Sometime later, prior to assessing MERCOSUR's compliance with WTO rules, CTD decided that such RTA would need to simultaneously fulfil the requirements of both the Enabling Clause and the provisions of Article XXIV.[60]

After four CTD meetings, MERCOSUR's preliminary evaluation – called factual examination - was concluded in 2006.

According to Prazeres:

> "The large amount of rules and exceptions, as well as the implementation deficit, were important factors which delayed the conclusion of this elementary phase (…). During the debates, the maintenance of the automobiles and sugar regimes – set aside from the trade liberalization rules – motivated most of the questions and replies."[61]

One of the concluding documents of this phase was the publication in 2005 by the WTO Secretariat of MERCOSUR's Weight Average Tariff Rates and Customs Duties.[62] This report is central to the RTA's examination because of its comparative evaluation of trade barriers level pre and post the RTA coming into force.[63]

In MERCOSUR's case, the factual evaluation was favourable, as the table below demonstrates:

Table 4: MERCOSUR's Weight Average Tariff Rates and Customs Duties

	Pre-Customs Union	1995 applied tariff rates	CET 2006
Weighted average tariff rates (%)	12.5	12.0	10.4
Average customs duties (million US)	4,768	4,545	3,945

Source: WTO Secretariat (2005)

After concluding the factual examination, based on the new Transparency Mechanism procedures described above, in section 3.5, the CTD is currently examining MERCOSUR's compliance with Article XXIV and the Enabling Clause and is due to complete such an assessment shortly with the presentation of a full report.

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[57] LAIA's signatories are Argentina; Bolivarian Republic of Venezuela; Bolivia; Brazil; Chile; Colombia; Cuba; Ecuador; Mexico; Paraguay; Peru; and Uruguay. The legal texts and agreements signed under LAIA are available at http://www.aladi.org/nsfaladi/textacdos.nsf/vaceweb.

[58] (GATT/ L/5342/ 01 July 7 1982). LAIA's notification to the Committee on Trade and Development.

[59] (GATT/L/0744/ 9 July 1992). MERCOSUR's notification to the Committee on Trade and Development.

[60] (WT/COMTD/5/Rev.1 25 October 1995). Working Party on the Southern Common Market Agreement.

[61] Prazeres, T. (2008). *A OMC e os Blocos Regionais*. São Paulo: Aduaneiras. Free translation by the authors of the original in Portuguese.

[62] (WT/CMYD/1/Add15 24 May 2005). MERCOSUR's Weight Average Tariff Rates and Customs Duties. Note by the Secretariat.

[63] In fact, at the final CTD meeting after this report, MERCOSUR's member delegations argued that, if the Secretariat took as a time reference, instead of the pre-Customs Union years (1992 to 1994), used the pre-Asunción Treaty years (1991), MERCOSUR's evolution would be much higher. In this period, the weighted average tariff rates were over 18.34% in Argentina, 20.73% in Brazil, 14.09% in Paraguay and 23.40% for Uruguay. (WT/COMTD/1/Add.16 16 Mat 2006). Note on the Meeting of the CTD for MERCOSUR examination.

More recently, MERCOSUR was notified to the WTO pursuant to Article V of GATS[64] and is still in the stage of preparing its factual presentation to be submitted to the CRTA.[65]

The CRTA has been criticized for its ineffectiveness.[66] Its lack of dynamics and objectivity in assessing RTAs has been its major problem: it has been unable to fill in the vital gap of setting the rules and directions of RTAs proliferation. The difficulties experienced by the CRTA were recognized in its own 2009 report:

> Although considerable progress has been made in the preparation of factual presentations, the Committee continues to experience some difficulties in adhering to its work programme. This is due to a number of factors: delays in the receipt of statistical data from parties, data discrepancies in Members' submissions, and delays in the receipt of comments from parties. The Secretariat is working actively with the parties concerned in an effort to overcome these difficulties.[67]

In any event, the Transparency Mechanism in force since 2006 has permitted a more intense dialogue between RTA parties and the CRTA. As can be seen in MERCOSUR's consideration procedures under WTO law, it has had a reasonable communication with the CRTA,[68] which increased the chances of the CRTA eventually coming to a conclusion of its assessment of whether MERCOSUR rules are WTO compatible or not. Nevertheless, the fact remains that, after almost 20 years since its notification, the examination of MERCOSUR is not concluded yet. Therefore, there is still no official and definitive WTO conclusion about MERCOSUR's legality under RTA rules.

2.7. Relevant WTO Jurisprudence on RTAs for MERCOSUR

While the CRTA has failed so far to effectively analyze the almost 500 RTA notifications, the WTO Dispute Settlement Body (DSB), through the Panel and the Appellate Body (AB), has few but significant rulings regarding the compatibility of RTAs with WTO rules.

The leading WTO case on RTAs is *Turkey-Textiles*, in which some clarification on Article XXIV provisions was provided. Additionally, the legal implications of the CRTA review procedure and the competence of the DSB to analyze the compatibility of notified RTAs were also addressed.[69]

The case concerned a claim lodged by India against Turkey, which had imposed quantitative restrictions on Indian textiles alleging that they were necessary to fulfil its obligations under the EC-Turkey Customs Union Agreement.[70] In Turkey's view, since the EC maintained its own set of quotas on India's textile products, the imposition of quotas was required as per paragraph 8 of Article XXIV,

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[64] (WT/ S/C/N/388 / 05 December 2006). MERCOSUR's notification as an Economic Integration Area.
[65] (WT/REG/20 / 16 October 2009). Report of the Committee on Regional Trade Agreements to the General Council.
[66] It must be stressed that such an inefficiency is partly due to the vagueness of GATT (Article XXIV and Enabling Clause) and GATS provisions related to formation and rules of RTAs.
[67] (WT/REG/20 / 16 October 2009). Report (2009) of the Committee on Regional Trade Agreements to the General Council.
[68] Available in http://rtais.wto.org/UI/PublicShowMemberRTAIDCard.aspx?enc=cxlE/jp1Q6Qlzkvva DSyvyGjCyds4F92CgtQ6tuKRLk=. Access in 20 August 2010.
[69] *Turkey – Restrictions on Imports of Textile and Clothing Product - Case DS34.*
[70] For the EC-Turkey agreement, see http://ec.europa.eu/trade/creating-opportunities/bilateral-relations/countries/turkey/.

which provides that Customs Union members must apply substantially the same duties and other regulations of commerce to the trade of non-members. The panel found though that these quotas were not covered by the WTO Agreement on Textiles and hence were inconsistent with the GATT Article XI (*General Elimination of Quantitative Restrictions*).

Moreover, according to the panel, Article XXIV could never be used to validate an exception for an unlawful quantitative restriction. This panel's finding was not upheld by the AB. The AB ruled that in principle Article XXIV could be used to validate any GATT article violation provided that two conditions were met: (i) "… that the measure at issue is introduced upon the formation of a customs union that fully meets the requirements of sub-paragraph 8 (a) and 5 (b) of Article XXIV; and (ii) "…the party must demonstrate that the formation of customs union would be prevented if it were not allowed to introduce the measure at issue". It is incumbent on the interested party to prove the need for any such measure.

As stated by UNCTAD:

> This leading case has a significant impact on the legal security of RTAs in all those cases where there has been no definitive report or recommendation from the CRTA as to the compatibility of an RTA with Article XXIV, as well as GATS Article V. In essence, the burden of proof has been altered where previously regional parties held that once notified, if the consensus procedures of paragraph 7 did not result in a negative recommendation, the RTA was essentially legally secure from any later challenges. Arguably, the reverse is true now. In the failure to obtain a positive recommendation from the GATT and GATS specific councils, a regional member invoking its Article XXIV defence must be in the position (with the burden of proof) to demonstrate that its agreement is lawfully qualified under WTO law in a panel proceeding.[71]

This was the first dispute submitted to the DSB for the analysis of the legality of a notified RTA, whose evaluation has not yet been concluded. This is exactly the current status of MERCOSUR. Another reason for conferring importance to this case for MERCOSUR's analysis is the double condition test set out by the DSB. These criteria were applied by the DSB on both cases that involved MERCOSUR: the 1998 *Argentina – Footwear* case and the 2002 *Brazil- Retreated Tires*, which are examined below.

In the case *Argentina – Footwear* regarding safeguard measures within the scope of RTAs, the DSB addressed the issue of compatibility with the WTO rules.[72]

In 1998, the European Community (EC) questioned the legality of the definitive safeguard measures imposed by Argentina over the import of footwear originated from all WTO members, except from MERCOSUR countries. Argentina alleged that, according to GATT Article XXIV and the Agreement on Safeguards[73], it was authorized to exclude MERCOSUR's members from these restrictions in view of their customs union commitments.

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[71] Document (UNCTAD/DTL/KTCD, 2008/2). *Virtual Institute Teaching Material on Regional Trade Agreements*. Geneva, 2010. P. 70

[72] *Argentina — Safeguard Measures on Imports of Footwear (DS121).*

[73] The specific legal basis of this case is the footnote of Article 2 of the Agreement on Safeguards, which states: "A customs union may apply a safeguard measure as a single unit or on behalf of a member State. When a customs union applies a safeguard measure as a single unit, all the requirements for the determination of serious injury or threat thereof under this Agreement shall be based on the conditions existing in the customs union as a whole. When a safeguard measure is applied on behalf of a member State, all the requirements for the determination of serious injury or threat thereof shall be based on the conditions existing in that member State and the measure shall be limited to that member State. Nothing in this Agreement prejudges the interpretation of the relationship between Article XIX and paragraph 8 of Article XXIV of GATT 1994."

However, the EC raised the issue that, when Argentina's investigation took place, it had also taken into consideration imports from MERCOSUR in the investigation. Only at a later stage, Argentina decided to exclude imports from MERCOSUR from the application of the safeguard measures.

Moreover, the EC and other third parties, such as Indonesia and US, argued that these definitive safeguard measures were not imposed by the customs union, i.e. MERCOSUR, but solely by Argentina, which would prevent them from being founded on Article XXIV and the WTO Agreement on Safeguards. Indonesia and the US went even further and sustained that MERCOSUR had not been notified under Article XXIV, as its members have chosen to notify it only under the Enabling Clause. Therefore, in their view, MERCOSUR would not be eligible to invoke the status of a customs union under article XXIV and footnote of Article 2 of the Agreement on Safeguards.

The DSB confined itself to analyzing specifically matters of the Agreement on Safeguards and avoided addressing directly the compatibility of MERCOSUR with Article XXIV and the Enabling Clause.

According to the panel:

> Argentina, on the facts of this case, cannot justify the imposition of its safeguard measures only on non-MERCOSUR third country sources of supply on the basis of an investigation that found serious injury or threat thereof caused by imports from all sources, including imports from other MERCOSUR member States.[74]

The AB upheld the Panel's findings that:

> Based on the Agreement on Safeguards, a safeguard measure must be applied to the imports from "all" sources from which imports were considered in the underlying investigation, Therefore, Argentina's investigation was found inconsistent with the agreement since it excluded imports from MERCOSUR from the application of its safeguard measure while it had included those imports from MERCOSUR in the investigation.[75]

Although the DSB has not examined MERCOSUR under WTO's legal framework on RTAs, this can be deemed a landmark ruling for MERCOSUR for two reasons.

First and most important is the implicit DSB conclusion that MERCOSUR, although formally notified under the Enabling Clause, is, *de facto* and *de jure*, a RTA falling under Article XXIV. The DSB did not state this expressly, but when it analyzed MERCOSUR under the Agreement on Safeguards, it implicitly extended the rights and obligations of Article XXIV to the customs unions notified under the Enabling Clause.

Therefore, the US and Indonesia argument was not taken into consideration. From this case on, it is valid to say that if Article XXIV is the gender of RTAs, the agreements falling under the Enabling Clause are species. The rules of Article XXIV apply to all RTAs, even those notified under the Enabling Clause.

A second and also crucial consequence of this decision is that it was a major push forward to the evolution of MERCOSUR's common trade policy. From there on, MERCOSUR was compelled to establish a common trade defence policy, conducted by the customs union and not by single member states.

The second DSB case concerning MERCOSUR was the dispute *Brazil-Retreated Tires.*[76] Although it constituted an opportunity for the DSB to assess

[74] *Argentina – Footwear* Panel Report. Circulated in 25 June 1999.
[75] *Argentina – Footwear* AB Report. Adopted in 12 January 2000.
[76] *Brazil — Measures Affecting Imports of Retreaded Tires (DS332).*

MERCOSUR's compliance with RTA rules, it did not do so and, once again, dodged an objective and definitive decision over MERCOSUR's legality.

This case, initiated in 2002 by the EC against Brazil, involves matters of environment and public health combined with regional integration. Basically, it is concerned with a Brazilian trade policy which banned the import of retreated tires from all over the world, while allowed the import of such tires when originated from MERCOSUR.

According to the EC, the measure was a violation of the MFN and represented a quantitative restriction of its exports, which is incompatible with WTO rules. Brazil alleged that the import of huge amounts of retreated tires had severe environmental impacts in Brazil and that the quantitative restrictions were justified under GATT's Article XX (b):

> GATT Article XX - General Exceptions: Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures: (b) necessary to protect human, animal or plant life or health.

At the same time, Brazil's defence had to combine its arguments with MERCOSUR's obligations to justify the discriminatory treatment. Here, the main argument was that Brazil was simply following a decision of MERCOSUR's dispute settlement system, which had determined that the country should eliminate all barriers on imports of retreated tires from MERCOSUR. For this reason, Brazil had modified its trade policy for retreated tires and allowed the imports strictly from MERCOSUR.

The DSB, in the end, condemned Brazil's measure by invoking the rationale of the leading case of *Turkey-Textiles*, even though it hasn't based the decision on Article XXIV. Although it understood that Article XX's *rationale* is necessary for international trade, according to the double test set by case Turkey-Textiles, *the specific measure cannot constitute an unjustified or arbitrary discrimination between countries with the same conditions*.[77]

The AB maintained that the measure constituted *an unjustified or arbitrary discrimination* because the justification was not related to the objective of the measure - the protection of human, animal or plant life or health. If Brazil continued to import retreated tires from MERCOSUR, this objective would be undermined. Article XX's *rationale* was not met.

The main AB findings are the following:

> In our view, the ruling issued by the MERCOSUR arbitral tribunal is not an acceptable rationale for the discrimination, because it bears no relationship to the legitimate objective pursued by the Import Ban that falls within the purview of Article XX(b), and even goes against this objective, to however small a degree. Accordingly, we are of the view that the MERCOSUR exemption has resulted in the Import Ban being applied in a manner that constitutes arbitrary or unjustifiable discrimination.[78]

Therefore, the DSB once again ruled in this case based on an exception rule - article XX - and did not analyze MERCOSUR under Article XXIV.

Reference should also be made to another dispute brought to the DSB, which, despite not being ruled based on article XXIV, established further guidelines for

[77] *Brazil — Retreaded Tires.* AB Report adopted in 17 December 2007.
[78] *Brazil — Retreaded Tires.* AB Report.

interpreting the Enabling Clause and is therefore relevant for MERCOSUR. It is the *EC-GSP* case.[79]

The panel was established in 2003 to assess India's complaint against EC's regulation granting differentiated tariff preferences to developing countries under a GSP framework. India sustained that, under the European GSP, there were five specific subsystems, each with different tariff preferences and respective beneficiaries. India challenged specifically the EC Drug Arrangement alleging that it failed to comply with the MFN principle to the extent that some developing countries received additional tariff benefits and others did not. Basically, the DSB was requested to rule on the validity of the MFN principle in a GSP scheme.

The main provision of the Enabling Clause invoked by India was footnote 3 of Paragraph 2, which states that:

> "Preferential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences" shall be established observing "generalized, non-reciprocal and non discriminatory preferences beneficial to the developing countries".[80]

According to India, the discrimination against it under the European GSP scheme was inconsistent with the Enabling Clause.

The AB interpreted such provision of the Enabling Clause based on the preamble to the WTO pursuant to which first "there is a need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth of international trade *commensurate* with the needs of their economic development", and second WTO members shall "enhance the means for doing so in a manner consistent with their respective needs and concerns at *different* levels of economic development".[81]

The DSB ruled that, although the preamble to the WTO allows for differential treatment according to the different levels of Members economic development, such treatment should be granted pursuant to objective and positive standards. The DSB condemned European GSP by ruling that:

> "The term "non-discriminatory" in footnote 3 does not prohibit developed-country Members from granting different tariffs to products originating in different GSP beneficiaries, provided that such differential tariff treatment meets the remaining conditions in the Enabling Clause. In granting such differential tariff treatment, however, preference-granting countries are required, by virtue of the term "non-discriminatory", to ensure that identical treatment is available to all similarly-situated GSP beneficiaries, that is, to all GSP beneficiaries that have the "development, financial and trade needs" to which the treatment in question is intended to respond".[82]

Although the EC-GSP case is not directly related to MERCOSUR, it constitutes a relevant jurisprudence for such RTA since it is also legally founded in the Enabling Clause. The DSB ruling concerning this dispute may be a fundamental guideline for future MERCOSUR regulations, especially when establishing preferential arrangements with specific developing countries, under the South-South agreements framework, such as MERCOSUR-SACU and MERCOSUR India, which are analysed in section 5 below.

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[79] *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries.*

[80] Enabling Clause, formally known as "Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries" was adopted in 28 November 1979 as part of the Tokyo Round.

[81] Preamble of the Marrakesh Agreement Establishing the World Trade Organization.

[82] *EC-GSP* AB Report adopted in 7 April 2004.

Two major conclusions must be drawn in this section. One refers to the lack of official and definitive statements about MERCOSUR's compliance with WTO Law. Both the CRTA and the DSB had the possibility to express their opinions on the matter but failed to do so.

As a consequence of this first conclusion, a second and broader conclusion is inevitable. In more than 400 cases submitted to the DSB only *one* was directly assessed and ruled upon based on Article XXIV: the *Turkey-Textiles*.

As pointed out by Prazeres, one main reason for this absence of DSB rulings on RTA rules is due to a *glass rooftop syndrome.*[83] This means that a country avoids questioning other countries' RTA initiatives because it feels itself also involved in a potentially challengeable RTA. Evidence of this is that, since the *Turkey – Textile* case, no WTO Member has ever again questioned another Member for its involvement in a RTA.

Another structural reason for the absence of objective decisions, be it from the CRTA or from the DSB, is that WTO Members seem unwilling to clarify the interpretation and application of the RTA rules because such clarification could constrain today's most widespread foreign policy strategy in trade relations: the continuing expansion of RTAs. "In sum, if the ambiguity of RTA rules does not seem to interest any member, at the same time, it seems to interest all".[84]

Therefore, unless there is a turning point in the WTO's decision making processes – by the CRTA and the DSB – in matters concerning RTAs legal status, the worldwide phenomenon of RTA proliferation will carry on its path, which could ultimately, in a pessimistic scenario, put in jeopardy the entire multilateral trading system. The absence of a clear MERCOSUR status *vis-à-vis* the WTO rules is just another loose end of this great spaghetti bowl of RTAs.

3. The Legal Framework for the Management of Asymmetries

At the heart of the debate on asymmetries is the tension over trade between developed and developing countries at large. The discussion turns on the flexibilities that developing countries need to make up for the asymmetry in order to retain room for development. The debate also hinges on whether trade is a means to an end in or an end in itself; and if the analysis should be focused on how development occurs, rather than an analysis of how trade occurs, examining the role of trade within development processes.

In this debate, the multilateral trading system still manifests very clear indications of the North-South conflict[85] and this is directly reflected in the protracted tensions in relation to asymmetries between developed and developing countries, the Special and Differential Treatment (S&D), the Enabling Clause, and the Global System of Trade Preferences, as described below.

However, the actions in the multilateral system for reducing North-South asymmetries do not necessarily help reduce asymmetries among Southern countries. Such is the case with the promotion of South-South agreements through the Enabling Clause. While these South-South agreements are one of the 'remedies' to build up economic prowess and thus reduce asymmetries, they will in turn sow the seed that

[83] Prazeres, T. (2008). *A OMC e os Blocos Regionais*. São Paulo: Aduaneiras.
[84] Prazeres, T. (2008). *Op. cit.*
[85] Tussie, D. (2000). "Latin America in the World Trade System". Oxford Handbook of Latin American Economics. *Forthcoming.*

reproduces asymmetries within the southern partners if offsetting mechanisms are not incorporated into the process.

In this section, we analyse the multilateral framework for the management of asymmetries, in order to help reveal the context in which MERCOSUR is developing its internal and external agenda on asymmetries.

3.1. The Management of Asymmetries under the GATT[86]

At inception, developing countries that joined the GATT did so on the basis of sovereign determination; they were considered equal partners in the multilateral trading system, at least under the 1948-1955 GATT.[87] The only provision available to developing countries was Article XVIII, which enabled developing countries to derogate from their scheduled tariff commitments or implement non-tariff measures, such as quotas, in order to promote the setting up of certain industries in their territories, that is, the protection of infant industries.[88]

From then on, the number of developing countries participating in the GATT increased, also increasing awareness and accumulating pressure for more flexible rules accounting for the asymmetries of the system. Thus, S&D Treatment, understood as preferential treatment in favour of developing countries in every aspect of their trade relations, was born as a result of the coordinated diplomatic efforts meant to correct what they felt were inequalities in the post-Second World War system.[89] This development paradigm, pioneered by Latin America, India, Egypt and later supported by a wide array of countries from Asia and Africa, was based on the need to improve trading terms, reduce dependence on exportation of primary products, correct the volatility and imbalances in the balance of payments and industrialization by offering protection to infant industries and export subsidies, among other objectives.

In the following years, several S&D provisions were introduced in the GATT. Firstly, through the amendment to Article XVIII in the GATT Review Session of 1954-55. The new item (Article XVIII: B) offered flexibilities to developing countries so as to cope with difficulties in their balance of payments. As previously mentioned, later on, in 1965, the Kennedy Round introduced another measure of S&D in the drafting of Part IV to GATT, exempting developing countries from the requirement to offer reciprocity in trade negotiations. Additionally, over this period many developing countries joined the GATT under Article XXVI, which enabled them to evade the

[86] 4.2 and 4.2 sections of this article are based on Peixoto Batista, J. (2010). "Flexibilities for Developing Countries in Doha Round as à la carte Special and Differential Treatment: Retracing Uruguay Steps?, Serie Working paper, n. 126, LATN. Published online at: www.latn.org.ar.

[87] Kessie, E. (2000). "Enforceability of the Legal Provisions Relating to Special and Differential Treatment under the WTO Agreements". Paper presented at the WTO Seminar on Special and Differential Treatment for Developing Countries. 7 Mach 2000, Geneva, Switzerland.

[88] Singh, A. (2005). "Special and Differential treatment: The Multilateral Trading System and Economic Development in the Twenty-first Century", in Gallagher K. P. (ed.) *Putting Development First: The Importance of Policy Space in the WTO and IFIs*. London and New York: Zed Books.

[89] UNCTAD (2000), Training Tools for Multilateral Trade Negotiations: Special & Differential Treatment, Commercial Diplomacy Programme, document UNCTAD/DITC/Misc.35. Geneva: UNCTAD.

commitment to bind tariffs as part of their accession agreements[90], as detailed in the section 3.

Flexibilities in relation to negotiations on market access were deepened through the incorporation of the non-reciprocity provision (Art. XXXVI:8) in Part IV of GATT in 1964. Furthermore, a waiver was granted in 1971 for the Generalized System of Preferences (GSP).

In the Tokyo Round (1973-1979), the efforts of developing countries to consolidate the special treatment in their favour resulted in the Enabling Clause. In addition, the protocol on trade-related negotiations among 16 developing countries was introduced in the GATT, as waivers to Article I (MFN). The management of asymmetries thus reached the core of the multilateral trading system (Decision L/4903, adopted in 1979). It is worth noting that this achievement is closely related with the action of the Group of 77, and the United Nations Conference on Trade and Development (UNCTAD). In fact, with the help of UNCTAD, developing countries summarized their position on the Tokyo Round codes and rephrased the battle, led by especially by Brazil, Egypt, India, and the former Yugoslavia. Since then, the treatment of asymmetries was carried out in different *fora*. The precedent of the Enabling Clause and the treatment embodied in the GATT/WTO remained the ground from which developing countries tried to make strides to defend their interests in trade negotiations.

3.2. The Shift towards the WTO and the Current Doha Round

The Marrakech agreement turned out to be an unbalanced package. The greater participation of developing countries was not linked to more favourable results.[91] The outcome of the Uruguay Round was markedly uneven in favour of developed countries and dealt a hard blow to the treatment of asymmetries in the WTO rules. There was no consensus among developing countries for the adoption of a general "umbrella" framework for S&D provisions, although there were few chances for resistance at a time when the Soviet empire was crumbling and the neoliberal agenda was gaining momentum. Developing countries were torn in the dilemma: would they accept all the rules and obligations resulting from the negotiation or would they remain outside the organization?[92] As a matter of fact, the single undertaking caused developing countries and developed countries to assume very similar undertakings[93], based on rules widely biased in favour of conditions of competition in developed countries. These became standard benchmarks.

The treatment of asymmetries was changed though a restricted concept of S&D[94]; it was a reflection of the unwillingness on the part of developed countries to continue granting special treatment at large, particularly to middle-income countries.

[90] Such was the case of Argentina which joined the GATT at the end of the Kennedy Round, when the negotiations in the United Nations Conference on Trade and Development (UNCTAD) were still in full swing.

[91] Tussie, D. and Lengyel, M. (1999). "Developing Countries and the WTO: Participation versus Influence". World Bank.

[92] Tempone, E. (2007). "Los dilemas institucionales de la OMC: comentarios sobre el Informe Sutherland". Agenda Internacional, Año XIV no. 25. Buenos Aires.

[93] Fukasaku, H. (2000). "Special and Differential Treatment for Developing Countries: Does It Help Those Who Help Themseleves?", Working Paper n. 197 (Brugge: World Institute for Development Economic Research, The United Nations University.

[94] About the difference between S&D before and after the Uruguay Round, see Whalley, J., 1999.

This is evidenced by the express implementation of graduation mechanisms, similar to what was already being unilaterally done with GSP beneficiaries. The focus was then shifted towards the Least Developed Countries (LDCs), as already contemplated in the general framework of the multilateral system, Article XI: 2 of the WTO Agreement.

Clearly, the WTO's evolution towards the inclusion of beyond-the-borders issues was not accompanied by a similar evolution of the instruments to deal with that. In most cases, texts contain vague, ambiguous and general S&D provisions. In the agreements currently in effect, the only S&D provisions clearly establishing rights and obligations enforceable against the dispute resolution system are those related to longer transition periods for implementation of obligations; and flexibility with some obligations and procedures, in addition to certain provisions on technical assistance.[95]

This is not enough if one considers the significant implications of multilateral trade rules for developing economies, as there are no S&D provisions capable of overcoming the anti-development impact of several provisions in multilateral agreements, such as TRIPs, TRIMs, and the Agreement on Subsidies, which at times seem to invert the reasoning and grant special treatment to developed countries.[96] In short, the main idea behind the treatment of asymmetries through S&D seems to involve merely affording room for adjustment and implementation of the new, controversial rules; a far cry from a genuine concern for the development.

However, that debate, which seemed to be living on borrowed time, gained relevance once again, in the years following implementation of the Marrakech agreements, when many developing countries became fully aware of how biased Uruguay Round (UR) agreements were in favour of developed countries. For their part, the US and the European Union wanted to continue moving forward in the advancement of the Marrakech agreements, and with that in mind they proposed a new round. Developing countries, on the other hand, unhappy with the outcome of the UR that did little for their development needs, accepted the offer, subject to prior exclusion of such issues as employment, and under the condition that the mandate of the new round should be as comprehensive as possible to include their interests and development needs.[97]

Thus, the Doha Development Round was launched in 2001 at the Doha Ministerial Conference, in the aftermath of the 9-11 terrorist attacks. The Doha Declaration, paragraph 44, provided that S&D provisions are part of WTO Agreements and that particular attention will be paid to them, in an effort to reinforce them and make them more accurate, effective, and operational.

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[95] For considerations on the binding effect of S&DT provisions, see Kessie (2000). Additionally, other authors have classified the S&DT provisions contained in the Marrakech agreements. See Fukusaku H., op. cit.; Hoeckman, B (2005). "Operationalizing the Concept of Policy Space in the WTO: Beyond Special and Differential Treatment". Journal of International Economic Law. Vol 8, No. 2, pp. 405-424. Oxford University Press; Kleen, P. and Page, S. (2004). "Special and Differential Treatment of Developing Countries in the World Trade Organization". Serie Global Development Studies no. 2, EGDI Secretariat- Ministry for Foreign Affairs, Sweden-Overseas Development Institute.
(2000); Hoekman (2005), Kleen & Page (2004), among others. In turn, the WTO has also established a classification. For WTO jurisprudence on binding provisions in WTO agreements, see, for example, India-US dispute regarding Art. 15 of the Antidumping Agreement (DS206, 7.111)

[96] Some examples of the referred bias in the special treatment afforded to developed countries include quotas on textiles, agricultural subsidies, the agreement on subsidies (where the subsidies allowed are adequate for industrialized countries), or the restrictions on the competition policy allowed under the TRIPs Agreement. See Singh, A., op. cit.

[97] Steinberg, R. (2002). "In the Shadow of Law or Power? Consensus-Based Bargaining and Outcomes in the GATT/WTO". International Organization 56, 2.

From then on, S&D continued moving forward along two related paths. The first one involved the commitments already undertaken at the UR and their development, which in practice meant an important restriction in the S&D universe of application and their beneficiaries. The other path moved around the declarations and negotiations under way in the Doha Round.

Regarding the commitments already undertaken at the UR -such as the Agreement on Subsidies and Countervailing Measures (SCM), the Agreement on Trade-Related Investment Measures (TRIMs), and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs)-, an increasing restriction on the flexibilities for developing countries is observed. In fact, the S&D provisions of the Uruguay Round have been subject to an increasingly restrictive interpretation and have failed to have the expected impact on the development agenda. Those agreements have a tendency to restrict, in practice, S&D provisions to LDCs and, to a lesser extent, to other developing countries in a less advantageous situation, excluding most developing countries, especially large and emerging economies and middle-income countries. [98]

Moreover, in the negotiations currently under way, the initial S&D agenda in the Committee on Trade and Development (in special session) when the Doha Round was launched was ample and comprehensive —mandatory or non-mandatory nature of provisions and their consequences; S&D principles and objectives; technical and financial assistance and training of capacities; S&D incorporation into WTO rule structure. However, currently this agenda is limited to implementation of measures in favour of LDCs, a surveillance mechanism, and some S&D proposals for specific agreements, while all other aspects that were being discussed at the beginning of the Round at the CTD seem to have been lost along the way.[99]

Meanwhile, developing countries, especially those excluded from the benefits of general flexibilities in the WTO, are trying to find ways to keep resorting to measures that, on one hand, recognize the existing asymmetries between developed and developing countries, and, on the other, allow them to maintain their development strategies in order to reduce these asymmetries. In fact, in the Doha Round negotiations, developing countries - with the help of their new coalitions such as NAMA 11, G-33 and G-20, G90 etc - have been fighting for flexibilities on each issue of critical importance to them, such as agriculture and Non-Agricultural Market Access (NAMA), and have thus obtained certain flexibilities matching their respective trade interests.[100]

The negotiation of the flexibilities on these modalities responds to a liberalization criterion for "less than full reciprocity", to respond to the more general requirements of the Development Round, and the balance between agriculture and NAMA, set forth in paragraph 24 of Hong Kong, and each country or group of countries is negotiating its particular and additional flexibilities. That is the case of

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[98] For details on specific agreements, see Peixoto Batista, J. (2005). "De Uruguay a Doha: prorrogas, plazos y renegociaciones", serie Brief LATN, n. 23, octubre. Published online at: www.latn.org.ar

[99] See WTO Committee on Trade and Development reports, from 2002 to 2008, available at: http://docsonline.wto.org

[100] See Narlikar, A. (2003). *International Trade and Developing Countries: Bargaining coalitions in the GATT & WTO*. London: Routledge; Tussie, D. and Narlikar, A. (2004) "The G20 at the Cancun Ministerial: Developing Countries and their Evolving Coalitions in the WTO". *The World Economy*, Vol. 27, July; Uzquiza, L. G. (2009). "Crisis y estancamiento negociador: cuando el todo es más que la suma de las partes", LATN Working Paper, n. 107, july. Published online at: www.latn.org.ar; Diego-Fernández, M. (2008). "Trade negotiations make strange bedfellows", World Trade Review, vol. 7/02, april. pp. 423-453, among others.

MERCOSUR, for instance, which is negotiating a list of exceptions that will not be included in the tariff reduction.

3.3. South-South Arrangements: The Global System of Trade Preferences among Developing Countries

As mentioned above, one of the most important achievements with regard to the management of asymmetries is, undoubtedly, the 1979 Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries", which is known as the "Enabling Clause". The Enabling Clause comprises: (a) the Generalized System of Preferences; (b) Non-tariff measures in GATT instruments; (c) Global or regional arrangements among developing countries, and (d) Special treatment to LDCs. For the purpose of this paper, special attention will be paid to item (c), which covers South-South arrangements.

First of all, it is worth noting that the Enabling Clause authorizes preferential trade arrangements among developing and least-developed countries as a departure from the WTO's "most-favoured nation" principle. This exception to the general rule allowed developing countries to continue old regional integration initiatives build new ones which were not fully fledged free trade areas or custom unions as required by the more stringent criteria of Article XXIV -such as LAIA, CAN, and MERCOSUR[101]– as well as global initiatives, such as the Global System of Trade Preferences among Developing Countries (GSTP).

The Global System of Trade Preferences among Developing Countries (GSTP) was established in 1988 as an arena for developing countries to exchange trade preferences, so as to promote trade among them. This idea, however, dates back to over a decade before (1976), at the ministerial meeting of the Group of 77 in Mexico City. Subsequently, the idea was gradually developed at the ministerial meetings of the Group of 77 (G77) in Arusha (1979) and Caracas (1981). In 1982 in New York, the Foreign Affairs Ministers of G77 defined the basic components of the agreement and established a framework for negotiations. In 1984, in Geneva, the G77 began the preliminary work on the various aspects of a structural agreement. In 1986, at the ministerial meeting in Brasilia, the provisional structure of the agreement was established and the first negotiation round was launched. In 1988, the final text of the agreement was adopted –which came into force in 1989- and the first negotiation round was completed in Belgrade.

According to the Belgrade Agreement economic cooperation among developing countries is a key element in the strategy of collective self-reliance and an essential instrument to promote structural changes contributing to a balanced and equitable process of global economic development. In this sense, the GSTP aims at including all products, manufactures, and commodities in their raw, semi-processed and processed forms. It consists of the arrangements on tariffs, para-tariffs, non-tariff measures, direct trade measures including medium and long-term contracts, and sectoral agreements, and is reserved to the exclusive participation of developing countries members of the G77. In addition, the GSTP shall complement – not replace

[101] As mentioned in the Section 3.6., the MERCOSUR agreement was submitted for revision under Art XXIV as well as under the Enabling Clause which gave legal cover to the host of preferential schemes that used the ALADI umbrella as explained in section 2 of this article.

– economic groups of G-77 developing countries members, being them regional, sub regional or interregional groups (Art. 18, GSTP).

The Agreement establishes a Committee of Participants, which is composed of representatives from the participant countries. The Committee is in charge of the functioning of the GSTP, contributing for the achievement of its objectives.

The GSTP negotiation takes into account the limitations of developing countries and moves on a step-by-step basis, admitting negotiations to be conducted on a bilateral, plurilateral, or multilateral basis, with a "product-by-product", "across-the-board tariff reduction" or "sectoral" approach. In these lines, the first lists of concessions were quite modest.[102]

Over the 90s with the sway of neoliberal trade policies and the establishment of the WTO, the GSTP presented modest improvements, which became manifest in the second negotiation round[103], results from which were not ratified by the participants.

In the following decade, however, new factors came into play and the GSTP was reborn with new strength by the consolidation of Brazil and India as speakers for the developing world, devoted to highlighting South-South relations in the construction of the new geography of trade. The third round of GSTP negotiations was then launched in São Paulo in 2004, during the 11th Session Period of UNCTAD. In order to encourage participation, the MFN clause in the GSTP, which stated that the results of each round were applicable to all the participants in the agreement, was abolished by the Committee of Participants.[104]

The GSTP consists of 43 members[105], although only 22 of them have chosen to participate in the current round of concessions.[106] The São Paulo Declaration calls for a "package of substantial liberalization commitments on the basis of mutuality of advantages in such a way as to benefit equitably all GSTP participants". In addition, although 22 countries participated in the current round, only 19 finally adopted the agreement.[107] Neither China nor South Africa is current members of the GSTP.[108] MERCOSUR has been participating as a group since 2006,[109]and India, since GSTP's beginnings.

In 2008, in Ghana, countries acknowledged the importance of GSTP negotiations and committed themselves "to act quickly to conclude the

[102] Approximately 1800 preferences were exchanged, from which 900 were effectively applied (Fossati, V. and Levit, L., op. cit.)

[103] Tehran Declaration on the Launching of the Second Round of Negotiations Within the GSTP, 1992. Available online at: http://www.unctadxi.org/templates/Page____6342.aspx

[104] Fossati, V. and Levit, L. (2010). "El sistema global de preferencias comerciales entre países em dsarrollo: Una oportunidad para el comercio exterior argentino", Revista del CEI, n. 17, Abril, Buenos Aires.

[105] Algeria, Angola, Argentina, Bangladesh, Benin, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Egypt, Ghana, Guinea, Guyana, Haiti, India, Indonesia, Iran, Iraq, Lebanon, Malaysia, Mexico, Morocco, Mozambique, Nicaragua, Nigeria, North Korea, Pakistan, Peru, Philippines, Paraguay, Qatar, Romania, Singapore, South Korea, Sri Lanka, Sudan, Tanzania, Thailand, Trinidad and Tobago, Tunisia, Uruguay, Venezuela, Vietnam, (ex)Yugoslavia, Zaire, and Zimbabwe.

[106] Algeria, Argentina, Brazil, Chile, Cuba, Egypt, India, Indonesia, Iran, Malaysia, Mexico, Morocco, Nigeria, North Korea, Pakistan, Paraguay, South Korea, Sri Lanka, Thailand, Uruguay, Vietnam, and Zimbabwe.

[107] Chile, Mexico and Thailand participated in negotiations, but decided not to sign the agreement.

[108] ICTSD (2009). "Developing Countries Close to Deal to Boost South-South Trade" in Bridges Weekly Trade News Digest, volume 13, number 41. ICTSD: Geneva, 25 November.

[109] Argentina and Brazil have been members since 1990 and 1991, respectively (CEI, 2010)

negotiations".[110] In December 2009, in Geneva, countries adopted the ministerial decision on modalities that establish tariff cuts on at least 70 percent of participants' dutiable tariff lines, and a possible conclusion of the round is expected by the end of 2010.[111]

The significance of GSTP trade is a matter of discussion, and some positive and negative aspects can be detailed. Pessimistic views stress that the market access negotiated under the GSTP is not economically significant in comparison to autonomous liberalization, or to tariff cuts arising from regional agreements or the WTO.[112] Besides, over half the projected increases in intra-GSTP trade would arise from trade diversion.[113]

Optimistic views highlight that the GSTP has significant potential, since exports from GSTP members to the rest of the world represents almost 14% of global exports.[114] Moreover, intra-GSTP exports and imports consist of 18% and 19.4% of GSTP exports and imports to the rest of the world.[115] In addition, it is stressed that GSTP represents an actual improvement in market access since the bases for tariff cuts are the applied tariffs, rather than the WTO bound tariffs. UNCTAD also provides some evidence of the fast growth of intra-GSTP; the increasing level of export complementarities among GSTP countries; the capacity of intra-GSTP tariff cuts to enhance exports among GSTP members within each region, as well as inter-regionally. Also, the volume of trade within the bloc seems to have shifted to capital goods from more basic commodities, and trade within GSTP has been created, rather than simply been diverted, from more efficient sources.[116]

Regardless of the studies on the limitations and opportunities of the GSTP, it is still an important stage in the confirmation of the relevance of South-South trade for developing countries to depend less on the markets of developed countries.

Regarding the asymmetries among the developing countries participating in the agreement, GSTP benefits are less clear. In the agreements and declarations approved to date, this issue is contemplated differently. Firstly, according to Article 3, f, of the Belgrade Agreement of 1988, the special needs of the least developed countries (LDCs) shall be clearly recognized and concrete preferential measures in favour of these countries should be agreed upon; the least developed countries will not be required to make concessions on a reciprocal basis.

Besides, Article 17 (Special Treatment for LDCs) states that LDCs shall not be required to make concessions and shall benefit from all tariff, para-tariff or non-tariff concessions which are multilateralized, and that they can seek technical assistance from the United Nations in order to identify the export products for which they may wish to seek concessions in the market of other participants. They may also make

[110] Joint Communiqué, Special Session of the Committee of Participants at Ministerial Level, Accra, Ghana, 22 April 2008 (GSTP/CP/SSG/2)

[111] Ministerial Decision on Modalities, Sao Paulo Round of the Global System of Trade Preferences Among Developing Countries, Geneva, 2 December 2009 (SPR/NC/MN/1)

[112] Oxfam. (2004). "Oxfam Background Briefing on South-South Trade and GSTP", June. Available online at: http://www.oxfam.org.uk/resources/policy/trade/downloads/south_trade.pdf

[113] UNCTAD. (2005). "GSTP Trade: Current Trends and Implications of Intra-GSTP Tariff Reductions". Power point presentation. Available online at: http://www.unctadxi.org/Secured/GSTP/Articles/GSTPPresentationPuri.ppt

[114] Fossati, V. and Levit, L., op. cit.

[115] Idem.

[116] Fossati, V. and Levit, L. op. cit.; Endoh, M. (2005). "The effects of the GSTP on trade flow: mission accomplished?", was published in the Journal of Applied Economics, 37, 487-496.

specific requests to other participants for concessions and direct trade measures, including long-term contracts.

The GSTP Agreement requires that special attention be paid to the application of safeguards regarding exports from LDCs, and establishes a special rule of origin for LDCs - Rule 10, Annex 2- with regard to products not wholly produced or obtained in those countries and cumulative rules of origin.

Finally, Annex III encourages participants to adopt additional measures in favour of LDCs: technical assistance and co-operation arrangements designed to assist LDCs in issues such as the establishment of industrial and agricultural projects, formulation of export promotion strategies, training, and joint ventures, among others.

In the following years, the special treatment to LDCs was reaffirmed in the São Paulo Declaration Launching the Third Round (2004), the Accra Joint Communiqué (2008), and the Ministerial Decision on Modalities.[117] Bearing in mind that this is the first time that actual progress is observed in GSTP negotiations, a matter pending consideration is whether the special treatment to LDCs will in fact be applied or not. In any case, the GSTP does not generally advance in foreseeing asymmetries among non-LDC developing countries. Considering the diverse economies present in this round of negotiations, this will call for an important effort for cooperation, technology transfer, and other measures seeking to prevent concentration and polarization effects once the preferences have been put into practice and if the range of products covered by the GSTP increases.

In consideration of the foregoing, it is worth bearing in mind that the GSTP can play a crucial role in the *new geography of trade*, helping to promote trade otherwise neglected in multilateral negotiations and by the same token contribute to some extent to level the playing field. Furthermore, the agreement contains comprehensive provisions on the special treatment to LDCs that acknowledge non-reciprocity, flexibilities in rules of origin, cooperation to encourage the promotion of exports, the establishment of agricultural and industrial sectors, among others. This, however, does not rule out certain risks in relation to the asymmetries among non-LDC developing countries. While the GSTP has a gradual (step-by-step) approach – which enables handling asymmetries through the exclusion of sensitive sectors-, it is not enough to face asymmetries as the universe of preferences is broadened.

4. Regionalism in South America and the Dilemmas whithin MERCOSUR

The situation of South American integration has changed considerably in the last twenty years. In a time of renovating regionalisms in South America, some trade integration processes – such as the Andean Community of Nations (ACN) and the Southern Common Market (MERCOSUR) - coexist with a set of overarching initiatives throughout the entire subcontinent, in the context of the Latin American Integration Association (LAIA). Regional institution building has turned into a complex, multi-layered arena where contending political interests compete, a far cry

[117] Ministerial Decision on Modalities, Geneva, 2 December 2009. Available online at: http://www.unctadxi.org/Secured/GSTP/Declarations/sprncmm1.PDF

from a crystallized and conceptually neat project in the hands of a single uncontested leader.[118]

The region now faces the challenge of harmonising these phenomena or learning to live with the competing projects. This harmonisation depends on high doses of pragmatism enabling the advancement –under a single framework- of more pro-development initiatives coupled with some more liberal ones, so as to continue supporting regional integration as an alternative that adds value to national and bilateral policy options. The situation is in a state of flux, yet it is necessary to observe the latest developments of these initiatives in order to identify possible scenarios and, especially, to understand the relationship between the political overtones of current South American integration and the progress of South-South agreements.

MERCOSUR's internal agenda reflects those dilemmas. This section will analyse the situation of regional integration initiatives in the Southern Cone with the aim of unveiling the new regional geometry, and the challenges the MERCOSUR internal agenda – on services, investments and asymmetries - has to face in this context.

4.1. Open Regionalism Initiatives in South America in the Last Ten Years

In the course of the 90s, during the peak of the (neo) liberal ideas enshrined in the Washington Consensus, regional integration in South America built on previous initiatives so as to adapt them to open regionalism. This wave led to new region building initiatives. Thus, the MERCOSUR was born in 1991, and in addition the Andean Pact was amended and turned into the Andean Community of Nations (ACN) in 1992. Both initiatives fall under the Latin American Integration Association (LAIA) and have since then become the two axis of regional trade integration. These initiatives arose at a time of unbundling policies of import substitution. A feature of these projects was their grand ambition concerning trade in goods and services, investment protection, and the goal of establishing customs unions and common markets.

In fact, both initiatives progressed the most in terms of trade liberalisation.[119] However, although there was an initial success in terms of political consolidation of alliances and trade within blocks[120], by the mid-90's both initiatives lost lustre and faced a number of hurdles, worsened by successive crises as from the late 90's: Brazil's currency devaluation in early 1999, Argentina's meltdown in 2001, crises in Bolivia and Ecuador. The region faced a turning point.

In the case of MERCOSUR, following the 1994 establishment of a free trade zone, a customs union (imperfect), and the design and implementation of a definite

[118] Tussie, D. (2009). "Latin America: contrasting motivations for regional projects", Review of International Studies, Volume 35, Supplement S1, February, pp 169-188.

[119] ALADI/MERCOSUR/CAN/04 (2006). "Convergencia comercial de los países de América del Sur hacia la Comunidad Sudamericana de Naciones: Aranceles y Comercio en Sudamérica: análisis de la convergencia hacia el libre comercio". Published online at:http://www.mercosur.int/portal%20intermediario/es/publica/doc_temp_archivos/Convergencia5-%20Defensa%20comercial.pdf

[120] Botto, M. and Tussie, D. (2007). "De la rivalidad a la cooperación: Limites y desafíos de un contacto creciente". In: Hofmeister, W.; Rojas, F.; Solís, L.G. (comp.) La percepción de Brasil en el contexto Internacional: Perspectivas y desafíos, Tomo 1: América Latina, FLACSO/Konrad Adenauer Stiftung. 41-77; Souza, A. M. and Oliveira, I. T. M.; Gonçalves, S. S. (2010). "Integrando desiguais: asimetrias estruturais e políticas de integração no MERCOSUL", Paper for discussion, n. 1477, IPEA

institutional structure for the bloc, progress became increasingly hard to attain. The customs union was not fully completed[121]; commitments lost credibility as they were not internalized after joint approval; there was a multiplication of inter-sector conflicts that found no institutional channels for resolution. The divergence of macroeconomic policies aggravated tensions and became all too apparent when Brazil devalued its currency in January 1999, while Argentina remained bound to convertibility.

By then, the bloc showed a decrease in trade flows and investment, and an increase in trade-related disputes. The share of MERCOSUR in total trade fell steadily from 1997 to 2002.[122] The 2002 diagnosis of the bloc was that there was a mismatch between MERCOSUR rules and the reality they were supposed to regulate; that there were no institutions for preventing and forecasting problems that would channel and direct the implementation of 'pro-integration' actions, reducing vulnerability to internal political circumstances of member states; that MERCOSUR rules were too soft, particularly in relation to incentives and subsidies; and that there was a lack of effective intermediate stages for dispute resolution and negotiation.[123]

Some progress was made toward solving some of these problems, for example through approval of the Olivos Protocol for the settlement of disputes and the decision on the free movement of workers. In addition, MERCOSUR approved a Decision establishing that – since MERCOSUR was a Custom Union with legal entity - all agreements involving MERCOSUR should be signed by the bloc's four members.[124] However, these initiatives were isolated steps rather than part of a more comprehensive strategy in order to face obstacles and give a new direction to integration.

The ACN also advanced in the 90's, achieving full liberalisation of the goods market[125] and some institutional progress. As in the case of MERCOSUR, trade within the Andean region grew at a more dynamic rate than world trade during the 90's.[126] Furthermore, the institutional structure of the Community incorporated the Andean Presidential Council and the Andean Council of Foreign Affairs Ministers, included into the ACN's institutional structure. In the same sense, the Cartagena Agreement board was turned into a General Secretariat.

As in the case of MERCOSUR, by the mid-90's the ACN stumbled when faced with the challenge of deepening of trade integration and the adoption of the Common External Tariff (CET). The tensions were particularly acute in relation to the negotiation of agreements with developed countries. In this connection, disputes accumulated and trade lost steam. As rates of growth plunged, so did trade and investment flows.[127]

Briefly, although the generation of integration initiatives in the 90's made significant inroads in the liberalisation of trade in goods, they evidenced little progress in trade-related business disciplines, such as rules of origin, sanitary and phytosanitary

[121] On August 3rd, 2010 though, during its 39th Summit held in Argentina, MERCOSUR members seem to have eventually taken the steps towards the consolidation of the customs union, which is to be phased in over the next year and a half before fully taking effect in 2012. MERCOSUR members also decided to eliminate by 2012 the double recovery of the common external tariff.

[122] Souza, A. M. and Oliveira, I. T. M.; Gonçalves, S. S., op. Cit.

[123] Delich, V. and Peixoto Batista, J. (2010). "La agenda de integración regional de Argentina post-2001", UNCTAD, *forthcoming*

[124] Decision 32/2000, available at: www.mercosur.int

[125] LAIA/MERCOSUR/ACN, op.cit.

[126] INTAL-IADB (2005), Andean Report n. 1, 2002-2004, Buenos Aires.

[127] INTAL-IADB, op.cit.

measures, technical rules and regulations and customs procedures, and even less progress was made in disciplines not directly related to trade in goods, such as government procurement, intellectual property and specially services and investments. In view of the importance of services and investments rules to the deepening of the integration and/or cooperation processes involved in RTAs we now turn to highlight the way in which they have been regulated in MERCOSUR.

4.2. The trade in Services in MERCOSUR

The Protocol of Montevideo is an integral part of the Treaty of Asunción.[128] The liberalisation of trade in services was in the MERCOSUR agenda since the early stages of the integration process. In June 1992, MERCOSUR Common Market Council approved an ambitious working programme for the transition period, which determined the adoption of a number of measures aimed at the functioning of the common market by 31 December 1994. Some of these measures had the purpose of advancing the liberalisation of trade in services either by way of negotiating general obligations and disciplines or through the harmonisation of legislation or by adopting mutual recognition agreements for specific sectors.[129] However, it was not until November 1997 that the Protocol of Montevideo was enacted.[130] Additional time was required to complete the drafting of the sectoral annexes to the Protocol and for the negotiation of Member States' initial schedules of specific commitments.[131]

The Protocol of Montevideo, a RTA between four WTO Members, was designed in the light of the GATS, adopting most of its provisions without modifications. Pursuant to Article I, the purpose of the Protocol is to promote free trade services within MERCOSUR. Such purpose must be achieved in compliance with GATS' conditions for economic integration, which essentially require preferential agreements to have "substantial sectoral coverage" and to provide for the elimination of "substantially all discrimination". It seeks to consolidate in a single instrument a set of general rules and principles aimed at promoting free trade in services and ensuring the increasing participation of less developed countries and regions in the services market.[132]

The Protocol of Montevideo is, on one hand, a "negative integration contract", to use Mavroidis' words[133], i.e., it is primarily concerned with the elimination of discrimination without interfering with Member States' right to regulate in accordance

[128] In turn, as already mentioned, the Treaty of Asunción is part of a broader regional integration framework established by the Treaty of Montevideo (1980).
[129] Gari, G. (2009). *The liberalisation of Trade in Services in Mercosur*. London: Cameron. p. 105.
[130] Decision No. 13/97 (Protocol of Montevideo on MERCOSUR's Trade on Services).
[131] Decision No. 09/98 (Annexes to the Protocol and to the Initial Schedule of Commitments). The Protocol of Montevideo came into force after having been ratified by three Mercosur State-members, namely Argentina, Uruguay and Brazil.
[132] The reference to "the need to ensure the increasing participation of less developed countries and regions in the services market" was included in the Preamble to the Protocol, subject to reciprocity. "Indeed, "the latter part of the preamble's recital ("on the basis reciprocal rights and obligations"), waters down the impact that such reference could have on the development of an effective and non-reciprocal treatment in favour of less development countries and regions." Gari (2009), p. 109 (footnote 17).
[133] Mavroidis, P. (2007). "Highway XVI Re-visited: the Road from Non-Discrimination to Market Access in GATS. 6 *World Trade Review* 1, p. 11.

with their legitimate policy objectives and, on the other, an integration process whose ultimate objective is to liberalise the services sector.

Some scholars sustain that the liberalisation process combined with States-members' right to regulate, that is, the maintenance of their policy space to implement legitimate public policies regarding services sector and subsectors, would be a "blatant contradiction"[134] in the context of an integration process such as MERCOSUR. On the contrary, rather than a "blatant contradiction", it is concerned with a "balance", which is by all means necessary, especially when the asymmetries among MERCOSUR Member States are taken into consideration.

Under the Protocol, the Programme of Liberalisation on Trade in Services contains a mechanism for advancing trade liberalisation through the negotiation of specific commitments on market access and national treatment. Such a mechanism is based on the so-called "positive list" approach, which consists of a gradual liberalisation strategy by which State-members inscribe in national schedules of commitments the sectors in which they intend to make specific commitments on market access and national treatment.[135]

While under the GATS, the "positive list" approach is the mechanism which better fits into the progressive liberalisation strategy contained in Article XIX and is therefore the most appropriate to protect developing countries interests[136], there seems to be no reason to contend that it would not be equally the most appropriate to the MERCOSUR Programme of Liberalisation on Trade in Services, in view, as already highlighted, of the asymmetries among its Member States.

From a different perspective, Low and Mattoo[137] underscore the advantages of the "negative-list" approach (i.e., all services are covered and liberalised unless expressly excluded) over the "positive-list" one. In their view, among other reasons, a negative-list approach may generate a greater pro-liberalisation dynamic, as governments might be embarrassed by long list of exceptions. Moreover, such an approach would imply that any new services developed as a result of innovation or technological advancement, or for any other reason, would automatically be subject to established disciplines. In spite of this, they admit that this potentially liberalising argument may also be the one that makes governments cautious about adopting this approach.

Developing countries' governments should indeed be cautious about adopting such an approach *vis-à-vis* the negative listing, as the latter is much more prone to benefit developed countries, which, in the vast majority of cases, possess an organised, systematic and balanced domestic regulatory framework, which, incidentally, constitute a pre-condition for developing countries to participate in the liberalisation process of trade in services in a more active manner. It is true, however, that the negative listing mechanism has been adopted by numerous RTAs, such as

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[134] See Gari, G. (2009), p. 140.

[135] Pursuant to the Programme, State-members must hold successive rounds of negotiations aimed at the progressive inclusion of sectors, sub-sectors, activities and modes of supply of services in their schedules, as well as the reduction or elimination of trade-restrictive measures in order to ensure effective market access. After seven rounds of negotiations, due to the absence of political will, no more than a partial consolidation of the status quo of States-members' domestic legal systems has been achieved so far.

[136] See Celli, U. (2009). *Comércio de Serviços na OMC: liberalização, condições e desafios*. Curitiba: Juruá. p. 126.

[137] Low, P.; Mattoo, A. (2000). "Is there a Better Way? Alternative Approaches to Liberalisation under GATS", in Pierre Sauvé and Robert Stern M. (ed.), *GATS 2000: new directions in services trade liberalisation*. Washington, D.C. p. 467.

NAFTA, and bilateral agreements, such as Canada-Chile; Chile-Mexico; Bolivia-Mexico; Costa Rica-Mexico, among others.

In any event, the Protocol of Montevideo essentially reproduces GATS main characteristics, which favour developing countries: flexibility; progressive liberalisation through positive lists of specific commitments; the maintenance of Member States policy space to implement policies through the regulation of sector and sub-sector of services. As well as in the case of GATS, the essence of its framework and structure should remain unchanged.

This is especially important in the context of South/South cooperation agreements expected to be shortly entered into MERCOSUR and other developing countries.[138] In this regard, it should be noted that, while a number of countries and or regional blocs, due to the Doha Round negotiations stalemate, entered into numerous FTAs, MERCOSUR – despite certain periods of tension among its Member States – chose to keep firmly committed to the multilateral trading system. This policy seems to be now gradually changing. MERCOSUR/India and MERCOSUR/South Africa negotiations aimed at the formation of FTAs seem to be a clear signal of such a change.

4.3. Trade and Investments in MERCOSUR

In the MERCOSUR framework, there are two Protocols concerning Investments: one is the "Protocol of Colonia for the Reciprocal Promotion and Protection of Investments in MERCOSUR" (1994) and "the Protocol of Buenos Aires for the Promotion and Protection of Investments Originating from States non-Parties of MERCOSUR" (1995).

The Protocol of Colonia regulates or deals with intra-regional investments, i.e., investments made by investors from a Member State in another Member State. A broad concept of investment is adopted. It also contains rules on the entrance and establishment of capital, treatment, protection, transfer of funds, guarantees and disputes resolution, among others. In its turn, the Protocol of Buenos Aires was conceived with the purpose of harmonizing the treatment accorded by Member States to investments deriving from non-Member States. Neither of the Protocols is in force due the lack of ratification by the Member States.[139]

The table below shows the current status of the Protocols in the Member States:

Table 5: Current status of the Protocols in the Member States

	Argentina	*Brazil*	*Paraguay*	*Uruguay*
DEC. Nº 11/93 - Protocolo de Colonia para la Promoción y Protección Recíproca de Inversiones en el MERCOSUR. Firmado. Colonia del Sacramento, 17 de enero de 1994	Pending	Pending	Pending	Pending
DEC. Nº 11/94 - Protocolo sobre Promoción	L: 24554	Pending	L: 593	L: 17.531

[138] Mercosur signed with Chile (May 27, 2009), within the ALADI framework, its first agreement on services liberalisation. Negotiations with Colombia are well advanced.

[139] See Celli, U. (2005). "Acordos de Investimentos e Políticas Industriais", *in* Dreyzin de Klor, A.; Arroyo, D. F.; Pimentel, L.O. (Org.). (2005)., *Investimento Estrangeiro*. Revista DeCITA 03. Direito do Comércio Internacional: temas e atualidades. Florianópolis: Editora Fundação Boiteux. p. 117.

y Protección de Inversiones Provenientes de Estados No Partes del MERCOSUR. Firmado. Buenos Aires, 5 de agosto de 1994	D: 14-MAR- 96		15-JUN-95 D: 12-SET-95	9-AGO-02 D: 11-JUL-03

Source: Ministry of Foreign Relations of Paraguay 2010

Due to the absence of common rules on investments, Members have separate Bilateral Investment Treaties (BIT) BITs with different countries, as can be noted from the tables below:

Table 6: Argentina's BITs (57 agreements – 50 in force)

Agreement/Partner(s)	*Date of Signature*	*Entry into Force*
Algeria	04 October 2000	28 January 2002
Armenia	16 April 1993	20 December 1994
Australia	23 August 1995	11 January 1997
Austria	07 August 1992	01 January 1995
Belgium-Luxemburg	28 June 1990	20 May 1994
Bolivia	17 March 1994	01 May 1995
Bulgaria	21 September 1993	11 March 1997
Canada	05 November 1991	29 April 1993
Chile	02 August 1991	01 January 1995
China	05 November 1992	01 August 1994
Costa Rica	21 May 1997	01 May 2001
Croatia	02 December 1994	01 June 1996
Czech Republic	21 September 1996	
Denmark	06 November 1992	02 January 1995
Dominican Republic	16 March 2001	
Ecuador	18 February 1994	01 December 1995
Egypt	11 May 1992	03 December 1993
El Salvador	09 May 1996	08 January 1999
Finland	05 November 1993	03 May 1996
France	03 July 1991	03 March 1993
Germany	09 April 1991	08 November 1993
Greece	26 October 1999	
Guatemala	21 April 1998	07 December 2002
Hungary	05 February 1993	01 October 1997
India	20 August 1999	12 August 2002
Indonesia	07 November 1995	
Israel	23 June 1995	10 April 1997
Italy	22 May 1990	14 October 1993
Jamaica	08 February 1994	01 December 1995
Korea	17 May 1994	24 Setember 1996
Lithuania	14 March 1996	01 Setember 1998
Malaysia	06 Setember 1994	20 March 1996
Mexico	13 November 1996	22 July 1998
Morocco	13 June 1996	19 February 2000
Netherlands	02 October 1992	01 October 1994
New Zealand	27 August 1999	
Nicaragua	10 August 1998	01 February 2001
Panama	10 May 1996	22 June 1998
Peru	10 November 1994	24 October 1996
Philippines	20 September 1999	01 January 2002

Poland	31 July 1991	01 September 1992
Portugal	06 October 1994	03 May 1996
Romania	29 July 1993	01 May 1995
Russia	20 November 2000	
Senegal	06 April 1993	
South Africa	23 July 1998	01 January 2001
Spain	03 October 1991	28 September 1992
Sweden	22 November 1991	28 September 1992
Switzerland	12 April 1991	06 November 1992
Thailand	18 February 2000	07 March 2002
Tunisia	17 June 1992	23 January 1995
Turkey	08 May 1992	01 May 1995
Ukraine	09 August 1995	06 May 1997
United Kingdom	11 December 1990	19 February 1993
United States	14 November 1991	20 October 1994
Venezuela	16 November 1993	01 July 1995
Vietnam	03 June 1996	01 June 1997

Source: OAS SICE 2010

Table 7: Brazil's BITs (13 agreements – 1 in force)

Agreement/Partner(s)	*Date of Signature*	*Entry into Force*
Chile	22 March 1994	
Denmark	04 May 1995	
Finland	28 March 1995	
France	21 March 1995	
Germany	21 September 1995	
Italy	03 April 1995	
Korea	01 September 1995	
Netherlands	25 November 1998	
Paraguay	27 October 1956	06 September 1957
Portugal	09 February 1994	
Switzerland	11 November 1994	
United Kingdom	19 July 1994	
Venezuela	04 July 1995	

Source: OAS SICE 2010

Table 8: Paraguay's BITs (28 agreements – 26 in force)

Agreement/Partner(s)	*Date of Signature*	*Entry into Force*
Argentina	20 July 1967	03 October 1969
Austria	13 August 1993	01 December 1999
Belgium/ Luxemburg	06 October 1992	09 January 2004
Bolivia	04 May 2001	04 September 2003
Brazil	27 October 1956	06 September 1957
Chile	07 August 1995	17 December 1996
Costa Rica	29 January 1998	25 May 2001
Czech Republic	21 October 1998	24 March 2000
Denmark	22 April 1993	
Ecuador	28 January 1994	18 September 1995
El Salvador	30 January 1998	08 November 1998
France	30 November 1978	01 December 1980
Germany	11 August 1993	03 July 1998
Hungary	01 August 1993	01 February 1995

Italy	15 July 1999	
Korea	22 December 1992	06 August 1993
Netherlands	29 October 1992	01 August 1994
Peru	31 January 1994	13 December 1994
Portugal	25 November 1999	03 November 2001
Rumania	21 May 1994	03 April 1995
South Africa	03 April 1974	16 agosto 1974
Spain	11 October 1993	22 November 1996
Switzerland	31 January 1992	28 September 1992
United Kingdom	04 June 1981	23 April 1992
Exchange of Notes	17 June 1993	13 June 1997
United States	24 September 1992	19 May 1993
Uruguay	25 March 1976	01 July 1976
Venezuela	05 May 1996	14 November 1997

Source: OAS SICE 2010

Table 9: Uruguay's BITs (26 agreements – 20 in force)

Agreement/Partner(s)	*Date of Signature*	*Entry into Force*
Armenia		
Australia	01 September 2001	
Belgium-Luxemburg	04 November 1991	23 April 1999
Bolivia	03 March 2000	
Canada	16 May 1991	02 June 1999
Chile	20 October 1995	10 February 1999
China		01 December 1997
Czech Republic	26 September 1996	29 December 2000
El Salvador	24 August 2000	23 June 2003
France	14 October 1993	09 July 1997
Germany		29 June 1990
Hungary		01 July 1992
Israel	30 March 1998	07 October 2004
Malaysia	09 August 1995	
Mexico	30 June 1999	07 July 2002
Netherlands	22 September 1988	01 August 1991
Panama	18 February 1998	14 April 2002
Poland	02 August 1991	21 October 1994
Portugal	25 July 1997	03 November 1999
Romania	23 November 1990	30 August 1993
Spain	07 April 1992	06 May 1994
Sweden	17 June 1997	01 December 1999
Switzerland	07 October 1988	22 April 1991
United Kingdom	21 October 1991	
United States	25 October 2004	11 April 2002
Venezuela		18 January 2002

Source: OAS SICE 2010

As well as with the trade in services, investment provisions will be part of RTAs[140] with developed countries and/or cooperation agreements with developing countries (regardless of their modality) under the Enabling Clause and/or UNCTAD SGP that might be signed by MERCOSUR in the forthcoming years. The question arises as to how MERCOSUR can negotiate such agreements without having common rules on investments, i.e., intra-regional investments rules, and harmonized rules on treatment accorded by Member States to investments deriving from non-Member States. It is indeed a very complex and complicated normative situation.

Member States can no longer postpone the ratification of both Protocols.[141] Once they have been ratified, Member States will be better prepared to negotiate RTAs and South/South cooperation agreements. The greatest challenge will be though to negotiate agreements, whose investment provisions contain a necessary balance between the need to attract, promote and protect foreign investments and preserve Member States policy space to implement industrial policies aimed at their development.

4.4. The "re-launch" of South American Integration processes

The loss of steam of South American integration processes came about at the time that serious questions about globalization were raised in many quarters. While Europeans voted against the Lisbon Treaty, a new mindset seemed to take shape as exemplified by Dani Rodrik's book: "Has globalization gone too far?".[142]

In this context, the advent of the so-called "New Left" governments in the region played a decisive role in the review of South American integration processes. This seems to be the response of a region to two closely intertwined sets of challenges: increasing mass mobilization, and widespread public opinion against neoliberal reforms. Both reactions reflected strong dissatisfaction with the results of reform strategies; for having failed to generate high growth levels, for not having included politically excluded groups, and for their inability to promote more equitable models of income distribution.[143] This perception of having paid a high price for such modest results gave new air to already existing blocs.

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[140] Reference could also be made to the Preferential Trade and Investment Agreements (PTIAs), and notably of economic integration agreements (EIAs). EIAs today also increasingly address investment issues, thus forming a special category of International Investment Agreements (IIAs). According to UNCTAD, if they include investment provisions, they are referred by UNCTAD as economic integration investment agreements or PTIAs. By the end of 2007, there were 254 of such agreements. Investment provisions in PTIAs may be narrow or extensive and may address issues related to promotion, protection, liberalization and other investment related and important rules, such as competition policy. In many aspects, therefore, investment provisions in PTIAs are similar to provisions in BITs. In fact, BITs have influenced the investment provisions of many PTIAs (UNCTAD, 2009, p. 61) (See *The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries*, UNCTAD Series on International Investment Policies for Development. New York/Geneva: United Nations, 2009)

[141] This will be no easy task either. Under the Protocol of Buenos Aires, for example, disputes are to be solved by the ICSID to which Brazil is not a party as it did not sign the Washington Convention (1965).

[142] Rodrik, D. (1997). *Has the Globalization Gone Too Far?.* Washington D.C.,Peterson Institute of International Economics:

[143] Tussie, D. and Heidrich, P. (2006). "América Latina: ¿Vuelta al pasado estatista-proteccionista o en la senda de políticas de consenso democrático?", Foreign Affairs en español, april-june. Available at: www.foreignaffairs-esp.org

MERCOSUR and ACN were then 're-launched' under the paradigm of the so-called post-commercial or post-liberal regionalism, with a strong pro-development tone, a concern for maintaining policy spaces and the consideration for the distributional impacts of trade liberalization. Additionally, post-liberal regionalism[144] questions the exclusively commercial nature of the preceding integration processes and attempts to include the sectors/players excluded from the process during the nineties. The integration agenda must then be extended to include social and political issues, and the trade dimension must comprise such items as structural and policy asymmetries.

Triggered by the boom in economic growth experienced by the subcontinent as from 2003, MERCOSUR was then 're-launched' once again at the Asunción Summit held by mid-2003, with Néstor Kirchner and Lula da Silva as heads of government in Argentina (2003-2007) and Brazil (2003-2007), and with the participation of Bolivia, Chile, and Venezuela as guest countries. The *de facto* macroeconomic convergence between the two largest partners -Argentina and Brazil- contributed a good feeling factor.

In line with the new paradigm, there was a declaration on the need to deepen the so-called 'political MERCOSUR', moving forward with the instruments that would go beyond trade integration, and incorporating such issues as democratic commitment, social and labour arrangements, freedom of residence and work for individuals, employment growth, human rights protection, cultural promotion, involvement of civil society organizations, among others.[145] In terms of the economic-commercial agenda, new initiatives were launched, such as the Fund for MERCOSUR's Economic Convergence (FOCEM), the Program for Small and Medium Enterprises (MERCOSUR Pymes) and the decisions on productive complementation. The process seemed to have finally found a suitable political environment on which to thrive. In this context, the concern about the distributive effects of liberalization led governments to re-consider the direction taken for the treatment of asymmetries among MERCOSUR member states, to make it part of the core initiatives in the bloc's economic agenda, as will be explained below.

The ACN, in turn, also attempted to go beyond trade-related matters, including in its agenda such issues as the environment, social cohesion, citizen participation, movement of persons, among others. In 2003, member countries agreed that the bloc's mandate would include the generation of an Integrated Social Development Plan, which was drafted and approved in 2004.[146] Additionally, the Andean Integration System (AIS) created supranational organizations, which reflected the intention to consolidate supranationalism in the Andean bloc, asserting the objective of establishing a Common Market in the short run.[147]

Encouraged by a favourable political scenario, in 2004, MERCOSUR and ACN signed a memorandum of understanding intended to find common ground for promotion of a fuller integration between the two blocs. Since the beginning, this understanding between the two initiatives had to face both legal and commercial

[144] Rios, S. P. and Veiga, P. M. (2007). "O regionalismo pós-liberal na América do Sul: origens, iniciativas e dilemas", International Trade Serie, n. 82, International Trade and Integration Division, ECLAC.

[145] MERCOSUR 2004–2006 Work Program, Decision 26/03, available at: www.mercosur.int

[146] Decision 601, 2004. Available at: http://www.comunidadandina.org/NORMATIVA/DEC/D601.HTM

[147] The initial deadline for the establishing of a Common Market was 2005. Since then, the deadline has been postponed.

challenges –given the management of overlapping preferences- and political challenges, such as tensions among members of the two blocs.

Regarding preferential treatment, as early as 2000, ACN and MERCOSUR had moved forward in the execution of Partial Scope Agreements under LAIA, wherein trade preferences were established. In 2002, they signed an Economic Complementation Agreement (ECA) that required the formation of the free trade area in December 2003, a deadline which was not achieved. The original idea was to have "bloc to bloc" negotiations between MERCOSUR and the ACN. In time, as differences arose in the ACN, the negotiation gradually turned into a bilateral one (MERCOSUR and each of the Andean Community members). These agreements were formalized through the ECA under the Latin American Integration Association, and their primary purpose is to incorporate the bilateral preferences already existing among those countries under LAIA, to later establish a liberalization schedule for the rest of the products. Notwithstanding these bilateral achievements, the idea of unifying the region under a free trade zone did not progress.

The lack of political consensus led to tense moments among ACN members. In 2006, the different political views about the direction to be taken by ACN and the heterogeneous commercial interests resulted in Colombia and Peru negotiating FTAs with the United States, while Venezuela, in protest, decided to withdraw from the bloc and become a full member of MERCOSUR[148], which represents an additional challenge for the convergence of the two blocs.

The withdrawal of Venezuela and the execution of the FTAs posed an enormous challenge to CAN in terms of advancing its integration process. Firstly, Colombia-Venezuela are sub regional hubs and their mutual trade is an engine in the sub-region. On the other hand, the FTAs implied discarding the CET, elimination of the Colombian automotive program, elimination of the price range used by Peru, protection of test data in intellectual property, among others. In summary, the execution of FTAs, by deepening trade relations under bilateral agreements, reduces the room for advancement of the regional scheme.[149]

The arrival of Venezuela in MERCOSUR has not been smooth either. Brazil and Venezuela hold different worldviews and approaches in many aspects concerning the extent of integration and the relationship with the United States. On the one hand, President Hugo Chavez's view after the 2002 coup that tried to overthrow him with the blessing of the US has become radical and rambunctious; he holds militaristic and highly confrontational tones, primarily based on the idea of building a multipolar world opposed to United States hegemony. On the other hand, President Lula da Silva's view is a multidimensional one, based on productive, industrial, and commercial development, and seeks not to confront the US and to be identified as an intermediary in a relationship that will not threaten regional and global aspirations.[150]

4.5. Post-liberal Regionalism in South America

Going with the flow of political renovation in the subcontinent, new projects started to shape up. An example of an initiative that was nourished by the arrival of new leaders to the region is the Bolivarian Alternative (currently, Alliance) for the

[148] The Venezuela's Adhesion Protocol to the MERCOSUR is pending approval from Paraguay.
[149] Rodrik, D., op. cit.
[150] Serbin, A. (2009). "América del Sur en un mundo multipolar: ¿es la Unasur la alternativa?, Nueva Sociedad, n. 219, enero-febrero. Published online at: www.nuso.org

Americas and the Caribbean (in Spanish, ALBA), launched in 2004, an initiative of Venezuela's President, Hugo Chávez, and Cuba's President, Fidel Castro.[151] Based on the principles of solidarity and cooperation to fight against poverty, the area in which integration has advanced the most among these countries is cooperation in health and education.

Another example, the most interesting one for this analysis, is the present building of Union of South American Nations (UNASUR), which started to shape up in different meetings of South American presidents, in 2000 and 2002. In 2004, South America was formally defined as a different concept from Latin America.[152] At the meeting in Cusco (Peru) in the same year, the South American Community of Nations was born, an initiative that was based on such principles as solidarity, cooperation, pluralism, democracy, and peace.[153]. The Community undertook to build upon the integration processes then under way in the region, mainly ACN and MERCOSUR.

Brazil was the midwife of this initiative and, although all of the countries signed the Declaration, it should be pointed out that the remaining three presidents in MERCOSUR did not attend –neither Argentina's, Paraguay's, nor Uruguay's. In addition, in reading the Declaration, it is clear not only that it contains general provisions –as if only certain minimum thresholds had been agreed upon-, but also that the goal of integration would be attained through free trade agreements and infrastructure projects, an issue that has gained relevance as an engine of region building.

Four years later, in May 2008, in the city of Brasilia, the South American Community gave way to the Union of South American Nations (UNASUR), a body that integrates the whole subcontinent and that seeks to develop an integrated area for political, social, cultural, economic, financial, environmental, and infrastructure matters. UNASUR members are Argentina, Bolivia, Brazil, Colombia, Chile, Ecuador, Guyana, Peru, Paraguay, Suriname, Uruguay, and Venezuela, committed to annual presidential summits. Semi-annual ministerial meetings and bi-monthly delegate meetings are also scheduled. A Secretariat in Quito was inaugurated (presided by a General Secretary) and a Parliament to be based in Bolivia is planned.

Since the beginning, UNASUR has had a strong strategic approach and has placed a strong emphasis on physical and energy-related connectivity in South America. The infrastructure agenda at UNASUR is currently under development, as is the proposal that the Initiative for the Integration of the Regional Infrastructure of South America (IIRSA) –an initiative launched in 2000 as a discussion forum for the authorities responsible for transportation, energy, and communications infrastructure in the twelve South American countries- become the executive-technical forum of a Council of Infrastructure and Planning Ministers under UNASUR.[154]

Additionally, UNASUR has important proposals for the region, such as the Defence Council and the Bank of the South. The first initiative is a clear indication of the political glue of UNASUR, while the Bank of the South contemplates issues that open new paths for of trade and financial integration. Following successive back-and-forth moves, the Bank's Founding Charter was signed by the presidents of Argentina, Bolivia, Brazil, Ecuador, Paraguay, Uruguay, and Venezuela. Based in Caracas, the bank will initially operate as a development bank, although some countries, led by

[151] Bolivia has been member since 2006, and Nicaragua since 2007.
[152] In other words, Mexico, Central America and the Caribbean were not included in this initiative.
[153] Source: www.comunidadandina.org
[154] Source: www.iirsa.org

Venezuela, are interested in extending its operation as a regional monetary fund, aiding countries confronting a balance of payments crisis.

To sum up at present in South America MERCOSUR and the Andean Community of Nations inherited from the 90's now coexist with the new generation of post-trade regional institution building initiatives. As an example of the latter trend, UNASUR intends to build upon the assets of the two already existing blocs, in addition to having an agenda that gives priority to such issues as energy, infrastructure, the political stability of the region or defence, which are transversal to the subcontinent.

Nevertheless, the new framework remains contested. Venezuela and Brazil compete on different grounds and with different styles, so the institutionalization of new projects is still far from stable. Yet the dimensions of the competition should not be exaggerated. In their mutual dealings both avoid direct confrontation with the other and have even searched for spaces of cooperation. The joint venture between the Venezuelan and Brazilian oil companies in petrochemicals is a case in point as is Brazilian provision of arms to Venezuela. In the same way, Brazil and the Alliance for the Americas and the Caribbean (ALBA) governments have avoided antagonizing each other.[155]

There is no substantial legal incompatibility between the construction of UNASUR and trade initiatives of the 90's. Yet the underlying differences among members point to two risks: on the one hand, that UNASUR may advance toward minimum consensus in the subcontinent and, on the other, that there may be increasing distance between the Atlantic coast (MERCOSUR *plus* Venezuela) and the Pacific coast (CAN *plus* Chile).[156] The Pacific coast would continue seeking to strengthen its bonds with Northern countries, while MERCOSUR, led by Brazil, would continue supplying a more pro-development tone to integration and giving preference to South-South agreements.

A more pacific coexistence of both views should not be ruled out either. If the countries maintain a pragmatic vision on integration processes, it is likely that the regional agenda will continue moving forward anyway, at different paces, more in line with an endogenous dynamic than so far has been the case and in multiple partner groups.

In this context, one of the ways to preserve the alignment of smaller partners in the MERCOSUR bloc would be to give more relevance to the management of asymmetries, a long standing complaint of Uruguay and Paraguay to their larger partners, Brazil and Argentina. The next section will analyze changes on MERCOSUR's internal agenda on the management of asymmetries since the emergence of the new regional mindset in the region.

4.6. Asymmetries on MERCOSUR's: from the nineties' commercial agenda towards neo-developmentalist concerns

In terms of promoting trade, MERCOSUR has shown a good record, as detailed above. However, as regards the management of internal asymmetries, mostly

[155] Tussie, D., op. cit.

[156] Rios, S. P. and Veiga, P. M., op. cit.; Valladão, A. (2007). "The New Tordesillas Line. The Present Great Latin American East-West Divide", OBREAL/EULARO background papers, Paris, July.

the structural ones[157], MERCOSUR was created with the LAIA's heritage together with an open regionalism bias: it acknowledges asymmetries in longer terms and provides some exemptions to less developed economies; in this case, Uruguay and Paraguay.

In fact, Article 6 of the Treaty of Asunción, 1991, states that members recognize certain differences regarding implementation timing for Paraguay and Uruguay, as described in the Trade Liberalization Program. In the bloc's founding agreement, there is no mention to the word "asymmetry", and S&D is granted in the longer timetables for implementation and a larger number of exceptions to the Common External Tariff. Yet the Treaty of Asuncion is a remarkably lean, almost skeletal treaty that set out the trade liberalization programme with few considerations and conditions.

Four years later the preamble to the Protocol of Ouro Preto calls attention to the need to afford special consideration to the less developed countries and regions. Nevertheless, bloc asymmetries continued to be addressed by means of *negative policies*, granting smaller economies certain flexibilities in relation to the obligations undertaken.[158] Those flexibilities include the lists of exceptions, laxer rules of origin regarding extra regional value added for the purpose of granting a MERCOSUR certificate of origin to a product, and temporary admission regimes.

This was the scenario during the nineties and the first years of the new century. Nothing more was to be expected from smaller countries, other than to accept these specific flexibilities and to seek for extensions for their lists of exceptions to the Common External Tariff (CET). These trade measures hardly had an impact on asymmetries. In fact, MERCOSUR has led to greater economic concentration.[159]

Additionally, according to a study carried out by the *Instituto de Pesquisa em Economia Aplicada*,[160] since the creation of the bloc, Brazil has been in surplus *vis à vis* all three members, thus failing to operate as the bloc's buyer of last resort and to prop up the trade-related growth of the smaller partners. Tension increased during bloc negotiations for a free trade area with Bolivia and Chile, because Uruguay and Paraguay feared the dilution of their preferential access to the markets of the bloc's large countries for the benefit of the two newcomers.

Moreover, the newcomers to the free trade area were not obliged to adopt the CET – as Uruguay and Paraguay were - and therefore did not have to pay the costs associated with the protection of Brazilian – and in a less extent, Argentinean - industrial goods.[161] As tensions built up, and the international prices of commodities increased, Paraguay and Uruguay were increasingly dissatisfied with the bloc - including the threat to negotiate FTAs with the US, which would represent the dilution of the MERCOSUR's CET. This context was reflected in a decrease in the MERCOSUR share of total exports from Paraguay and Uruguay between 1998 and 2004.[162]

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[157] Asymmetries can be classified in those called structural – which origin from differences in economy size, Geographic position, factor endowment, infrastructure, institutional quality, and development level of countries -, and policy asymmetries – resulting from lack of both policy and institutional convergence and coordination among countries (Bouzas, 2005).

[158] Fossati, V. and Levit. L., op. cit.

[159] Calfat, G. and Flores Júnior, R. (2001). "Questões de geografia econômica para o Mercosul. In: Chudnovsy, D. and Fanelli, J.M. El desafío de integrarse para crecer. Balances y perspectivas del Mercosur en su primera década. Buenos Aires: Red Mercosur-Siglo XXI Editores.

[160] Fossati, V. and Levit, L., op. cit.

[161] Rios, S. P. and Veiga, P. M., op. cit.

[162] For data, see Fossati, V. and Levit, L., op. cit..

The increasing dissatisfaction of smaller partners in relation to the results of trade integration, and the emergence out of the crisis and severe contraction that hit the region led to conceiving a regionalism less focused on trade.

At the time of the relaunching of MERCOSUR in 2003, the agenda was extended and the issue of asymmetries slowly gained ground. Gradually, greater attention was paid to positive actions intended to reduce and overcome asymmetries among partners and promote integration of value chains.[163] More and more frequently, the agenda included concerns about production structures and excluded sectors, which is reflected in the launching of programs dedicated to production and social issues: MERCOSUR Social, and MERCOSUR Productive Integration, MERCOSUR Pymes, and the MERCOSUR the Fund for Structural Convergence and Institutional Strengthening - FSCIS, or FOCEM in its Spanish acronym.[164]

Among these initiatives, the Fund is undoubtedly one of the most relevant ones. Although massively underfunded, it is a step in the direction for the treatment of asymmetries. Its goal is to promote structural convergence, develop competitiveness, and promote social cohesion, particularly in relation to smaller economies and less developed regions, support the institutional structure operation and the strengthening of the integration process. The Fund recognizes the asymmetries arising from the size of economies and also from regional inequalities. In fact, while Brazil is the biggest economy in the bloc, having the highest GDP, it has the third lowest GDP *per capita* in the region (followed only by Paraguay) and the Brazilian Northeast is among the least developed regions, in terms of GDP *per capita* and human development index.[165]

The total annual capital of the Fund is 100 million dollars, out of which Brazil contributes 70%, Argentina 27%, Uruguay 2%, and Paraguay 1%. Although this is a small figure for the needs of the region in terms of infrastructure, social and economic development, it is an important step towards keeping the bloc together on new terms.
There are other initiatives worth of note. That is the case with the public-private spaces dedicated to competitiveness ("foros de competitividad") that should serve to develop value chains, particularly between Brazil and Argentina. The initiative began in the timber and furniture sector (2003), and in 2007 a second forum was launched, in the film industry sector.

Other more recent cases include the MERCOSUR Guarantee Fund for Micro, Small and Medium Enterprises[166] and the MERCOSUR Family Agriculture Fund (FAF).[167] The first fund, amounting to 100 million a year, is intended to guarantee, either directly or indirectly, credit transactions made by micro, small and medium enterprises participating in productive integration activities under MERCOSUR. In turn, the second fund, amounting to 300 thousand dollars a year, is intended to finance programs and incentive projects for family agriculture activities under MERCOSUR. Contributions are made *pro rata* to each member country, subject to the same percentages as FOCEM.

Another advancement seen in 2008 granting special treatment to Paraguay and Uruguay is the consolidation of a framework to guide extra-regional negotiations. The framework contemplates some flexibility in regards to rules of origin and special tariff quotas for the exports of smaller countries.

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[163] MERCOSUR Secretariat, 2006.
[164] For more information, see Holzhacker and Santos (2007).
[165] Fossati, V. and Levit, L., op. cit..
[166] Decision CMC 41/08, available at: www.mercosur.int
[167] Decision CMC 06/09, available at: www.mercosur.int.

Evolution in the social dimension is reflected in the creation of the MERCOSUR Social Institute (ISM) for instance.[168] The general objectives of the ISM are to contribute to social dimension as a pillar in MERCOSUR development; to contribute to the reduce asymmetries; to provide technical assistance in the design of regional social policies; to systematize and update regional social indicators; to collect and share good practices in social issues, to identify funding sources. The ISM has started to operate and it is slowly building its institutional structure. Once it is operational, the Institute will perhaps represent a step toward harmonization of social policies in the bloc.

In sum MERCOSUR initially had a quite narrow trade approach in relation to asymmetries among member countries. With few exceptions, flexibilities reflected longer periods of time for smaller economies to fit in new rules. This situation was gradually dented, and in the new context, there is an increasing acceptance that the bloc needs deeper structural measure in order to survive and overcome the risk of unravelling.

In the next section, we will analyze whether MERCOSUR's external agenda on asymmetries reflects those internal changes.

5. MERCOSUR's External Agenda on Asymmetries: Tensions Between Two Models of South-South Agreements

MERCOSUR was born under the aegis of open regionalism. As a regional bloc in transition, MERCOSUR is trying to deal with the new challenges in south-south trade relations. The treatment of asymmetries reflects this dilemma.

This section will address the remedies to deal with the asymmetries in relevant South-South agreements signed by MERCOSUR with the Southern African Customs Union (SACU) and India. The agreement between MERCOSUR and Israel is also analyzed to highlight similarities and differences concerning the treatment of asymmetries. With this analysis we hope to shed light on how tensions in MERCOSUR's internal agenda re-emerge and tint the external agenda.

5.1. Agreements between MERCOSUR and Some Extra-Regional Partners: MERCOSUR – India, MERCOSUR – SACU, MERCOSUR - Israel

In general, preferential agreements involving MERCOSUR and extra-regional developing countries fall under the GATT Enabling Clause. As with GSTP and MERCOSUR, these agreements seek to increase trade relations among Southern countries, creating new alternatives, reducing dependence on northern markets, and ultimately uniting developing countries to negotiate on more equitable terms.

Nevertheless, there is no guarantee that greater southern interdependence leads to mutual benefit at all times. There may be joint gains and losses and there may at the same time be relative gains and distributional losses. This may be particularly accurate in trade arrangements among developing countries groupings that have great internal asymmetries (among countries and within countries), as in the case of MERCOSUR (see section 4.6.). The regional bloc seeks greater interdependence with

[168] Decision CMC 03/07, available at: www.mercosur.int.

extra-regional trade partners, without affecting trade interests of smaller countries or less developed regions.

The agreements that MERCOSUR has negotiated with India, with the Southern African Customs Union (SACU), and with Israel are examples of a new vintage. In the three agreements, the Free Trade Area is set out as a long-term objective. Although the agreement between MERCOSUR and Israel falls under GATT Article XXIV -and it is not a clear example of South-South trade[169],- it will be analyzed in order to show contrasts between the three agreements.

Of these agreements, the only one currently in effect is the MERCOSUR-India preferential agreement, notified to the WTO in February 2010 under the Enabling Clause. This agreement is perhaps the most emblematic one of the three, because it brought together two huge subcontinents with a proactive trade diplomacy. This is not a coincidence, as the agreement was signed the same year as UNCTAD XI, in 2004, when the third round of GSTP was launched, one year after the establishment of the agricultural G20, with Brazil and India acting as brokers for the developing world.

The agreement with SACU was also signed in 2004 as part of an encompassing effort to bring the South Atlantic countries together. The agreement with Israel is the most recent one, dated 2007.

The joint analysis of the three agreements aims to highlight similarities and differences concerning the treatment of asymmetries, both at the multilateral level (in the case of MERCOSUR-India and MERCOSUR-SACU, as a tool for strengthening South-South trade) and internally in the agreement (the manner in which the three agreements acknowledge and deal with asymmetries among signatory countries).

In this regard, certain aspects are worth noting. The MERCOSUR-SACU and MERCOSUR-India agreements recognize the importance of trade promotion and cooperation in strengthening South-South trade. The agreements with India and SACU are more upfront in the ambition to open new avenues of cooperation. In both preambles they assert that regional integration and trade among developing countries, including through the creation of free trade areas, are compatible with the multilateral trading system, and contribute to the expansion of world trade, to the integration of their economies into the global economy, and to the social and economic development of their peoples. The mention could be considered formal desiderata since both agreements do not detail on how they are compatible with WTO or how to better integrate southern economies into the global economy. Nonetheless, the interpretation of specific provisions in agreements extend to the preamble according to Article 31 of the Vienna Convention, so the preamble does carry some weight when differences arise and the agreement must be interpreted.

With regards to trade instruments *per se* - such as antidumping or countervailing measures, safeguards, national treatment, customs valuation, technical barriers to trade, sanitary and phytosanitary measures - these agreements refer to the WTO rules as a framework. As a general rule, in the case of trade issues that are also regulated in the WTO agreements; they also allow signatories to choose between the dispute settlement in the trade agreement or the WTO dispute settlement understanding. At times, the WTO is even the exclusive *fora* to resolve certain

[169] Israel has never been perceived or perceives itself as part of the south. As a core part of the Western security coalition, it has enjoyed multiple trade privileges and has never joined the coalitions of developing countries. In fact, Israel was the first country with which the US under Reagan signed an FTA and before contemplating a turn to regional relations such as the Canada US Free Trade Agreement.

matters, as in the case of the MERCOSUR-India Agreement regarding antidumping and countervailing measures.

In relation to provisions to face asymmetries, their treatment differs depending on the agreement.

The agreement with India consists of around 450 products per party, with trade preferences ranging from 10 to 100%. Despite the fact that all parties are champions of S&D, there is no upfront reference to flexibilities for smaller or less developed countries, not even in rules of origin. There are just two specific considerations for Paraguay in the tariff schedules: differential trade preferences in relation to a few agricultural products in addition to a quota in the Indian market for soybean oil.

The greatest interest of these two small open economies in the agreement is not related to access to the Indian market[170] but to reduce the high CET they had to accept as part of the cost of accession to MERCOSUR. The new agreement is an opportunity to redress the trade diversion they have paid so far. A declining tariff on imports from India can enable the establishment of processing industries to export to their MERCOSUR partners. Here they count on laxer rules of origin so that some of these processing activities for the wider MERCOSUR market can become gradually more relevant. In fact one can almost assume that Paraguay and Uruguay have been supporters of these agreements given they can free themselves of the hold of Argentine and Brazilian businesses that had preferential access to their markets thanks to the relatively high CET. At any rate, an important feature to note is that this agreement adopts a tariff quotas approach to deal with asymmetries.

While in the MERCOSUR-India agreement S&D treatment is left to the fine print of tariff schedules, in the MERCOSUR-SACU Agreement the considerations are part of the core principles, given that SACU comprises Lesotho, Swaziland, Namibia and Botswana, over and above South Africa, the regional powerhouse. The preamble states upfront that negotiations have taken into consideration the principle of special and differential treatment for smaller countries and less developed economies in both blocs.

In addition, in the Understanding between SACU and MERCOSUR on Conclusion of their Preferential Trade Agreement, the Parties commit themselves to broaden and deepen the Agreement, including, among others, the fisheries sector, with priority attention to the product interests of the smaller Members of both customs unions.

At the beginning of the agreement, in Article 6, d, the definition of customs duty excludes the duties levied by the Governments of Botswana, Lesotho, Namibia, and Swaziland for development of infant industries, pursuant to the SACU Agreement. In these cases, there will be consultations whenever those duties affect the preferential exports of Paraguay or Uruguay. That is the case where the S&D treatment granted to SACU's less developed members are protected from nullification in agreements between SACU and non-members countries. It seems that Botswana, Lesotho, Namibia, and Swaziland have no real legal obligation to reduce tariffs if they designate the duties as part of a program to develop infant industries, unless that reduction affects Paraguay or Uruguay's exports. However, in those cases, countries have the dispute settlement procedure as the last resort, in case they do not reach "satisfactory solutions".[171]

[170] In fact, almost all Indian trade is concentrated with Argentina and Brazil (UNCTAD, 2004).

[171] This expression is taken from the agreement in its original Portuguese version and could be understood as "non-legal" or "diplomatic" solutions..

In addition to the items mentioned, no considerations are contemplated in the rules of origin for Paraguay and Uruguay. No flexibilities have been established either in relation to safeguard measures, dispute resolution proceedings or in the lists of concessions, consisting of around 950 products with trade preferences ranging from 10 to 100%.

As observed, both agreements are hardly wide-ranging. They cover very few items and so are oblivious to asymmetries. They adopt isolated measures to deal with asymmetries instead of counting on an active plan to face them. The main difference between the two agreements is the way they adopt such isolated measures. The agreement with India seems to protect real export interests from a least developed country (soy exports from Paraguay), while the agreement with SACU protects interests of SACU's less developed members. These follow SACU's own rules, which naturally do not include Paraguay and Uruguay, which are nevertheless allowed to initiate consultations in the case their exports are affected.

While these two agreements are sold as part of a grand strategy to strategically *influence* the global trade process, they make progress with extreme paucity and have so far provided small stepping stones only covering small trade flows where actual business interests are present, soy bean, export processing of raw material, etc.

The MERCOSUR-Israel Agreement in contrast is posited as extending opportunities for existing trade flows rather than the strategic ambition to give way to the new geography of trade. It focuses on binding obligations to liberalise trade, rather than fuzzy rhetoric that seeks to mask the absence of binding trade obligations. In line with Israel different political inclinations, the agreement does not include a preamble highlighting the benefits of South-South trade.

However, the rules of origin include special consideration for Paraguay and Uruguay in relation to manufactured products. The agreement also contains an annex concerning cooperation intended to develop sectors and industries, through technology transfer, joint projects for the development of new technologies, among others. Particular attention should be given not only to the MERCOSUR smaller economies but also to SMEs.

In the case of the SACU Agreement, the special rights of SACU's less developed members for protection of infant industries have been granted, while Paraguay and Uruguay come into the picture only in the event that those rights cause them any detriment.

Finally, the agreement that focuses the most on the asymmetries among signatories and goes beyond exhortations is the Israel Agreement. It not only establishes more flexible rules of origin for Paraguay and Uruguay, but also includes an annex about technology cooperation where calls for special attention to be paid to less developed signatory countries and SME's as well. While this agreement is driven by a logical opportunity, the other two agreements are more strategically oriented and less encompassing at the same time.

As observed, the management of asymmetries in trade agreements involving MERCOSUR does not follow the same pattern observed in the bloc's internal agenda. However, as an integration process in transition MERCOSUR's external agenda on asymmetries struggles with two models of South-south agreement: one with ambitious desiderata in the preambles and few concrete measures, and the other that protects the most the smaller economies of the MERCOSUR.

6. Final Remarks

While South American integration processes, such as MERCOSUR and CAN, are not merely consequences of the last 10-year period of unprecedented proliferation of RTAs, their institutional and legal structure, liberalisation mechanisms and objectives were adapted to the trends of open regionalism. Whether MERCOSUR's rules are WTO compliant is still pending confirmation by the CRTA. Moreover, WTO jurisprudence on MERCOSUR failed to deliver a more direct and conclusive position in this respect.

MERCOSUR has made significant progress in the establishment of a free trade zone, especially regarding the liberalisation of trade in goods. However, the customs union has not been fully completed yet and progress in the design and implementation of a definite institutional structure for the bloc has been increasingly hard to attain. Additionally, certain commitments lost credibility as they were not internalized after joint approval. There has also been a multiplication of sectoral conflicts that have found no institutional channels for resolution so far.

On the other hand, there has been little progress in trade-related business disciplines, such as services and investments. The Protocol of Montevideo essentially reproduces GATS' main characteristics, which favour developing countries: flexibility; progressive liberalisation through positive lists of specific commitments; and the maintenance of Member States policy space to implement policies through the regulation of sector and sub-sector of services. As well as in the case of GATS, the essence of its framework and structure should remain unchanged, which is especially important in the context of South/South cooperation agreements expected to be shortly entered into more steadily by MERCOSUR and other developing countries.

Investment provisions will also be part of RTAs with developed countries and/or cooperation agreements with developing countries (regardless of their modality) under the Enabling Clause and/or UNCTAD GSTP that might be signed by MERCOSUR in the forthcoming years. This becomes a crucial issue given that MERCOSUR does not yet have common rules on investments, neither for intra-regional investments nor harmonized rules extra-regional flows.

This loss of steam in South American Integration processes, including MERCOSUR, came about at a time when serious questions about globalization were raised in many quarters. In this context, the advent of the so-called "New Left" governments in the region played a decisive role in the review of South American integration processes. This seems to be the response of a region to two closely intertwined sets of challenges. There is increasing mass mobilization and widespread public opinion dissatisfaction with the results of reform strategies, questioned for having failed to generate high growth levels, for not having included politically excluded groups, and for their inability to promote more equitable models of income distribution.

This perception of having paid a high price gave new air to already existing blocs, which were 're-launched' under the paradigm of the so-called post-commercial or post-liberal regionalism, with a strong pro-development tone, a concern for maintaining policy spaces and the consideration for the distributional impacts of trade liberalisation. It became clear, *inter alia*, that the integration agenda should be extended to include social and political issues and the trade dimension should comprise such items as structural and policy asymmetries.

Issues such as asymmetries were refreshed by the new wave of post-commercial regionalism. In fact, MERCOSUR initially had a trade related and quite

narrow approach in relation to *ex ante* and *ex post* asymmetries among member countries. This situation was gradually dented, and in the context of a new mindset in the region there is an albeit shy acceptance that the bloc needs fresh glue to survive and overcome the risk of unravelling.

With regards to MERCOSUR's external agenda on asymmetries, it is striking to note that those agreements involving MERCOSUR and developing countries (India and SACU) – seen as a powerful tool to reduce North-south asymmetries by encouraging South-South trade - have so little to say about South-South asymmetries. The agreement that focuses the most on asymmetries among signatories and goes beyond exhortations is the Israel Agreement. While this agreement is driven by a logical opportunity, the other two agreements are more strategically oriented and less encompassing at the same time.

In sum, the management of asymmetries in trade agreements involving MERCOSUR does not follow the same pattern observed in the bloc's internal agenda. However, as an integration process in transition, the MERCOSUR's external agenda on asymmetries is in the middle of two South-South agreement models: one with pompous preambles and few concrete measures, and the other, with a north-south bias, which does not include rhetorical speeches, but protects the most the smaller economies of the MERCOSUR.

This context presents some challenges to MERCOSUR in order to be better prepared to negotiate RTAs and South/South cooperation agreements, as well as to preserve the alignment of smaller partners in the MERCOSUR bloc. On the one hand, both MERCOSUR Protocols related to investments should be ratified. However, the greatest challenge will be to negotiate agreements whose investment provisions contain a necessary balance between the need to attract, promote and protect foreign investments and preserve Member States policy space to implement industrial policies aimed at their development. On the other hand, MERCOSUR should give more relevance to the management of asymmetries, mainly in the external agenda, where provisions undermining the trade interests of Uruguay and Paraguay would be much more complex to renegotiate than in the internal agenda.

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