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EC-EAC EPA'S COMPATIBILITY TO WTO RULES

A Brief Analysis

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INTRODUCTION

The compatibility of the Economic Partnership Agreements (EPAs) between the European Union (EU) and the former Africa Caribbean and Pacific (ACP) group of countries to the WTO rules has been widely debated. In this short note, a brief analysis of the EU – East Africa Community (EAC) EPA is made with regard to its compatibility to the WTO rules, a body to which all parties in the agreement are Members.

The note briefly reviews the state of play of the ongoing EU-EAC negotiations. Then, highlights some of the pertinent economic questions under consideration, and finally focuses on the EPA's compatibility with the WTO rules, especially looking at Article XXIV of GATT 1994.

Following expiration of the Yaoundé and the four Lomé Conventions, and the signing of the Cotonou Agreement in June 2000, EPAs between the EU and the ACP group of countries were drawn up with the objective of *inter alia* bringing the relations between the EU and ACP group of countries into conformity with the WTO regime. The 79 ACP Member countries were constituted in different configurations to negotiate the EPAs with the EU; amongst these a set of 15 countries under the Caribbean Forum of ACP States (CARIFORUM) have since concluded their EPA with EU, while negotiations are still ongoing with respect to the others.

The aim of these Free Trade Agreements is discriminatory, creating a shift in trade policy away from non-reciprocal trade agreements towards reciprocal ones between the parties to the agreement. With that said, the EPAs have several objectives, the first being reciprocity among parties belonging to it. Under this objective, trade barriers are to be limited and eventually phased out between the parties, making liberalization a vital component of the success of the EPAs. The other objective is to integrate ACP countries into the global economy, which, if realized will help alleviate poverty and create development in these countries. Another objective of the EPAs as spelt out is to encourage regional integration through which it is hoped that the pace of integration into the world economy, of the ACP countries will be faster. Finally, the other broad objective of the EPAs is said to be provision of Special and

Different Treatment to nations that are developing at a dissimilar pace, while also ensuring the parties conformity to their WTO obligations.

Amongst the configurations negotiating the EPAs with the EU is the EAC. The goal of this agreement is to help the EAC, which consists of Rwanda, Burundi, Tanzania, Uganda, and Kenya, become more integrated into the world economy. The EPA agreement is expected to enhance the agricultural sectors, since the agriculture sector presents the main potential from this region, but many questions still remain and need to be resolved if this will be achieved. There are also issues with Kenya being the only country in the region that is not categorized as a Least Developing Country (LDC) and hence with less viable alternatives in preferentially accessing the EU market, this has resulted in pressure to conclude the EPA despite glaring differences between the parties' positions on some aspects of the proposed agreement.

STATE OF PLAY AND ISSUES COVERED IN THE EU-EAC EPA

At the end of 2007, an interim Economic Partnership Agreement called a Framework EPA (FEPA) was drawn up between the EU and the EAC. This was to facilitate the continued preferential trade relations between the two parties', given that the WTO waiver for non-reciprocal preferences had come to an end. At the time there was commitment on both sides to negotiate a comprehensive EPA that would cover among others, agriculture, Sanitary and Phytosanitary Measures (SPS), Technical Barriers to Trade (TBT), customs and trade facilitation (C&TF). Negotiations on trade-related issues such as investment, competition and Government procurement, as well as trade in services were to be dealt with at a later stage. The comprehensive EPA was expected to be completed by 2009, however, five years later the negotiations are still ongoing, with only the consolidated EPA text in place.

The slow pace at which negotiations between the EAC and the EU have occurred is a result of several factors among which is the pace at which the integration process within the EAC is occurring. The process of integration of the EAC

is directly linked to the commitments nations within the EAC are willing to make which translates into the overall commitments of the region itself. After a brief set of negotiations in September 2011, another round occurred in December 2011 that laid out a timeframe for concluding the agreements in 2012. In January 2012 the Chapters on SPS, TBT, C&TF were finalized, while the EAC submitted to EU the proposed text on Economic and Development cooperation with regard to agriculture, SPS, TBT and C&TF¹. The EPA also includes an extensive Chapter on fisheries in order to reinforce sustainable use of resources in EAC.

The contentious issues, on which agreement is yet to be reached, include the Most Favored Nation (MFN) clause in the agreement, export taxes provision, rules of origin, dispute settlement, institutional and final provisions.

COMMITMENTS UNDERTAKEN

The commitments under the EPA are asymmetrical, whereby the EAC will have full access to the EU market, and gradual opening of its market to the EU goods. Since 2008, all imports from the EAC have entered the EU market Duty Free Quota Free (DFQF), except with a transition period for sugar until 2015, and arms, which the DFQF does not apply to. The goal for the EAC is to gradually liberalize its market, which will occur in three phases: the initial phase was envisioned to start in 2010 with 65.4% liberalization of imports from the EU involving 1,950 tariff lines, which were already zero-rated. The second phase is foreseen to be effective from 2015-2023 comprising of 1,129 tariff lines and accounting for aggregated liberalization of 80% of imports from the EU and the final liberalization will be done between 2020-2033 and account for 2% liberalization of

¹ The EPA experts recalled that EAC EU technical and senior officials Negotiations session held on 12th-15th December, 2011 in Brussels, two areas of divergence on Economic and development Cooperation remain:

- (a) Whether the EAC EPA Development Matrix should be annexed to the EPA, which is preferred by the EAC, as this would indicate commitment by both Parties to mobilize resources towards the Implementation of the Development matrix.
- (b) Whether the benchmarks, indicators and targets should be developed six months after the signature (EAC position) or entry into force (EU position) of the EPA.

market involving 960 tariff lines. However, the EAC will not liberalize 18% of its trade, which constitutes sensitive agriculture products, wine and spirits, chemicals, plastics, wood based paper, textiles, clothing, and shoes among others.

The EAC countries have the same liberalization schedules but the impact on the different EAC countries is dependent on the level and distribution of imports from the EU in the recent past. The higher the quantities of EU imports that are liberalized earlier, the faster the EAC country has to face the adjustment of lost tariff revenue. Burundi, Tanzania and Uganda would incur the highest shares of revenue losses i.e. 91% for the former and 77% in the case of the latter two, while Kenya and Rwanda would experience 68% and 71% revenue losses during the 2nd tranche of the liberalisation.

The EU is an important trading partner for the EAC with around €3 billion worth of imports in mainly oil products, machinery, electrical appliances, cars, etc and with around €2 billion worth of exports to the EU mainly in agro-food products. The EPA is expected to result in more trade creation than trade diversion. In Tanzania, however it likely to result in trade diversion, meaning that trade is diverted from more efficient suppliers from outside the trading bloc to less efficient suppliers within the bloc. In the other EAC countries also, there may be switching of consumption away from local producers to EU producers.

WTO RULES AND THE EC-EAC EPA

The initial quick start of the negotiations in 2007 was due to the WTO obligation for members to ensure that their trade relations are in compliance with the WTO rules. As highlighted before, the FEPA has been governing the trade relations ever since while the subsequent rounds of negotiations are towards concluding the 'full' EPA. It is critical that the resultant agreement is in conformity with WTO rules.

Under the WTO, there are several rules applicable to the EU-EAC EPA. Given that the Framework EPA in place covers only goods, the first WTO rules that apply are GATT 1994 Article XXIV which covers trade in goods. However, these GATT Article XXIV rules that determine

WTO compatibility remain ambiguous and subject to different interpretations. Furthermore, what is problematic in Article XXIV of GATT 1994 for the developing countries is that it does not avail specific Special and Differentiated Treatment.

Article XXIV: 2 of GATT Agreement is fulfilled under the EU-EAC FEPA, to the extent that it a Free Trade Area between the EAC and the EU. Further, Article XXIV: 4 of the GATT states that the FTA should facilitate trade between the parties to the agreement. It is argued that this provision does not constitute a separate obligation on the parties to the FTA and that only paragraphs 5-9 of GATT Article XXIV create positive obligations. However, the purpose stated in paragraph XXIV: 4 is to be observed constantly and it informs the other paragraphs of the Article. Thus in the negotiations of the EPA between the EAC and the EU one has to constantly address the question of whether the EPA leads to facilitation of trade or rather acts as a barrier to trade to non-participating parties. But to the extent that the EPA actually liberalizes trade and does not create barriers to other parties, it is compatible with Article XXIV: 4.

GATT Article XXIV: 5 provides that duties and other regulations of the FTA cannot be more restrictive against non-parties. However, the meaning of what belongs under Other Regulations of Commerce (ORC) is sometimes disputed with contention as to whether SPS, TBT rules, Rules of Origin (RoO), Competition Rules, and Quantitative Restrictions can also be included here.

Turning to each of these issues, the WTO Panel has ruled that quantitative restrictions are regulations of commerce under Article XXXIV: 5. Under the FEPA, quantitative restrictions are prohibited, except in times of critical food shortage. In addition, RoO in the FEPA are defined broadly, making them compatible with Article XXIV: 5 as well as with those of the WTO Agreement on RoO. In terms of the TBT and SPS measures, it is not yet clear if they fall under the ORC. To ensure that harmonization of the rules do not become trade barriers to third parties, Chapter V of the Framework EPA first listed TBT and SPS as the areas of future negotiations, which have now been concluded, though with some issues with regard to RoO have yet to be settled.

Since the FEPA is accompanied with a plan and schedule for the formation and completion of the FTA, it complies with Article XXIV: 5(c). Liberalization of trade under the FEPA will take place over the next 25 years, which exceeds the proposed ten year indication of "reasonable amount of time" to liberalize trade under Article XXIV: 5(c), unless there is an "exception case." Though WTO members have still not defined what constitutes an exception case, the EAC-EU EPA could be considered as one since the FEPA is between a developing and developed party exemplifying large differences in the partners' development. Furthermore, ACP countries have requested from the WTO a transition period of 18 years to allow industries of the developing countries to adapt to radically increased competition, to introduce measures to compensate for tariff revenue losses, and to allow African countries to achieve better regional integration before fully opening their markets to the EU.

GATT 1994 Article XXIV: 7 obliges WTO members to notify their agreement to the WTO, which would require the FEPA to be formally notified in WTO.

GATT 1994 Article XXIV: 8(c) ensures that FTA liberalization is undertaken to the required extent, that participating countries are not violating the MFN rules selectively, that FTA is welfare enhancing and trade diversion is avoided. It is not clear how much liberalization is necessary to satisfy the test of Article XXIV: 8 calling for "substantially all trade." For instance, it is not clear whether it is quantitative calling for some substantive percentage of trade or if it is qualitative ensuring that no major sector can be excluded from liberalization. Initially the aggregated trade liberalization foreseen for the EAC is 82%, with the ultimate goal being 91% of trade.

Taking into consideration the FEPA compliance with the WTO rules, it is likely that it will be compatible with the WTO rules to create a FTA as laid out in Article XXIV of GATT 1994.

Aside from the GATT 1994 Article XXIV, other WTO rules that apply to the FEPA are enshrined in the Enabling Clause. Adopted under GATT in 1979, this clause permits developing countries to receive preferential and differential economic treatment from developed countries. This clause states that the equal treatment of developing or

least developed countries that have different economic capabilities would be unjust. Through offering preferential and differential treatment, the objective of this clause is to increase the participation of developing countries in the global economy. Therefore, notwithstanding the MFN treatment clause drawn out in Article I of GATT 1994, the contracting parties to an agreement may accord differential and more favorable treatment to developing countries without according such treatment to other members of the WTO. FTAs between developed and developing countries on that basis are discriminatory, reducing and eroding trade barriers only among the FTA members and relative price of goods for those outside of the FTA will increase. However for the enabling clause to apply, a trade dispute panel found that the following rules must be complied with:

With regard to issues covered under the EPA, there is nothing in the WTO rules that requires parties to an FTA to include trade related issues such as intellectual property, investment, competition, and government procurement in order to comply with their WTO obligations. Services have also been discussed under the EU-EAC EPA negotiations, thus GATS Article V will also apply to the version that will include trade in services. More specifically, its main purpose is to encourage the integration of labor markets between developing and developed countries but with no obligation to liberalize their services sectors.

There are further guidelines in terms of RTAs under the WTO rules that have been perfected during the current Doha Round negotiations. Paragraph 29 of the Doha Declaration provides guidance in negotiating RTAs calling for *clarifying and improving* WTO rules that apply to RTAs. The Declaration also emphasizes the

taking into account of the developmental aspect of the RTAs. The guidelines include a transparency mechanism which has been agreed upon. Under this mechanism, RTAs are to be announced early, the WTO is to be informed immediately of the conclusion of RTA agreements, and the constant updating of information and progress of procedures for notified RTAs. The EU-EAC EPA is required to conform to these obligations.

CONCLUSION

From the discussions above the EU-EAC EPA should pass the test of WTO compatibility, in the event that any of the other WTO members challenges it on the basis of Article XXIV of GATT Agreement on establishing free trade areas (FTAs).

A crucial element to this compatibility and the success of the agreement is the EAC's status as a common market. Thus, it is important that the member countries of the EAC develop a single agenda in order to more effectively negotiate the EPA settlement with the EU. With negotiations still ongoing, it is essential that countries of the EAC accomplish this goal of establishing a uniformed agenda so that they may more clearly lay out their aims. This would increase the pace and effectiveness of the negotiations of the EPA which in turn would quicken the pace of the EAC's integration into the global economy. In addition, one of the main aims of the WTO is to allow for increased liberalization in markets across the globe. Hence, even though this agreement institutes reciprocal preferential treatment in the short run, it encourages, in accordance with the aim of the WTO and member countries around the world, liberalization in the long run.

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