The Implementation and Rules of Regional Preferential Agreements: The Experience of the Latin American Integration Association and MERCOSUR

Félix Peña

Director of the International Trade Institute at the BankBoston Foundation and of the Interdisciplinary Center of International Studies at the National University of Tres de Febrero (UNTREF).

Summary

Regional preferential agreements (RPA's) are a relevant dimension of international economic relations. A challenge ahead is to assure that they could be always consistent with the main principles and collective disciplines of the World Trade Organization (WTO). That means that they could really be a "building block" toward an integrated and open global economy.

What seems necessary then is to improve global collective disciplines to assure that all RPA's -both old and new- could really be consistent with WTO. The effective "rule-oriented" approach of RPA's is an important condition to preserve the strength of the multilateral global trade system. The proliferation of RPA's with poor implementation and without strong collective disciplines could be negative for free trade and development objectives at the global level.

Low quality RPA's are the result of poor rules of the game and weak enforcement capacity. In that case, they could play against the interest of smaller member countries and in favor of bigger and more developed members. Eventually, MERCOSUR could be an example. To preserve the "rule-oriented" character of a concrete RPA -against the "power-oriented" alternative- is then crucial for the protection of the national interests of those relatively smaller member countries.

This paper is the result of his research work under the auspices of both academic institutions.

I. Introduction

This paper aims to contribute to the analysis of the implementation of different modalities of regional preferential agreements (RPAs).[1] The subject can be approached from at least three perspectives.

The first is by considering the relationship between the RPA rules and collective disciplines resulting from the rules of the multilateral global trading system represented by the World Trade Organization (WTO).

The second is by considering the connection between the rules of certain RPAs and the collective disciplines resulting from the broader RPA to which they are formally related. This perspective is relevant for cases such as the Latin American Integration Association (LAIA), which in formal terms is the enabling framework for most RPAs between Latin American countries. Depending on the final format, this may prove to be of importance for the Free Trade Agreement of the Americas (FTAA).

A third perspective is the relationship between an RPA's rules and the domestic laws of each participant country, particularly concerning the normative framework of public policies affecting foreign trade, as well as firms' strategies and investment decisions.

I begin by analyzing the phenomenon of RPAs and their rules, and then deal with the approaches mentioned above, with special reference to LAIA and Southern Common Market (MERCOSUR). Finally, I draw some conclusions about the main topic of the Second IDB/CEPII Conference.

II. RPAs and their Rules

RPAs have proliferated in recent years. Professor Jagdish Bhagwati refers - perhaps exaggerating somewhat - to an "epidemic".[2] Formally speaking, RPAs all view themselves as being consistent with WTO principles, objectives and rules. They want to be perceived as functional tools for expanding and freeing up global trade in goods and services, and for contributing to the greater welfare of their citizens -even for the human race as a whole.

This is not a new phenomenon. Historically speaking, the new event is the existence of a global framework of multilateral trade disciplines set in train in 1947 with the GATT, and culminating in 1994 with the creation of the WTO. Even before the Havana Conference, there had been various precedents for RPAs, usually associated with the beginning of a new sovereign State. The best-known of these, but not the only one, is the Zollverein (see Machlup [1977], see also Nolde [1924] and Anderson & Norheim [1993]).

Throughout history, we can observe the constant interaction of political, economic and legal factors in the genesis and development (and even in the failure) of RPAs. Capturing the entire essence and dynamics of each RPA -and of RPAs as historical and contemporary international phenomenon- demands an understanding of the interaction of the three logics of power, welfare and legality. This can easily be perceived by anyone who has ever taken part in the RPA negotiating and decision-making processes for each partner country, or been present at the multinational level of the institutional mechanism of an RPA.

Therefore, getting to grips with this interaction is important for any academic approach that deals with the RPA phenomenon and attempts a specific theoretical description. It is more important still in the context of policy-oriented approaches. Yet, having said this, it is still germane to address the dynamics of the three logics separately, while yet remaining aware that such an approach only partially captures a more complex reality.

RPAs are agreements adopting various different modalities. There is no one, universally valid, pre-established model. They can be classified according to various different criteria. The following four criteria are the most significant:

a) physical contiguity or discontiguity between partners;

b) bi- or multilateralist scope depending on the number of participant countries;

c) market integration techniques utilized within a free-trade area or customs union as stated by Article XXIV of GATT-1994, or those spaces permitted by the Enabling

Clause negotiated and approved during the Tokyo Round (see Winham [1986] pp. 141-146; 274-280; see also Srinivasan [1998] pp. 21, 24 and 99), and

d) the distribution of economic and political power between partners and, particularly, and the extent of disparity in economic development.

Each agreement develops its own system of rules. They can be viewed as a "private club" within the framework of a "global club" (Snape [1993] pp. 283-287). From the global trading system's point of view, RPAs are differentiated subsystems, and some possess a regionally distinctive geographical character. RPA rules can be visualized as encoded signals to markets -and third countries- as to what future conditions governing trade and investment flows within the economic area covered by partner countries will be like. In the context of contemporary global economic competition, these signals essentially attempt to attract productive investments and influence firms' strategic decisions, both those already operating within an economic area covered by an RPA -large companies and SMEs- and those competing in the global marketplace.

As a result, the perception of the rule quality of an RPA -as measured in terms of potential effectiveness, efficacy, sustainability and legitimacy- (Peña [2003a]) is a key factor for the strategic *decoding* carried out by firms competing, or attempting to compete, in global or regional goods and services markets. This also explains the importance for companies and investors of the smooth dissemination of rules information, including rules at the preparation stage (Peña [2003b]). From this viewpoint, transparency in RPA rule-making is a valuable thing for competitive company intelligence. We might suggest that the quality of an RPA nowadays, at least from the point of view of rule-production and decision-making processes, is reflected in the quality of its web page.

Those who operate in global and regional firms possess a clinical eye, honed by careful management of their competitive intelligence to distinguish solid, credible signals from predominantly empty exercises in "media diplomacy" or "special effect policies". In particular, the quality and sustainability of partner countries' political systems, as well as the quality of their respective macroeconomic, industrial and foreign trade policies, are major factors in assessing the credibility of signals arising explicitly or implicitly from an RPA's rules.

RPAs' rules generally originate in international multilateral legal instruments establishing a treaty -as defined under the Vienna Convention- whatever its formal denomination. A rule's system of association of States derives from an original constitutive agreement. It is applicable only between partners, regardless of whatever economic effects it may have beyond the limits of the economic area in question.

The constitutive pact is based on a satisfactory balance of national interests between partners. No one can force a sovereign State to be part of an RPA. If a country decides to take part, it is because the RPA is considered advantageous to the national interest. It is the expectation of mutual benefits by all partners that explains the origin of the constitutive pact. It also explains its maintenance over time. This perception enables an RPA to acquire social legitimacy before the citizens concerned, a key factor for the sustainability of an RPA over time (Peña [2003c]).

Three common denominators can be observed in the objectives of RPA rule systems, whatever their modalities:

a) guaranteeing access to the respective markets for the goods and, ultimately, the services and persons originating from each partner;

b) establishing a degree of discrimination in favor of the partners in terms of their access to the respective markets (e.g. through common tariffs for customs unions, or

specific origin rules and investment, and public procurement regulations for free trade areas), and ultimately, to the way of operating within each market, and

c) developing explicit or implicit collective disciplines between partners, with the practical effect of conditioning autonomy in shaping and implementing public policies, especially in the fields of macroeconomics, foreign trade and investments.

A mechanism for producing rules is also generally included in the original pact. Secondary or complementary rules may result from this in addition to those in the founding agreement. The rational conclusion is to suppose that, while producing these rules -as with the original agreement- the partners wish them to percolate through effectively into the real world, and therefore produce the expected economic and ultimately political results.

There is no single model deriving from international rules that prescribes how an RPA's institutions should be organized (see also Kahler [1997]). However, by analyzing specific cases, we can recognize certain functions that institutions should comply with. These include:

a) preservation over time of the reciprocity of national interests behind the original pact;

b) deriving complementary and secondary rules from the constitutive agreement, enabling implementation, adaptation to changing circumstances, or -particularly in the case of a common market or economic union- further development of a common project;

c) conflict management between partners as a result of implementing the RPA and resolution of trade or investment disputes through common jurisdictional mechanisms, arbitral or judicial, and

d) dissemination of information about rules and their implementation.

The deeper and more complex an RPA's objectives are, the broader these functions will be. For instance, monetary and economic union between a large number of contiguous sovereign States, either having developed or attempting to develop explicit political objectives (including the area of safety), may require more complex institutions than a simple free trade area between countries lacking physical proximity.

Finally, the characteristics and modalities of RPA institutions are strongly influenced by two further factors:

• the degree of interdependence and connectivity existing between the economies of the partner countries, as gauged in particular by the intensity of trade, investment and financial flows; and,

• the distribution between partners of relative economic and political power, in particular where asymmetries in the interdependence and connectivity of their respective economies are involved.

III. RPAs and the WTO

The issue of linking the multilateral global trading system with regional preferential subsystems -not to mention the tension between the two phenomena- has a significant place today, and will continue to in the near future, both academically and in terms of practical international economic relations.

Multilateralism is the system of principles, rules and institutions aimed at globally developing the collective disciplines affecting international trade in goods and services, including investment flows. The multilateral global trading system is developed within the WTO, especially under its main contractual frameworks, the General Agreement on Tariff and Trade (GATT) 1994 and the General Agreement on Trade in Services (GATS).

Regionalism is the set of regional subsystems resulting from preferential agreements -and is therefore discriminatory- as entered into by a group of two or more countries, contiguous or otherwise, whatever their modalities and objectives over and above economic and trade modalities and objectives may be. As such, these subsystems are exceptions to the principle of non-discrimination and most-favored-nation treatment -both cornerstones of the WTO's multilateral global trading system. From the WTO's perspective, these subsystems have their own objectives, rules and institutions.

The importance of the connection has grown in recent years since the Uruguay Round, the creation of the WTO and North American Free Trade Agreement (NAFTA), the expansion of the European Union (EU), the progress in negotiations of North/South free trade agreements -including the FTAA, Asia-Pacific Economic Cooperation (APEC), free trade agreements with the EU, free trade agreements concluded by the United States (US) and other countries with Mexico and Chile in the Latin-American arena, and the beginning of the negotiating process between MERCOSUR and the EU-, and the increasing array of free trade and integration agreements between developing countries, e.g. in LAIA, where one of the most economically significant is MERCOSUR.

The link between bi- or multilateral regional preferences and the multilateral global trading system is also one of the most important issues on the agenda of the Doha negotiating round within the framework of the WTO.

There has been a significant growth in the related bibliography as a result, with many contributions offering multidisciplinary approaches, and taking all factors, not just commercial ones, into account. They therefore come under the broader theoretical framework of international relations, and are not confined to the more restricted framework of international trade (Thorstensen [2001] pp. 237-254; Jackson [2000] pp. 99-112; Dam [2001] pp. 131-147; Lafer [1998] pp. 49-53; Hoeckman & Kostecki [2001] pp. 346-368; Bhagwati [1999] pp. 31-44; Messerlin [1999] pp. 45-86, and Roessler [1993] pp. 311-325).

Recent experience allows us to make some observations about the interaction between the multilateral global trading system and preferential regionalism with respect to international commercial and economic relations:

1) In terms of international trade, both the multilateral global system and preferential regionalism, as accurately expressed in the late 20th century, are political, economic and legal/institutional realities deeply rooted in their respective environments, and will continue to be part of the world scenario in the foreseeable future. Each system has its own logic and dynamics. The suppression of either reality could only be imagined in theoretical terms.

The multilateral global trading system reflects a deeper process with a clear political, economic and cultural dimension, namely, the growing and apparently irreversible globalization of the world economy and world politics.

Preferential regionalism reflects the existence of international subsystems where deep forces maintaining the distinction between "us" and "them" -the EU, MERCOSUR, NAFTA- reach far beyond the commercial sphere, responding from the moment of foundation to powerful political or even strategic reasons. These subsystems are nourished by their member countries sharing geographical, but above all, historical, strategic and cultural space. Yet preferential regionalism also reflects the international trade negotiating strategies that drive the growing numbers of bilateral free trade agreements between nations with economic and even political affinities, but no geographical proximity.

In terms of trade and economies, regionalism between neighboring countries is usually only part of a broader process aimed at generating spaces of peace, political stability

and democracy, where the logic of integration deeply rooted in open society values is prevalent. These progressive processes seek sustainability in social cohesion as both a central value and a privileged competitive global tool.

2) Multilateralism and regionalism are not necessarily contradictory forces in the building of a global system of international trade and economic relations based on principles of free trade and a reasonable balance between the interests of different nations.

On the contrary, since the creation of the European Economic Community (EEC) with the formation and enlargement of a single market, through to today's monetary union, there has been a constant interaction between the achievements of this regional experience with those occurring at the multilateral global level and in other regions.

The snowball effect of RPAs is translated into what has been labeled *competitive regionalism*, and into the driving forces of multilateral global trade negotiations themselves. The concern for competitive preferential regionalism is also a factor that has influenced the consensus achieved at the global multilateral level, as was in evidence at the Uruguay Round, and will be at Doha.

At the same time, however, the development of multilateral global trade disciplines, especially since the conclusion of the Uruguay Round, has conditioned the development of regional preferential schemes, leaving less room for the development of the much dreaded temptation to develop real or mythical commercial fortresses.

The phantom of *stumbling blocks* -made popular in the academic literature by Bhagwati's 1991 statement- (Bhagwati [1991]) has not come back to haunt us, even though there is room to believe that not all aspects of regional preferential manifestations fit comfortably into the concept of *building blocks*.

Special attention deserves to paid here to the potentially discriminatory effects arising from RPAs -especially in terms of access conditions by third countries- which are not the result of any geographical regional international subsystem, and which involve countries with no direct physical linkage.

3) Principles and rules, both multilateral and regional, interact on various levels.

Increasingly, RPAs -whatever their modality, be they free trade area or customs union- or the multiple hybrids we might observe in practice are governed by WTO rules. Their international legitimacy depends largely upon their conformity with Article XXIV and other contractual commitments taken on at the WTO, such as the above-mentioned Enabling Clause.

At the same time, the *WTO-plus* nature of RPAs in some cases establishes precedents that impact future global and regional multilateral negotiations, a case in point being NAFTA. The example will hopefully be repeated with the free trade agreement entered into by the US and Chile -at least for the US.

The interaction between multilateral global trade rules and regional preferences also has practical relevance when examined in the light of the domestic law of countries that are simultaneously members of the WTO and one or several RPAs. This is more evident with countries such as Argentina, where the Constitution guarantees the supremacy of treaties over national legislation. This will be dealt with later.

4) The trend in multilateralism and preferential regionalism not only toward peaceful coexistence, but constructive complementation, could be reinforced in at least three areas:

• At the *multilateral level*, to the extent that there has been a strengthening of WTO mechanisms designed to guarantee the dynamic compatibility of RPAs with multilateral global principles and rules.

Various different specialists have suggested a number of practical ideas about this (Serra *et al.* [1997] pp. 41-56; McMillan [1993] pp. 292-310). These mainly involve giving shape to collective disciplines about rules of access to the various different preferential agreements in order to avoid discrimination against countries with potential access; strengthening the rules to avoid the discriminatory effects that may result from the specific origin rules of free trade agreements; carrying out impartial and effective monitoring of the development of RPAs in light of multilateral global commitments; guaranteeing maximum transparency in RPA rules and implementation; and expediting access of particulars to the utilization of dispute resolution mechanisms in cases where an RPA clearly clashes with the principles and rules of the multilateral global system, thus weakening or nullifying their efficacy.

The idea at this level would be to believe in the global vocation of RPAs, while monitoring it closely and strengthening its effectiveness just in case.

• At the *regional* and indeed *interregional levels*, to the extent that RPA member countries carry out their express political will to keep to the commitments adopted at the WTO, within the rules applicable to their reciprocal relations and foreign trade policies.

To this end, an RPA's genuine will to *stability and permanence* is essential; that is, it cannot be perceived as a *disposable* instrument of foreign trade policy. It is this will - together with opening to the rest of the world- that confers legitimacy on preferential treatment from the perspective of the multilateral global trading system.

At the same time, consistency contributes to protecting the interests of smaller countries, especially in the cases of RPAs characterized by obvious asymmetries in the size and degree of development of their partners' respective markets. It also contributes to one of the central goals of a process of open preferential regionalism, namely, the creation of a predictable framework to attract investment from global competitors interested in introducing their investments and rendering services via networks beyond the limited dimension of a region.

• At the *national level,* to the extent that each country is capable of developing international economic insertion strategies to allow them to take maximum advantage of the broader operation margins allowed by the end of the bipolar Cold War world and economic globalization, and capitalize on today's greater degree of permissibility in order to profit from all the opportunities of economic competition on a global scale.

This leads to the seeking out of foreign commercial alliances that are neither exclusive nor excluding, in spite of privileging the strategic alliance with the contiguous region as the core of such a strategy.

This is more apparent from the recent trend to conceptually and practically assert the idea of integration in the world and in a given region, while at the same time privileging the national interest of creating stable, flexible and dynamic external environments favorable to domestic efforts toward the consolidation of democracy, economic modernization, social cohesion, and competitive insertion, both in a single region and throughout the world.

The concept of *network integration* (Castels [1998] pp. 330-332), with its institutional consequences, is becoming the counterpart of firms' development of trade and production networks on a global and regional scale. In this concept, lies one of the keys to understanding the dynamic, complementary relationship between global multilateralism and preferential regionalism, as perceived from an unavoidably privileged angle by both countries and firms.

It is in this context that we should approach and reinforce the arguments aimed at achieving the development of collective disciplines regarding RPA's within the WTO

framework, especially regarding those that do not reflect the commercial dimension of natural geographical regionalisms.

These collective disciplines may be a key factor in ensuring the preservation of their *rule-oriented* as opposed to *power-oriented* nature, not only of the multilateral global trading system but of each individual RPA (Jackson [2000] pp. 6-10) With a predominantly *rule-oriented* approach, we may finally find the answer to Bhagwati and many others' legitimate concern about the potentially negative effects caused by a proliferation -or "epidemic"- of RPA's, conceived mainly as instruments of international power, and not necessarily as a means of advancing the expansion and freedom of global trade.

IV. RPAs Implemented as Part of Broader Agreements: The LAIA

A wide range of RPAs between Latin-American countries are to be found in the framework of LAIA. The transformation of the LAFTA into LAIA in 1980 was aimed chiefly at facilitating the implementation of RPAs between peers or groups of member countries open to other partners, but with preferences not automatically extendible to all of them.

The LAIA has become a framework for the implementation of RPAs between some of its member countries, notwithstanding its more general objectives and other functions -including the achievement over time of a Latin-American common market. It complies or may comply in relation to the expansion and liberalization of trade and economic cooperation between partners.

Specifically and in theory -at this level at least- the LAIA guarantees a regional system of collective disciplines about the circumstances, modalities and procedures that a group of partners -two or more, but less than the total- have to use when developing trade preferences not applicable to other partners -in other words, to discriminate with respect to other partners. A key rule prescribes that these agreements be submitted for consideration to all other partners and remain open to access through prior negotiation.

In practice, however, LAIA's main impact has been to develop a register of RPAs that sets forth discriminations between partners, covering them legally in GATT through the application of the Enabling Clause. There has been little progress in extending these preferences to the other partners, nor in the development of another instrument foreseen by the 1980 Treaty of Montevideo, namely, to build a system of regional preferences as a step toward a common market, through regional scope agreements involving all member countries.

The fact that LAIA's legal system has been perceived by businessmen as being of poor quality, where rules can easily be left aside or changed according to circumstances, could be seen as one of the reasons for the extremely limited nature of its practical impact.

The 1980 Treaty of Montevideo that created LAIA was notified in GATT under the Enabling Clause. Since then the Secretary has periodically reported to the WTO on RPAs implemented within its jurisdiction via the WTO Commerce and Development Committee.

What is the extent of the *partial scope agreements* (Articles 4 and 7) foreseen by the 1980 Treaty of Montevideo? (Peña [2000]). The question is a germane one, considering the practice sometimes followed in the implementation of RPAs between member countries.

In the case of Argentina at least, it has been understood that these RPAs -implemented in the form of partial scope agreements according to LAIA norms- come

into force and are applicable in the country's domestic legal system, since their *protocolización*, or registration, with LAIA's General Secretary, and the notification of this record to Customs pursuant to Decree 415/91.

This practice stemmed from the fact that the Treaty of Montevideo allowed the Argentinian Executive Power to conclude agreements in simplified form when establishing the figure of partial scope agreements, that is, without submitting them to the Congress for approval. Moreover, the National Supreme Court endorsed this procedure in its judgment of May 7, 1998, in "Dotti, Miguel A. and Others on Smuggling".

What is really being established here by the 1980 Treaty of Montevideo? Two provisions are fundamental to a full comprehension of its text. First, Article 4 provides that "for fulfillment of the basic functions of the Association foreseen by Article 2 of the present Treaty, the member countries establish an area of economic preferences, composed of a regional preference on tariffs, agreements of regional scope and agreements of partial scope". Second, Article 44 of the Treaty provides that "the advantages, favors, franchises, immunities and privileges that the member countries apply to products coming from or destined to any other country whether member or non-member, by decisions or agreements not foreseen in the present Treaty or in the Cartagena Agreement, will immediately and unconditionally be extended to the remaining member countries".[3] The Third Section of the Treaty, from Articles 7 to 14, develops Article 4 in terms of partial scope agreements. Thereafter, member countries are regulated by Resolution 2 of LAIA's Council of Ministers. Article 5 of this stipulated the procedures for agreement within the framework of LAIA.

At no time does the 1980 Treaty of Montevideo or its regulation say anything direct or indirect about the way these agreements are to take effect in the respective domestic legal systems. This is an issue defined at the constitutional level of each member country, and to which the Treaty does not refer. Therefore, the issue of how a partial scope agreement takes effect in a domestic legal system shall be answered on a case-to-case basis, according to the respective constitutional provisions. It does not seem sustainable then to argue that the Treaty introduces the figure of agreements in simplified form when this was not foreseen by the respective Constitution.

This should warrant no attention, as the real significance was to define rules for one of the modalities by which member countries may agree reciprocal preferences or any commitments linked with the Treaty's objectives between themselves -in this case, limited only to a group of member countries- without applying the provisions of Article 44, i.e. the most-favored nation clause. To put it succinctly, the Treaty focuses on regulating the use of exceptions to Article 44, the true cornerstone of its legal architecture.

In any case, the way LAIA approaches the issue of the conciliation of RPAs implemented within its framework, and its broader regional objectives, could be a precedent to bear in mind in the FTAA negotiations. It seems possible that, if further developed using the experience already acquired, and if effectively applied in its two central components -control by the other partners and the right to access through negotiations by the other interested partners- LAIA's system of partial scope agreements could eventually serve as a precedent, in the event that the FTAA's architecture intends to combine the rules for the whole hemisphere with the RPAs developed between certain member countries.

V. The Validity of RPAs in Member Countries' Domestic Laws: The MERCOSUR & Argentina

Each country's domestic legal order, normally enshrined in its Constitution, determines the procedure for undertaking international commitments by way of Treaties agreed with third countries (Jackson [2000] pp. 6-10). We frequently observe a distribution of competences between the Executive Power, which negotiates and signs a treaty, and the Congress, which passes it. After passing it, the Executive Power ratifies the treaty, which takes effect pursuant to its provisions. In some cases, a Constitution will explicitly foresee, or give some reason to admit, agreements in simplified form -or executive agreements, which do not require Congressional approval.

At the same time, domestic law determines the rank of a treaty within a country's legal hierarchy. In some cases -like Argentina- a highly evolved form is used. This consists of explicitly conferring a superior legal status on international treaties. In other words, subsequent laws -still less so, more minor normative acts- cannot modify the rights acquired by citizens under the provisions of the relevant treaty.

For any country -in this case, Argentina- the international collective disciplines accepted at the WTO and at an RPA (e.g. MERCOSUR) restrict the room for governmental maneuver in the formulation and implementation of public foreign trade policies, and in international trade negotiations. These restrictions operate as counterweights to the advantages they offer, namely, access to other markets and predictable rules affecting the international competitiveness of firms. They are the result of the development of an international system of trade and investment based on legal rules adopted by consensus. They enforce a certain order in the competition for world and regional markets. It is not however a perfect legal system. But in terms of its share in world trade, for any relatively marginal country -as consequently more of a *rule-taker* than a *rule-maker*- this is a more reasonable option than having the implementation of rules decided upon by criteria of power.

These are collective disciplines undertaken by the sovereign will of a country, and generally require Congressional approval. In the specific case of Argentina, as per the 1994 Constitution, treaties expressing these disciplines are above domestic law. As such, they generate rights enforceable at jurisdictional proceedings in the country.

In the case of the WTO, the 1994 Marrakech Agreements define rules for the world trade in goods and services. They have implications for what member countries -including Argentina- may or may not do with their foreign trade, and among other things, with their intellectual property and investment legislation. They create rights and obligations enforceable by and against WTO member countries. In some cases, they are also directly enforceable at the domestic level too. Dispute resolution mechanisms guarantee their compliance. Disregarding WTO rules involves a cost for any country, not always apparent in the short term.

The Treaty of Asunción simultaneously created MERCOSUR, and originated legal commitments and collective disciplines to be undertaken within its framework. It provided a legal basis for unrestricted free trade between partners. This involves the rights acquired by the citizens and firms of the member countries to export and import goods to and from other partners, without tariffs or any other kind of restriction.

Among the commitments undertaken in the Treaty of Asunción is a common external tariff on conclusion of the transitional period. The 1994 Decision in this regard can be modified by consensus via another Decision by MERCOSUR Council or, in certain cases,

by the Common Market Group -the executive body. This means that, through its competent agencies, the partners have entrusted MERCOSUR with any valid modification to its import or export tariff. Yet it is not valid to do so unilaterally. The idea of having a common external tariff was part of the agreed strategy between Argentina and Brazil in June 1990. Hence, Chile did not participate in the creation of MERCOSUR, in spite of being invited to.

If any MERCOSUR partner were to put aside the commitments undertaken pursuant to the Treaty of Asunción, they would have to propose its subsequent modification or complementation (which would have to result from another treaty -generally named *Protocol*- with agreement from all partners and approval from every Congress), or to give notice of termination according to established procedure. Even so, the commitments undertaken in the Program of Trade Liberalization would remain in force for two more years. This would mean that imports coming from partners would continue to have zero tariffs, with no valid restrictions possible of any kind, save those contained in Article 50 of the 1980 Treaty of Montevideo, for reasons of public health and safety, for example.

Any breach by one of the partners may give rise either to a dispute resolution procedure under the Brasilia Protocol, or to an appeal to national jurisdictional proceedings in order to protect acquired rights. In the case of Argentina, we should not in theory overlook the fact that, if a foreign investor could prove that a breach of commitments in the Treaty of Asunción -e.g. on intra-MERCOSUR tariffs- has caused them significant damage, they may end up appealing to domestic jurisdictional, or ultimately to international arbitral proceedings, in order to secure any relevant compensatory damages. That being the case, the foreign investor could turn to some of the investment agreements signed by Argentina, all interrelated by most favorable treatment. Naturally, in addition to the damage, it would be necessary to prove that the investment was made on the basis of the commitments undertaken under MERCOSUR.

Unilateral behaviors contrary to the commitments undertaken at the WTO and MERCOSUR may affect a country's foreign credibility, and have a significant impact on investment decisions, especially those of multinational corporations. Those requiring greater scale may opt to settle in Brazil, to be guaranteed access to the largest market in South America. In any event, they would have legally assured access to the market of the other partners, at least up to two years after a country eventually gives notice of termination of the Treaty of Asunción.

According to the Treaty of Asunción, we can infer that member countries have formally undertaken the obligation of negotiating any international trade commitment affecting the common external tariff with their MERCOSUR partners, except in those cases where, by consensus, the partners would have accepted individual negotiations within the ordinary normative frameworks, as was the case with Mexico.

In the specific case of Argentina, we must highlight one legal problem because of its legal and practical significance (Peña [2000]). After the 1994 constitutional reform, the usual practice pursuant to Decree 415/91 was to incorporate commitments undertaken in MERCOSUR by way of LAIA *partial scope agreements* into Argentina's domestic legal system. They could not modify the Treaty of Asunción. In fact, were they to do so, they would be contrary to constitutional provisions and, therefore, judicially challenged since, on the one hand, the Constitution reformed in 1994 does not recognize "executive or simplified agreements" (as happens in other countries' legal systems, which explicitly or implicitly recognize this concept); on the other hand, they could not stand above the law. They would only have the legal status of an act of Executive Power. Were they to breach Legislative powers, they would be invalid.

What exactly does Decree 415/91 stipulate in this context? Article 1 prescribes that agreements underwritten by Argentina within LAIA's legal framework will take effect under the conditions and from the dates agreed for each one, notwithstanding their publication in the Official Gazette. Article 2 establishes that, for the application of the agreements mentioned in Article 1 on Argentinian territory, the Undersecretary of Industry & Trade of the Ministry of the Economy will forward to the National Customs Administration a duly certified copy from the Secretary General of LAIA and the Argentinian representation before this Association, requesting no other formality. This provision, which should be read in light of the provisions contained in Article 1, modifies a prior regulation (Decree 101/85), foreseeing the need for joint resolution from the Foreign Council and the Ministry of the Economy. This was the reason for Decree 415/91. Its practical purpose was to simplify the necessary procedure of notifying Customs about preferences negotiated under partial scope agreements, or about eventual modifications to trade preferences to be negotiated later. Whence the expression "without requesting any other formality".

Therefore, this decree cannot be said to have altered constitutional powers regarding the negotiation and approval of treaties. Proof lies in the fact that MERCOSUR was created by an international treaty duly approved by the Congress, notwithstanding the requirement to put its text in partial scope agreement ACE 18 in order to bring its preferences into line with the provisions of the Treaty of Montevideo, and avoid its automatic extension to the other member countries by virtue of the provisions of Article 44. Furthermore, Article 18 of ACE 18 contains the so-called *bolt clause*, stipulating that: "any modification to the present Agreement can only be made by agreement of all signatory countries and will be subject to the previous modification of the Treaty of Asunción according to the constitutional procedures of each signatory country".

It should also be remembered that Decree 415/91 precedes the 1994 constitutional reform which, by giving international treaties a status superior to domestic law, bestowed a different perspective on the interpretation of constitutional provisions concerning the negotiation and approval of treaties.

If practice recommends the flexibility of procedures to enter into and put into force international agreements within the framework of one of the treaties mentioned above, we should turn to an explicit legislative act from the Legislative Power or, if necessary, to the modification of the above treaties. Decree 415/91 offers only a flexible regulation for notifying Customs about concrete trade preferences granted in the setting of agreements duly put into effect, or their potential modifications. This has been the case with the preferences included in agreements executed within the framework of LAIA prior to the 1994 constitutional reform.

The issue is not academic. It involves the legal security of international economic relations in Argentina. It has to do with the reinforcement of Congress's participation in the integration process. It relates to the transparency of governmental acts, particularly that of the rules implemented in the domestic legal system, bearing in mind that actual practice allows major international agreements not to be published in the Official Gazette. This has been the case with automobile sector regulations between Argentina and Brazil, and even those of MERCOSUR. It has also been the case with some of the free trade agreements concluded with other LAIA countries such as between Chile and Bolivia.

The issue is even more serious when a simplified partial scope agreement may eventually introduce changes to rights acquired under treaties like the Treaty of Asunción that are approved by the Congress. In fact, this practice may allow the bilateral modification

of rules or procedures established in precise form by treaties like Asunción. Furthermore, it may put these bilateral agreements outside the reach of the Brasilia Protocol, which guarantees an efficient system of dispute resolution -though one where there is room for improvement.

In the case of MERCOSUR at least it is then recommendable to articulate more sound and flexible procedures for the incorporation into the domestic law of each member country of new regional agreements deriving from the Treaty of Asunción or concluded with other LAIA members. These procedures should result from legal instruments agreed by the member countries through Protocols duly approved by each Congress.

In any case -and this is at least clear for Argentina- the above practice is one of the reasons why MERCOSUR is perceived by investors as a low quality *rule-oriented* process. The fact that many rules formally approved by MERCOSUR institutions have not been enforced, further contributes to its poor image, and may help to explain its problems of efficacy, or even social legitimacy.[4]

VI. Conclusions

RPAs between both neighboring and non-neighboring countries are today an important dimension of the realities of international economic relations. They are part of the international landscape. Even if, from a theoretical point of view, it may be wise to recommend the limitation of the trend toward new RPAs, it seems difficult to imagine countries complying with any such recommendations.

In addition, it seems difficult to avoid all the existing or proposed RPAs being presented as highly consistent with the principles, objectives and rules of the multilateral global trading system: they all prefer to define themselves as models of *open regionalism*.

Quite the reverse, what may become necessary and possible is to improve global collective disciplines to assure that a higher number of old and new RPAs can really be WTO-consistent.

The main challenge ahead is therefore to ensure that RPAs can be consistent with the principles and collective disciplines of the multilateral global trading system. This means RPAs could be an effective *building block* toward a more integrated and open global economy. In addition, especially when they include developing countries, they could make a real contribution to the development of relatively smaller, poorer economies.

To obtain these objectives RPAs should always involve permanent commitments to open up the markets of member countries. In addition, they should include rules allowing third countries to become members through negotiations. This should always be the case when an RPA involves non-neighboring countries and is not therefore part of a broader political and economic strategy to build a stable and peaceful geographically based regional subsystem.

Preserving the *rule-oriented* nature of a specific RPA -as against the *power-oriented* alternative- could be crucial for the defense of the national interests of less developed members. Low quality RPAs could be the result of poor rules of the game and of weak enforcement capacity. They might then play against the interests of smaller member countries, and in favor of more developed members. MERCOSUR could become an example of this.

But the *rule-oriented* approach could also be crucial in preserving the health of the multilateral global trading system. The proliferation of RPAs without strong collective disciplines to implement them could be very negative for free trade and development at the global level.

From this point of view, strengthening the monitoring capacity of the WTO and the implementation of a reviewed Article XXIV of GATT 1994 should be one of the tangible results of the Doha Development Agenda negotiations. Among other requirements, strong collective disciplines concerning their rules of origin should be included in the review process of Article XXIV. Strengthening the effective role of the Regional Agreements Committee of the WTO should be also a priority.

A reasonable degree of interaction between the rules of both WTO and RPA legal systems could enhance predictability, and thus improve conditions for attracting investments and global competitors to developing countries.

This also involves strengthening the *rule-oriented* approach in the implementation of RPAs at the domestic level and within broader RTAs (those enabling the development of a network of other RTAs) as is the case with LAIA, and may also be with the FTAA.

LAIA's rules and experiences could in a way serve as a useful precedent for the final architecture of the FTAA, especially considering the need to conciliate the hemispheric preferential system with subregional agreements such as NAFTA and MERCOSUR.

Notes

[1] I use the concept of regional preferential agreements (RPAs) to include all kind of trade preferential agreements (TPAs) between both contiguous and non-contiguous countries.

[2] See Bhagwati & Panagariya [2003] p. 15. See also the interview with Professor Bhagwati in Clarín [2003]. For a reply to Professor Bhagwati's arguments, see Griswold [2003] p. 13.

[3] Article 44 was then modified because of Mexico's participation in NAFTA.

[4] For a more detailed analysis, see Machlup [1977], see also Nolde [1924] and Anderson & Norheim [1993]. The author has for many years been issuing warnings about the economic and political implications of MERCOSUR as a low-quality, "rule-oriented" process (see Peña [1996] pp. 395-408; Peña [2002] pp. 271-288).

Bibliography

ANDERSON, K. AND H. NORHEIM. "History, Geography and Regional Economic Integration", in Anderson, K. and R. Blackhurst (Eds.) *Regional Integration and the Global Trading System*. New York, USA: St. Martin's Press, pp. 19-51. 1993.

BHAGWATI, J. N. "Multilateralism and Regionalism in the Post-Uruguay Round Era: What Role for the US", in Memedovic O., Kuyvenhoven A. and Molle W. T. M. (Eds.), *Multilateralism and Regionalism in the Post-Uruguay Era: What Role for the EU*, NEI, Kluwer Academic Publishers, London. 1999.

_____. *The World Trading System at Risk*, Princeton University Press, Princeton, New Jersey, USA. 1991.

_____ AND A. PANAGARIYA. "Bilateral trade treaties are a sham", in *Financial Times*, London. 14 July, 2003.

CASTELS, M. *End of Millennium*. Ames, Iowa, USA: Blackwell Publishing. 1998.

CLARÍN. Interview with Professor Bhagwati. Buenos Aires, Argentina. June 27, 2003.

DAM, K. W. *The Rules of the Global Game: A New Look at US International Economic Policy*. Chicago, USA and London, UK: University of Chicago Press. 2001.

GRISWOLD, D. "Bilateral Deals are no Threat to Global Trade" in *Financial Times*. London. 28 July, 2003.

HOECKMAN, B. M. AND M. M. KOSTECKI. *The Political Economy of the World Trading System.* Oxford, UK: Oxford University Press. 2001.

JACKSON, J. *The Jurisprudence of GATT and the WTO*. Cambridge University Press. 2000.

KAHLER, M. "El nuevo regionalismo y sus instituciones", in Bouzas R. (Ed.), in *Regionalización e integración económica: instituciones y procesos comparados*, Nuevohacer. Buenos Aires, Argentina: Grupo Editor Latinoamericano. 1997.

LAFER, C. *A OMC e a regulamentaçâo do comercio internacional: uma visâo brasileira*. Porto Alegre, Brazil: Livraria do Advogado. 1998.

MACHLUP, F. *A History of Thought on Economic Integration*. New York, USA: Columbia University Press. 1977.

McMillan, J. "Does Regional Integration Foster Open Trade? Economic Theory and GATT's Article XXIV", in Anderson, K. and Blackhurst, R. (Eds.), *Regional Integration and the Global Trading System*. Hemel Hempstead, England: Harvester Wheatsheaf. 1993.

Messerlin, P. A. "MFN-Based Freer Trade and Regional Free Trade: What Role for the EU?", in Memedovic, *et al.* (Eds.) *Multilateralism and Regionalism in the Post-Uruguay Round Era*. Dordrecht, Kluwer. 1999.

Nolde, B. "Les Unions Douanières" in *Droit et Technique des Traités de Commerce* Chap. 10, Recueil des Cours de l'Académie de Droit International, Vol. 8. The Hague, Netherlands. 1924.

Peña, F. "Reglas de juego e instituciones en el MERCOSUR", in *Revista de Derecho Privado y Comunitario*, N° 14. 1996.

_____. "Entrada en vigencia de acuerdos de la ALADI y del MERCOSUR", in *Revista La Ley*. Buenos Aires, Argentina. 28 September, 2000.

_____. "Reflexiones sobre el MERCOSUR y su futuro", in Hugueney Filho C. and Cardim C.H. (eds.) *Grupo de Reflexâo Prospectiva sobre o Mercosul*, MRE/IDB/IPRI/FUNAG, Brasilia, Brazil. 2002.

_____. "Concertación de intereses, efectividad de las reglas de juego y calidad institucional en el MERCOSUR", Report for the State of Law Program, Konrad Adenauer Foundation/MERCOSUR Network. May, 2003a.

_____. "Civil Society, Transparency and Legitimacy in Integration Processes and Trade Negotiations: MERCOSUR's Experience and Lessons for the Negotiations with the European Union", paper prepared for the Chaire MERCOSUR de Sciences Po Working Group on EU/MERCOSUR Negotiations, Annual Seminar. September, 2003b.

_____. "Consensual Integration Alliances: The Importance of Predictability and Efficacy in MERCOSUR Institutional Experience", Jean Monnet/Robert Schuman Paper Series 2 3, Miami European Union Center. Miami, USA: University of Miami. Available at *http://www.miami.edu/EUCenter/penafinal.pdf*. March, 2003c.

Roessler, F. "The Relationship between Regional Integration Agreements and the Multilateral Trade Order", in Anderson K. and R. Blackhurst (Eds.), *Regional Integration and the Global Trading System*. London, England: Harvester Wheatsheaf. 1993.

Serra, J. *et al*. *Reflections on Regionalism: Report of the Study Group on International Trade*, Carnegie Endowment for International Peace. Washington D.C., USA. 1997.

Snape, R. H. "History and Economics of GATT's Article XXIV", in Anderson, K. and Blackhurst, R. (Eds.) *Regional Integration and the Global Trading System*. New York, USA: St. Martin's Press. 1993.

Srinivasan, T. N. *Developing Countries and the Multilateral Trading System*. Boulder, Colorado, USA: Westview Press. 1998.

Thorstensen, V. *Organizaçâo Mundial do Comércio: As Regras do Comércio Internacional e a Nova Rodada de Negociaçôes Multilaterais*. Aduaneiras, São Paulo, Brazil. 2001.

Winham, G. *International Trade and the Tokyo Round Negotiation*. New Jersey, USA: Princeton University Press, Princeton. 1986.