

Exceptions to WTO Rules:

General Exceptions, Security Exceptions, Regional Trade Agreements (RTAs), Balance-of-Payments (BOPs) & Waivers

ESTIMATED TIME: 4 hours

OBJECTIVES OF MODULE 8

- Explain the general exceptions available to the Members under the WTO Agreements and the conditions for their application;
- introduce the exceptions for the protection of Members' essential security interests;
- explain the rules on regional integration contained in the WTO Agreements; and,
- introduce the BOP exception and waivers.

I. INTRODUCTION

As indicated in Modules 1-3, WTO Members are subject to several general obligations set out in the [General Agreement on Tariffs and Trade 1994](#) (GATT 1994).

The Most-Favoured-Nation (MFN) principle requires Members not to discriminate among imported products from other Members. The national treatment principle requires Members not to discriminate against imported products as opposed to domestic products. In regard to market access for goods, Members are required to act in accordance with their scheduled commitments on tariffs and not to apply tariffs beyond the bound levels unless these are renegotiated. In addition, Members are not generally allowed to impose quantitative restrictions (QRs) on market access for goods. Furthermore, Members are required to ensure that their non-tariff barriers (NTBs) (such as customs formalities) do not constitute unnecessary obstacles to trade.

Nevertheless, in certain circumstances, **WTO Members may derogate from these obligations, provided that they comply with certain conditions.** These exceptions, which will be examined in this Module, include:

- **General exceptions** - Right to take measures, for example, necessary to protect human, animal or plant life or health, which may restrict trade in goods (GATT 1994). Such measures cannot constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade. Similar general exceptions also apply to trade in services ([General Agreement on Trade in Services](#) (GATS)), whereas there are no general exceptions as such under the [Agreement on Trade-Related Aspects of Intellectual Property Rights](#) (TRIPS Agreement);
- **Security exceptions** - Right to take measures to protect essential national security interests, which may restrict trade in goods (GATT 1994). Similar security exceptions are allowed under the GATS and the TRIPS;
- **Exceptions for Regional Trade Agreements (RTAs)** - Right to depart from the MFN principle in order to grant preferential treatment to goods (GATT 1994) or service suppliers (GATS) from trading partners within a customs union or a free trade area without extending such treatment to all WTO Members;
- **Balance-of-payments (BOP)** – Right to take measures to safeguard a Member's external financial position and its BOPs; and,
- **Waivers** - Temporary waivers granted with the authorization of the other Members, in exceptional circumstances.

EXCEPTIONS	ARTICLES		
General Exceptions	Article XX of the GATT 1994	Article XIV of the GATS	No general exceptions provision under the TRIPS
Security Exceptions	Article XXI of the GATT 1994	Article XIVbis of the GATS	Article 73 of the TRIPS Agreement
RTAs	Article XXIV of the GATT 1994; and "Understanding on the Interpretation of Article XXIV of the GATT 1994" Paragraph 2(c) of the Enabling Clause*	Article V of the GATS	No provision on RTAs under the TRIPS
BOPs	Articles XII & XVIII:B of the GATT 1994; and, "Understanding of the BOPs Provisions of the GATT 1994"	Article XII of the GATS	No BOP provision under the TRIPS
Waivers	Article IX:3 of the Marrakesh Agreement Establishing the WTO (WTO Agreement establishing the WTO)		

Besides, remember that Members are allowed to apply **trade defence mechanisms** – see Module 5 - to remedy a situation of unfair competition (anti-dumping and countervailing measures) or a surge of imports (safeguard measures) when these are causing injury, subject to certain requirements. Even if these measures are not referred to as exceptions, they allow Members to impose, for example, tariffs above the bound levels or QRs (depending on the measure).

The rules on **special and differential treatment** for developing countries and least-developed country (LDC) Members, which address the special difficulties that these countries may face in implementing the WTO Agreements, will be introduced in Module 9.

* Paragraph 2(c) of the 1979 Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation (the "Enabling Clause") allows developing country Members to conclude among themselves RTAs on trade in goods.

II. GENERAL EXCEPTIONS

IN BRIEF

Article XX of the GATT 1994 governs the use of the general exception for trade in goods. It recognizes that Members **may need to apply measures for purposes such as the protection of public morals; human animal or plant life or health; and, the conservation of exhaustible natural resources.**

However, any measure adopted under the general exceptions provision must **meet the requirements set out in the sub-paragraphs of Article XX** – depending on the objective of the measure - **and its introductory paragraph ("the Chapeau")**. According to the Chapeau of Article XX, the measure must not be applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restrictions on international trade.

II.A. GENERAL EXCEPTIONS IN THE GENERAL AGREEMENT ON TARIFFS AND TRADE (GATT) 1994

[Article XX](#) of the GATT 1994 permits Members to take certain measures, otherwise prohibited by GATT 1994 provisions, subject to stipulated conditions. The purpose of Article XX is to ensure that commitments undertaken by the Members under the covered Agreements do not hinder the pursuit of legitimate policy objectives, such as the protection of human, animal or plant life or health, or the conservation of exhaustible natural resources. In addition, measures taken under Article XX must be applied by the Members in a manner consistent with the Chapeau of that provision.

In this regard, the Appellate Body Report has stated that the exceptions listed in **Article XX -paragraphs (a) to (j) relate to all of the obligations under the GATT 1994** (including not only the MFN and national treatment principles, but others as well) ([US – Gasoline](#), Appellate Body Report, p. 24; [US – Shrimp](#), Appellate Body Report, para. 121).

NOTE

A summary of the *US-Gasoline* case is provided at the end of this section.

II.A.1. STRUCTURE OF ARTICLE XX –TWO-TIER TEST

Article XX of the GATT 1994: *Two-Tier Test*

In order to be justified under [Article XX](#), a GATT 1994-inconsistent measure must go through a *two-tier test*:

- The measure at issue must fall under one of the exceptions – sub-paragraphs (a) to (j) - listed under Article XX - each sub-paragraph concerns different objectives and contains different requirements; and,
- The measure must be applied in a manner that satisfies the requirements of the Chapeau of Article XX.

(*US – Gasoline*, Appellate Body Report, p. 22)

The order of the test cannot be reversed because it reflects the fundamental structure and logic of Article XX of the GATT 1994 (*US – Shrimp*, Appellate Body Report, paras. 119). Therefore, in assessing an Article XX claim, panels should always start the analysis with the particular exception(s) invoked by a party (sub-paragraph(s)) and only after the measure at issue has been found to be falling within the scope of the claimed exception(s), should they consider whether the application of the measure satisfies the conditions of the Chapeau (*EC – Asbestos*, Panel Report, para. 6.20; *US – Shrimp* (Article 21.5), Panel Report, paras. 5.27-5.28).

II.A.2. APPLICATION AND INTERPRETATION OF EXCEPTIONS – ARTICLE XX (B), (D) AND (G)

As stated by the Appellate Body Report, paragraphs (a) to (j) comprise measures that constitute exceptions to substantive obligations established in the GATT 1994, because the domestic policies embodied in such measures have been recognized as important and legitimate in character (*US-Shrimp*, Appellate Body Report, para. 121). WTO Members have invoked the exceptions provided in [Article XX](#) to justify policies, among others, designed to protect human, animal or plant life or health -paragraphs (b)-, to secure compliance with laws or regulations -paragraphs (d)-, or to conserve exhaustible natural resources -paragraph (g). GATT 1994/WTO case law has set up criteria for the interpretation of these paragraphs. Our study of Article XX will focus on the exceptions provided in paragraphs (b), (d) and (g).

The Appellate Body Report has ruled that, under the GATT 1994, it is within the authority of a WTO Member to set the public health or environmental objectives it seeks to achieve (*US – Gasoline*, Panel Report, para. 7.1; Appellate Body Report, p. 30); as well as the level of protection that it wants to obtain, through the policy it chooses to adopt (*EC – Asbestos*, Appellate Body Report, para. 168; *Brazil – Retreaded Tyres*, Appellate Body Report, para. 140). However **Members are bound to implement these objectives through measures consistent with the requirements provided in Article XX of the GATT 1994.**

In general, there are two steps in the application of Article XX exceptions under the sub-paragraphs (prior to further assessment under the Chapeau):

- a. **Identify whether the policy pursued through the measure falls within the range of policies provided in sub-paragraphs (a) to (j) of [Article XX](#)**, for example, designed to protect human, animal or plant life or health (XX(b)), to secure compliance with laws or regulations which are not inconsistent with the provisions of the GATT 1994 (XX(d)), or to conserve exhaustible natural resources (XX(d)) (see also box below).

Article XX of the GATT 1994: 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 Member of measures:

- (a) Necessary to protect public morals;
- (b) necessary to protect human, animal or plant life or health;
- (c) relating to the importations or exportations of gold or silver;
- (d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of [Article II](#) and [Article XVII](#), the protection of patents, trade marks and copyrights, and the prevention of deceptive practices;
- (e) relating to the products of prison labour;
- (f) imposed for the protection of national treasures or artistic, historic or archaeological value;
- (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption;
- (h) undertaken in pursuance of obligations under any intergovernmental commodity agreement which conforms to criteria submitted to Members and not disapproved by them or which is itself so submitted and not so disapproved;
- (i) involving restrictions on exports of domestic materials necessary to ensure essential quantities of such materials to a domestic processing industry during periods when the domestic price of such materials is held below the world price as part of a governmental stabilization plan; provided that such restrictions shall not operate to increase the exports of or the protection afforded to such domestic industry, and shall not depart from the provisions of this Agreement relating to non-discrimination; and,
- (j) essential to the acquisition or distribution of products in general or local short supply; provided that any such measures shall be consistent with the principle that all Members are entitled to an equitable share of the international supply of such products, and that any such measures, which are inconsistent with the other provisions of the Agreement shall be discontinued as soon as the conditions giving rise to them have ceased to exist. The Members shall review the need for this sub paragraph no later than 30 June 1960.

- b. Determine whether the legal elements of the relevant paragraph are met. This examination comprises, for example, the "necessity test" for paragraphs (b) and (d), and the analysis if a measure "relates to" for paragraph (g).

LEGAL TEXT	LEGAL ELEMENTS
<p>Article XX (b): Necessary to protect human, animal or plant life or health</p>	<p>(1) the policy in respect of the measures for which the provision is invoked falls within the range of policies designed to protect human, animal or plant life or health; and,</p> <p>(2) the inconsistent measures for which the exception is being invoked is "necessary" to fulfil the policy objective.</p> <p><i>(US – Gasoline, Panel Report, para. 6.20)</i></p>
<p>Article XX (d): Necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including (...)</p>	<p>(1) the measure must be one designed to secure compliance with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994; and,</p> <p>(2) the measure must be "necessary" to secure such compliance.</p> <p><i>(Korea – Beef, Appellate Body Report, para. 157)</i></p>
<p>Article XX (g): Relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption</p>	<p>(1) the measure is concerned with the conservation of exhaustible natural resources;</p> <p>(2) the measure "relates to" the conservation of "exhaustible natural resources"; and,</p> <p>(3) the measure is made effective in conjunction with restrictions on domestic production or consumption.</p> <p><i>(US – Shrimp, Appellate Body Report, paras. 127, 135, 143-145)</i></p>

a. Identification of the Policy Pursued through the Measure

1. PROTECTING HUMAN, ANIMAL OR PLANT LIFE OR HEALTH - [ARTICLE XX \(B\)](#)

There are several cases where panels and the Appellate Body have ruled that certain measures fell within the range of policies designed to protect human, animal or plant life or health. The following box includes some examples.

Examples of Measures Falling Within the Scope of Article XX(b) of the GATT 1994

In *Thailand – Cigarettes*, a GATT Panel acknowledged that:

- "smoking constitutes a serious risk to human health and that consequently measures designed to reduce the consumption of cigarettes fall within the scope of Article XX(b)" (*Thailand – Cigarettes*, GATT Panel Report, para. 73).

In the two *Tuna* disputes, a GATT Panel and the parties accepted - implicitly in *US – Tuna (Mexico)*, explicitly in *US – Tuna (European Economic Community (EEC))* - that:

- **the protection of dolphin life or health was a policy that could fall under Article XX(b)** (*US - Tuna (Mexico)*, GATT Panel Report, unadopted, paras. 5.24-5.29; *US – Tuna (EEC)*, GATT Panel Report, unadopted, para. 5.30).

In *US – Gasoline*, the Panel and the parties agreed that:

- "the policy to reduce air pollution resulting from the consumption of gasoline was a policy within the range of those concerning the protection of human, animal and plant life or health mentioned in Article XX(b)" (*US – Gasoline*, Panel Report, para. 6.21).

In *EC – Asbestos*, the Panel found and subsequently the Appellate Body confirmed that:

- "chrysotile-cement products pose a risk to human life or health" and thus "the EU policy of prohibiting chrysotile asbestos falls within the range of policies designed to protect human life or health" (*EC – Asbestos*, Panel Report, paras. 8.186, 8.193-8.194; Appellate Body Report, para. 162).

In *Brazil – Retreaded Tyre*, the Panel found and subsequently the Appellate Body confirmed that:

- the Brazilian policy of reducing exposure of the risks to human, animal, and plant life and health arising from the accumulation of waste tyres falls within the range of policies covered by Article XX (b) (*Brazil – Retreaded Tyres*, Panel Report, para. 7.115; Appellate Body Report, para. 134).

2. SECURING COMPLIANCE WITH LAWS OR REGULATIONS WHICH ARE NOT INCONSISTENT WITH THE PROVISIONS OF THE GATT 1994 - [Article XX\(d\)](#)

To find a measure falling within the policy range of Article XX (d), the measure must be designed to secure compliance with laws or regulations which are not inconsistent with the provisions of the GATT 1994.

A GATT Panel in *EEC – Parts and Components*, interpreted the phrase "**to secure compliance**" with laws and regulations to mean "to enforce obligations under laws and regulations" (para. 5.17). The Appellate Body further clarified that a measure can be said to be designed "to secure compliance" when it is suitable or

capable of securing compliance with the relevant laws and regulations, even if the measure cannot be guaranteed to achieve its result with absolute certainty. The Appellate Body also noted that the "use of coercion" is not a necessary component of the measure (*Mexico – Taxes on Soft Drinks*, Appellate Body Report, para. 74).

With respect to the term "**laws or regulations**", the Appellate Body stated that the use of the word "including" clearly denotes that Article XX (d) is susceptible of application in respect of a wide variety of laws and regulations to be enforced (*Korea – Beef*, Appellate Body Report, para. 162). This term covers rules that form part of the domestic legal system of a WTO Member, including "rules deriving from international agreements that have been incorporated into the domestic legal system of a WTO Member or have direct effect according to that Member's legal system" (*Mexico – Taxes on Soft Drinks*, Appellate Body Report, para. 79).

3. CONSERVATION OF EXHAUSTIBLE NATURAL RESOURCES - ARTICLE XX(G)

[Article XX\(g\)](#) concerns measures taken in pursuit of conservation of exhaustible natural resources. In [US - Shrimp](#), the Appellate Body held that the text of Article XX(g) **covers not only the conservation of "mineral" or "non-living" natural resources, but also living species**, which are in principle "renewable", and are in certain circumstances indeed susceptible of depletion, exhaustion and extinction, frequently because of human activities (*US – Shrimp*, Appellate Body Report, para. 128).

Examples of Measures Falling Within the Scope of Article XX(g) of the GATT 1994

In several GATT/WTO cases, various measures have been found falling into the range of policies of Article XX(g), including those to conserve: **tuna** (*US – Canadian Tuna*, GATT Panel Report, para. 4.9); **salmon and herring stocks** (*Canada – Herring and Salmon*, GATT Panel Report, para. 4.4); **dolphins** (*US - Tuna (EEC)*, GATT Panel Report, unadopted, para. 5.13); **clean air** (*US – Gasoline*, Panel Report, para. 6.37); and, **sea turtles** (*US – Shrimp*, Appellate Body Report, para. 134).

b. Specific Requirements under Article XX(b), (d) & (g)

Different terms are used in respect of the different categories of measures described in paragraphs (a) to (i) of [Article XX](#). According to the Appellate Body, **the use of different terms reflects different kind or degree of connection or relationship between the measure under appraisal and the state interest or policy sought to be promoted or realized** ([US – Gasoline](#), Appellate Body Report, pages 17 and 18).

1. "NECESSITY TEST" UNDER ARTICLE XX(B) AND (D) - "WEIGHING-AND-BALANCING" PROCESS

Paragraphs (b) and (d) of Article XX set forth a "**necessity test**": the measures at issue must be necessary either "to protect human, animal or plant life or health" (XX(b)) or to "secure compliance with laws or regulations" (XX(d)). In *Thailand – Cigarettes*, the Panel concluded that the term "necessary" has the same meaning under paragraphs (b) and (d) (*Thailand – Cigarettes*, GATT Panel Report, para. 74).

The ordinary meaning of the word "necessary" has been clarified in *Korea – Beef*, where the Appellate Body stated that the reach of this word is not limited to what is "indispensable" or "of absolute necessity" or "inevitable". The term "necessary" refers to a range of degrees of necessity. At one end of this continuum lies

"necessary" understood as "indispensable"; at the other end, is "necessary" taken to mean as "making a contribution to". A "necessary" measure, in this continuum, is located significantly closer to the pole of "indispensable" than the opposite pole of "making a contribution to" (*Korea – Beef*, Appellate Body Report, para. 161). The Appellate Body further explained that determining whether a measure is "necessary" within the meaning of Article XX(d) "involves in every case a process of weighing and balancing a series of factors" (*Korea – Beef*, Appellate Body Report, para. 164) (see box below).

The "Necessity Test " under paragraphs (a), (b) and (d) of [Article XX](#) of the GATT 1994

The "**necessity test**" involves a process of "weighing and balancing" a series of relevant factors, in particular:

- The contribution made by the measure to the achievement of its objective;
- the importance of the interests or values at stake;
- the trade-restrictiveness of the measure.

([Brazil – Retreaded Tyres](#), Appellate Body Report, para. 178)

In addition, the measure has to be compared with **possible available alternatives**, which may be less trade restrictive while providing an equivalent contribution to the achievement of the objective pursued (*Brazil- Retreaded Tyres*, Appellate Body Report, para. 156).

The weighing and balancing is a holistic operation that involves putting all the variables of the equation together and evaluating them in relation to each other after having examined them individually, in order to reach an overall judgement ([Brazil – Retreaded Tyres](#), Appellate Body Report, para. 182).

The Appellate Body has explained that a contribution exists "when there is a genuine relationship of ends and means between the objective pursued and the measure at issue" (*Brazil – Retreaded Tyres*, Appellate Body Report, para. 210). The contribution must not be "marginal or insignificant"; rather, the measure must be "apt to make a material contribution to the achievement of its objective" (*Brazil – Retreaded Tyres*, Appellate Body Report, para. 150).

The Appellate Body also has observed that the more vital or important the common interests or values pursued, the easier it would be to accept as "necessary" a measure designed to achieve those ends (*Korea - Beef*, Appellate Body Report, para. 162). In this respect, the Appellate noted that the preservation of human life and health is of a value both "vital" and "important in the highest degree" ([EC – Asbestos](#), Appellate Body Report, para. 172).

2. WHAT IMPLIES THE ANALYSIS OF "POSSIBLE AVAILABLE ALTERNATIVES"? – ARTICLE XX(B) AND (D)

In order to qualify as an alternative, **a measure must be not only less trade restrictive than the measure at issue, but should also "preserve for the responding Member its right to achieve its desired level of protection with respect to the objective pursued"** ([US – Gambling](#), Appellate Body Report, para. 308).

The Appellate Body has observed that an important aspect of determining whether a WTO-consistent alternative measure is "reasonably available" is the extent to which such alternative measure contributes to the realization of the end pursued (*Korea – Beef*, Appellate Body Report para. 166). Furthermore, an alternative measure which is impossible to implement is not a "reasonably available" alternative. In *US - Gambling*, the Appellate Body stated that an alternative measure may be found not to be reasonably available "where it is merely theoretical in nature, for instance, where the responding Member is not capable of taking it, or where imposes an undue burden on that Member, such as prohibitive costs or substantial technical difficulties" (*US - Gambling*, Appellate Body Report, para. 308).

3. "RELATING TO..." AND "...MADE EFFECTIVE IN CONJUNCTION WITH RESTRICTIONS ON DOMESTIC PRODUCTION OR CONSUMPTION" UNDER ARTICLE XX(g)

"RELATING TO..."

[Article XX\(g\)](#) requires that the measure sought to be justified be one which "relates to" the conservation of exhaustible natural resources. This term imposes a **lower standard than the term "necessary to"** (i.e. the "necessity test" is more difficult to demonstrate). In making this determination, the Appellate Body essentially looks into the relationship between the measure at stake and the legitimate policy of conserving exhaustible natural resources. Specifically, the Appellate Body stated that a measure would qualify as "relating to the conservation of natural resources" if the measure exhibited a "substantial relationship" with, and was not merely "incidentally or inadvertently aimed at" the conservation of exhaustible natural resources (*US - Gasoline*, Appellate Body Report, page 19). The fact that the design of the measure at issue is not disproportionately wide in its scope and reach in relation to the policy objective of protection and conservation of exhaustible natural resources would support the finding that the means and ends relationship between the measure at issue and the policy objective pursued is a close and real one (*US – Shrimp*, Appellate Body Report, para. 141).

"...MADE EFFECTIVE IN CONJUNCTION WITH RESTRICTIONS ON DOMESTIC PRODUCTION OR CONSUMPTION"

Article XX (g) contains as an additional requirement that the measure at stake be "made effective in conjunction with restrictions on domestic production or consumption". According to the Appellate Body, this is a requirement that the measures concerned impose restrictions, not just in respect of imported products at issue but also with respect to domestic products at issue. This requirement of even-handedness does not necessarily mean identical treatment of domestic and imported products at stake. The clause "if made effective in conjunction with restrictions on domestic production or consumption" is not intended to establish an empirical "effects test" for the availability of the Article XX (g) exception (*US – Gasoline*, Appellate Body Report, pages 20-21).

II.A.3. INTERPRETATION AND APPLICATION OF ARTICLE XX – THE CHAPEAU

Once a measure satisfies the conditions set by one or more of the sub-paragraphs of [Article XX](#), the panel or the Appellate Body will turn to the application of the Chapeau of Article XX. The Chapeau requires that in order to be justified under one of the sub-paragraphs of Article XX, measures must not be "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".

The Chapeau of [Article XX](#) of the GATT 1994

The Chapeau of Article XX requires that measures covered by an exception be not administered in a manner that would constitute:

- 1. Arbitrary discrimination between countries where the same conditions prevail;**
- 2. unjustifiable discrimination between countries where the same conditions prevail; or,**
- 3. a disguised restriction on international trade.**

([US – Shrimp](#), Appellate Body Report, para. 150)

In *US-Gasoline*, the Appellate Body held that "arbitrary discrimination", "unjustifiable discrimination" and "disguised restriction" on international trade may, accordingly, be read side-by-side. They impart meaning to one another (*US-Gasoline*, Appellate Body Report, p. 24).

The purpose and object of the Chapeau is generally the **prevention of abuse of the exceptions of Article XX**. Moreover, the Chapeau by its express terms addresses, not so much the questioned measure or its specific contents as such, but rather the manner in which that measure is applied. The Chapeau serves to ensure that Members' rights to avail themselves of exceptions are exercised in good faith to protect interests considered legitimate under Article XX, not as a means to circumvent one Member's obligations towards other WTO Members ([Brazil – Retreaded Tyres](#), Appellate Body Report, para. 215).

a. "Arbitrary or unjustifiable discrimination between countries where the same conditions prevail"

In order for a measure to be applied in a manner which would constitute "arbitrary or unjustifiable discrimination between countries where the same conditions prevail", **three elements** must exist. First, the application of the measure must result in discrimination. Second, the discrimination must be arbitrary or unjustifiable in character. Third, this discrimination must occur between countries where the same conditions prevail ([US – Shrimp](#), Appellate Body Report, para. 150).

In regard to the requirement of discrimination, the Appellate Body stated that the nature and quality of this discrimination cannot logically refer to the same standard(s) by which a violation of a substantive obligation of the GATT 1994 has been determined to have occurred (e.g. under [Article I](#) – MFN principle - or [Article III](#) - national treatment principle- of the GATT 1994). The question of whether inconsistency with a substantive rule existed is different from the question arising under the Chapeau of [Article XX](#) as to whether that inconsistency was nevertheless justified ([US – Gasoline](#), Appellate Body Report, p. 22-23).

With respect to the phrase "between countries where the same conditions prevail", the Appellate Body observed that the notion of discrimination under the Chapeau of Article XX refers to conditions in importing or exporting countries (i.e. discrimination between foreign countries on the one hand and the home country on the other) or only to conditions in various exporting countries ([US – Shrimp](#), Appellate Body Report, para. 150).

In [Brazil – Retreaded Tyres](#), the Appellate Body stated that the analysis of whether the application of a measure results in arbitrary or unjustifiable discrimination involves an analysis that relates primarily to the cause or the rationale of the discrimination (*Brazil – Retreaded Tyres*, Appellate Body Report, para. 225). In addition, it held that there is arbitrary or unjustifiable discrimination when the reasons given for this discrimination bear no rational connection to the objective falling within the purview of a paragraph of Article XX, or would go against that objective (*Brazil – Retreaded Tyres*, Appellate Body Report, para. 226 - 230). The effects of discrimination might be relevant, but is not the determinant factor.

Example: Finding on "Arbitrary or Unjustifiable Discrimination" – [US – Shrimp](#) Case

In *US – Shrimp*, the US imposed an import ban on shrimps or shrimp products through Section 609 except for those harvested either under conditions that do not adversely affect sea turtles or in waters subject to the jurisdiction of a nation currently certified pursuant to Section 609. The Appellate Body found that the measure was "related to" the conservation of exhaustible natural resources, and therefore was covered by Article XX(g). However, while examining whether the US measure satisfied the requirements of the Article XX Chapeau, **the Appellate Body Report found that the ban constituted "arbitrary" and "unjustifiable" discrimination**. In its finding of "unjustifiable" discrimination (whether the measure at issue discriminated between those countries that had been certified and, consequently, could export shrimp to the US and those non-certified countries that were subject to the import ban) the Appellate Body found the following omissions:

- 1. The failure of the US to engage in serious negotiations across-the-board** - the US failed to engage in serious negotiations with all the Members exporting shrimp to the US with the objective of concluding bilateral or multilateral agreements for the protection and conservation of sea turtles. Before enforcing the import ban- while the US negotiated with some Members, it did not negotiate with other Members (*US – Shrimp*, Appellate Body Report, paras. 166-172). The requirement for serious negotiation does not require the conclusion of an agreement (*US – Shrimp* 21.5, Appellate Body Report, para. 134);
- 2. Lack of flexibility of the measure**– the measure did not take into account the different situations which may exist in different exporting countries. The measure required "*essentially the same*" regulatory program to exporting Members as that adopted by the US, without any inquiry into the appropriateness or effectiveness of such program (*US – Shrimp*, Appellate Body Report, paras. 163-165).

b. "A Disguised restriction on International Trade"

Three criteria have progressively been introduced by GATT/WTO jurisprudence in order to determine whether a measure is a disguised restriction on international trade:

- **Whether the contested measure is published or not** – In *US– Gasoline*, the Appellate Body considered that concealed or unannounced restriction in international trade does not exhaust the meaning of "disguised restriction" (*US-Gasoline*, Appellate Body Report, p. 25);
- **the consideration of whether the application of a measure also amounts to arbitrary or unjustifiable discrimination** - deciding whether the application of a particular measure amounts to "arbitrary or unjustifiable discrimination" may also be taken into account in determining the presence of a "disguised restriction on international trade". Furthermore, disguised restriction embraces restrictions amounting to arbitrary or unjustifiable discrimination in international trade ([US - Gasoline](#), Appellate Body Report, p. 24);

- **the examination of "the design, architecture and revealing structure" of the measure at issue** – in [EC – Asbestos](#) the Panel examined as an additional requirement the "design, architecture and revealing structure" of the measure in order to discern the protective application of the measure ([EC – Asbestos](#), Panel Report, para. 8.236);

II.B. GENERAL EXCEPTIONS IN THE GENERAL AGREEMENT ON TRADE IN SERVICES (GATS)

Under the GATS, general exceptions are set out in [Article XIV](#) which permits Members to maintain inconsistent measures including on services and service suppliers, if the measure meets the conditions related to any of the policy purposes in sub-paragraphs (a) - (e).

Article XIV of the GATS is similar to [Article XX](#) of the GATT 1994, although there are certain differences. Both of these provisions affirm the right of Members to adopt measures which will otherwise be inconsistent with WTO obligations set out in other provisions, provided that certain conditions are satisfied. Similar language is used in both provisions, **notably the term "necessary" (paragraphs (a), (b) and (c)) and the requirements set out in the introductory clause ("the Chapeau")**.

Due to the similarities between Article XX of the GATT 1994 and Article XIV of the GATS, the Appellate Body has found previous decisions under Article XX of the GATT 1994 relevant for the analysis under Article XIV of the GATS (*US – Gambling*, Appellate Body report, para. 291). Therefore, Article XIV of the GATS, like Article XX of the GATT 1994, contemplates a "*two-tier test*":

***Two-Tier Test* under [Article XIV](#) of the GATS**

A GATS inconsistent measure must go through the following *two-tier test*:

- **The challenged measure must fall within the scope of one of the paragraphs of Article XIV**- the measure must address the particular interest specified in that paragraph and there shall be a sufficient nexus —or "degree of connection"—between the measure and the interest protected (the required nexus is specified in the language of the paragraphs themselves, through the use of terms such as "necessary to"); and,
- **the measure must satisfy the requirements of the Chapeau of Article XIV.**

([US – Gambling](#), Appellate Body Report, para. 292)

Sub-paragraphs (a), (b) and (c) of Article XIV of the GATS indicate that the measure must, in similar terms to [Article XX](#) of the GATT 1994, be **"necessary" either to protect public morals, or to maintain public order** (a specific definition of this term is in the accompanying footnote); **to protect human health , animal or plant life or health**; or to **secure compliance with laws or regulations which are not inconsistent with the provisions of the GATS**. Therefore, the "*necessity test*", as explained for Article XX of the GATT 1994 , also applies under sub-paragraphs (a), (b) and (c) of Article XIV of the GATS. Until now, only Article XIV (a) has been interpreted by WTO adjudicating bodies (see box below).

Example: US-Gambling - Measure necessary to protect public morals or to maintain public order (Article XIV(a) of the GATS)

In Module 6, we have seen, through a case study on [US – Gambling](#), that the Appellate Body upheld the Panel's finding that the US measures relating to gambling and betting services were inconsistent with Articles XIV:1 and XIV:2 of the GATS. The US however defended its measures as "necessary to protect public morals or to maintain public order" within the meaning of Article XIV(a). The **Appellate Body** applied the *two-tier tests* explained above and considered relevant decisions under Article XX of the GATT 1994:

- Article XIV(a) – *public morals defence*: upheld the Panel's finding that the US measures were designed "to protect public morals or to maintain public order" within the meaning of Article XIV(a), but reversed the Panel's finding that the US had not shown that its measures were "necessary" (the Panel erred in considering consultations with Antigua to constitute a "reasonably available" alternative measure). Instead, the Appellate Body found that the measure was "necessary" and that the US had made a prima facie case showing "necessity" while Antigua had failed to identify any other alternative measures that might be "reasonably available".

However, not all exceptions included in Article XX of the GATT 1994 are included in Article XIV of the GATS. Conversely, Article XIV of the GATS contains some general exceptions which are not listed in Article XX of the GATT 1994. In this regard, Article XIV of the GATS contains the following **exceptions in paragraphs (d) and (e), which are specific to trade in services**:

Article XIV of the GATS – sub-paragraphs (d) and (e)

- (d) measures inconsistent with Article XVII of the GATS, provided that the difference in treatment is aimed at ensuring the equitable or effective imposition or collection of direct taxes in respect of services or services suppliers of other Members.
- (e) measures inconsistent with [Article II](#) of the GATS, provided that the difference in treatment is the result of an agreement on the avoidance of double taxation or provisions on the avoidance of double taxation in any other international agreement or arrangement by which the Member is bound.

Paragraph (d) provides that Members can still take measures, otherwise inconsistent with the national treatment principle ([Article XVII](#) of the GATS), if the measure facilitates the collection of direct taxes. Such differential treatment, which appears to be less favourable to foreign service providers than for national ones, are authorized only where their purpose is to ensure that the imposition of direct taxes is "equitable and effective".

According to **paragraph (e)**, measures that do not conform with the MFN principle ([Article II](#) of the GATS) can still be taken if their purpose is to put into effect agreements to avoid double-taxation.

II.C. TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS (TRIPS) AGREEMENT

There are no general exceptions as such under the TRIPS Agreement. However, as we have studied in Module 7 (TRIPS Agreement), some provisions may apply to specific situations where protection is not required. See for example Article 13 (copyrights and related rights), Article 17 (trademarks), Article 24 (geographical indications) and Articles 27.2, 27.3, 30 and 31 (patents).

CASE STUDY

CASE STUDY: ARTICLE XX OF THE GATT 1994

[US – GASOLINE](#) (US – Standards for Reformulated and Conventional Gasoline)

(DS2)

PARTIES		AGREEMENTS	TIMELINE OF THE DISPUTE			
Complainants	Brazil and Venezuela	GATT 1994 Art. III & XX	Establishment of Panel	10 April 1995	(Venezuela)	
			Circulation of Panel Report	31 May 1995 (Brazil)		
Respondent	US		Circulation of AB Report	29 January 1996		
			Adoption	29 April 1996		

Table 1: US – Gasoline (US – Standards for reformulated and conventional gasoline)

IN A NUTSHELL

This dispute concerns the Clean Air Act, a law designed to prevent and control air pollution in the US. Following a 1990 amendment to the Clean Air Act, the Environmental Protection Agency (EPA) promulgated the Gasoline Rule on the composition and emissions effects of gasoline to ensure that pollution from the combustion of gasoline did not exceed 1990 levels. From 1 January 1995, the Gasoline Rule permitted only gasoline of a specified cleanliness ("reformulated gasoline") to be sold to consumers in the most polluted areas of the country. In the rest of the country, only gasoline no dirtier than that sold in the base year of 1990 ("conventional gasoline") could be sold. The Gasoline Rule applied to all US refiners, blenders and importers of gasoline. The EPA regulation provided two different sets of baseline emissions standards. First, a **domestic refiner** was required to establish an "**individual baseline**", which represented the quality of gasoline produced by that refiner in 1990. Second, the EPA established a "**statutory baseline**", intended to reflect average US 1990 gasoline quality.

The statutory baseline was assigned to those refiners who had not been in operation for at least six months in 1990, and to importers and blenders of gasoline. Venezuela and Brazil claimed that the Gasoline Rule was prejudicial to their exports to the US and that it favoured domestic producers since it **imposed a stricter burden on foreign gasoline producers**. Accordingly, the Gasoline Rule was inconsistent with Articles III of the GATT 1994 and was not covered by Article XX.

The Panel found that the US measure treated foreign gasoline "less favourably" than "like" domestic gasoline, in violation of Article III:4 of the GATT 1994; and that it was not justified under any of three exceptions in GATT 1994 Article XX (paragraphs (b), (d) and (g)) that were invoked by the US. The US appealed the Panel Report but limited its appeal to the Panel's interpretation of Article XX of the GATT 1994.

On appeal, the Appellate Body modified the Panel's reasoning, finding that the US law **fell within the terms of Article XX(g)**. However, the Appellate Body then found that the law was **not justified by Article XX, because the law did not satisfy the requirements of the Chapeau**.

SUMMARY OF THE KEY FINDINGS OF THE PANEL AND THE APPELLATE BODY

ARTICLE XX OF THE GATT – GENERAL EXCEPTIONIONS	<p>1. The general features of Article XX</p>	<ul style="list-style-type: none"> ▫ <i>Two-tier tests</i> 1. the measure at issue must come under one or another of the particular exceptions - paragraphs (a) to (j) - listed under Article XX; and, 2. it must also satisfy the requirements of the Chapeau of Article XX (Appellate Body Report, page 22); ▫ different terms ("necessary" or "relating to"): used in different sub-paragraphs of Article XX indicate different kinds or degrees of connection or relationship between the measure under appraisal and the state interest or policy sought to be promoted or realized (Appellate Body Report, page 17); ▫ burden of proof: demonstrating that a measure provisionally justified as being within one of the exceptions of Article XX rests on the party invoking the exception (Appellate Body Report, page 22-23).
	<p>2. Provisional Justification under Article XX(g)</p>	<ul style="list-style-type: none"> ▫ A policy to reduce the depletion of clean air was a policy to conserve a natural resource within the meaning of Article XX(g) (Panel Report, para. 6.37); ▫ a measure would qualify as "relating to the conservation of natural resources" if the measure exhibited a "substantial relationship" with, and was not merely "incidentally or inadvertently aimed at" the conservation of exhaustible natural resources (Appellate Body Report, page 18);

		<ul style="list-style-type: none"> ▫ the term "made effective in conjunction with restrictions on domestic production or consumption" implies a requirement that the measures concerned impose restrictions, not just in respect of imported products at issue but also with respect to domestic products at issue. However, it does not necessarily mean identical treatment of domestic and imported products (Appellate Body Report, page 20-21).
	<p>3. The Chapeau of Article XX</p>	<ul style="list-style-type: none"> ▫ Object and purpose of the Chapeau: is generally the prevention of abuse of the exceptions of Article XX. The Chapeau concerns the application of the measure at issue rather than the measure itself (Appellate Body Report, page 22); ▫ three elements: (a) "arbitrary discrimination" (between countries where the same conditions prevail); (b) "unjustifiable discrimination" (between countries where the same conditions prevail); or, (c) "disguised restriction" on international trade (Appellate Body Report, page 23); ▫ unjustifiable discrimination: would be one that could have been "foreseen" and that was not "merely inadvertent or unavoidable" (Appellate Body Report, page 28); ▫ Disguised restriction: whether the application of a particular measure amounts to arbitrary or unjustifiable discrimination may also be taken into account in determining the presence of a disguised restriction on international trade (Appellate Body Report, page 25).

Table 2: Summary of the key findings of the Panel and the Appellate Body

EXERCISES

1. Briefly describe the different exceptions to WTO rules studied in this Module.
2. Explain the structure of Article XX of the GATT 1994 (General Exceptions).
3. Explain the difference between the term "necessary" under Articles XX(b) and XX(d) and "relating to" under Article XX(g) of the GATT 1994.
4. Can Vanin (a WTO Member) apply a measure under Article XX of the GATT 1994, which bans the imports from some, but not all WTO Members?
5. Explain the object and purpose of the Chapeau of Article XX of the GATT 1994.

III. SECURITY EXCEPTIONS

IN BRIEF

A WTO Member is allowed to take any action which it considers **necessary for the protection of its essential security interests** or in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security. Members are not required to furnish information, the disclosure of which would be contrary to their essential security interests.

III.A. SECURITY EXCEPTIONS IN THE GENERAL AGREEMENT ON TARIFFS AND TRADE (GATT) 1994

For trade in goods, [Article XXI](#) of the GATT 1994 ("Security Exceptions") allows Members to take certain measures, otherwise prohibited by the GATT 1994, to protect essential security interests. Article XXI has three paragraphs (a), (b), and (c), which provide the following:

- **Paragraph (a)** refers to the disclosure of information that the WTO Member would consider contrary to its essential security interests.
- **Paragraph (b)** prescribes the condition under which a Member may take any action it considers "necessary for the protection of its essential security interests" including those relating to:
 - fissionable materials or the materials from which they are derived;
 - the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purposes of supplying a military establishment;
 - taken in time of war or other emergency in international relations.
- **Paragraph (c)** allows Members to take actions in pursuance of their obligations under the United Nations (UN) Charter for the maintenance of international peace and security. This is a reference to Chapter VII of the UN Charter.

Article XXI does not contain an obligation for Members to notify measures taken pursuant to the Security Exception. However, a Decision adopted by the GATT CONTRACTING PARTIES in 1982 (1982 Decision) states that "subject to the exception in Article XXI(a), WTO Members should be informed to the fullest extent possible of trade measures taken under Article XXI" ([L/5426](#)).

III.B. SECURITY EXCEPTIONS IN THE GENERAL AGREEMENT ON TRADE IN SERVICES (GATS)

For trade in services, the relevant provision is [Article XIVbis](#) of the GATS. The wording of Article XIVbis of the GATS is almost identical to Article XXI of the GATT 1994 (explained above), which governs the security exceptions for trade in goods, and the concepts do not differ in both instances.

However, unlike Article XXI of the GATT 1994, under the GATS there is an obligation to notify the measures taken under the security exceptions for trade in services. In this regard, the second paragraph of Article XIVbis of the GATS provides that the Council for Trade in Services (CTS) "shall" be informed to the fullest extent possible of measures taken under paragraph 1(b) and (c) and their termination.

III.C. SECURITY EXCEPTIONS IN THE AGREEMENT ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS (TRIPS)

For TRIPS, [Article 73](#) of the TRIPS Agreement governs the use of the "Security Exceptions". As in the case of the GATS, the wording of Article 73 of the TRIPS Agreement is identical to the provision governing trade in goods (Article XXI of the GATT 1994) and the application of the concept is the same as for trade in goods and trade in services. There is no explicit obligation to notify measures taken pursuant to Article 73 of the TRIPS Agreement.

EXERCISES

6. Explain briefly under which circumstances a Member may invoke Article XXI of the GATT 1994.

IV. REGIONAL INTEGRATION

IN BRIEF

WTO Members are allowed, under certain conditions, to **depart from the MFN principle in order to grant preferential treatment** to their trading partners **within a customs union or a free trade area**, without extending such treatment to all WTO Members.

By definition, parties to an RTA offer each other more favourable treatment in trade matters than to the rest of the world (including WTO Members). The coverage and depth of such preferential treatment varies from one RTA to another. Most RTAs go beyond tariff elimination to include regulations on non-tariff barriers and other trade policies areas such as customs matters, standards, trade remedies, and dispute settlement; several agreements also cover services and intellectual property, as well as matters not yet covered by the WTO Agreements, such as competition policy, government procurement, investment and provisions on environment and labour. Depending on the WTO legal provision utilized to notify an RTA, trade barriers may be completely abolished in intra-RTA or merely reduced.

[Article XXIV of the GATT 1994](#) and [Article V of the GATS](#) allow WTO Members to depart from the MFN rule to grant more favourable treatment to their trading partners within a customs union or a free trade area without extending such treatment to all WTO Members, subject to certain requirements.

In addition, **paragraph 2(c) of the 1979 Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries (the "Enabling Clause")** allows developing country Members to conclude among themselves RTAs on trade in goods subject to more flexible requirements than those contained in Article XXIV of the GATT 1994. The Enabling Clause also provides for some preferential schemes, other than RTAs, subject to certain circumstances (we will study the "Enabling Clause" in Module 9).

On 6 February 1996, the General Council established the **Committee on Regional Trade Agreements (CRTA)**.

Regional Trade Agreements: Some Figures...

The number of RTAs involving WTO Members has increased in the recent years. As of November 2008, 418 RTAs have been notified to the GATT or the WTO, 227 of which are currently in force against only 101 in 2005 *. The total number of RTAs currently in force and involving WTO Members is however estimated to be significantly higher, since not all RTAs have been notified. As of November 2008, more than half of all WTO Members were party to three or more RTAs. Free trade areas are more prevalent than customs unions and account for 82 per cent of all RTAs currently in force. Regional Trade Agreements (RTAs) concluded among developing countries account for 36 per cent of the total.

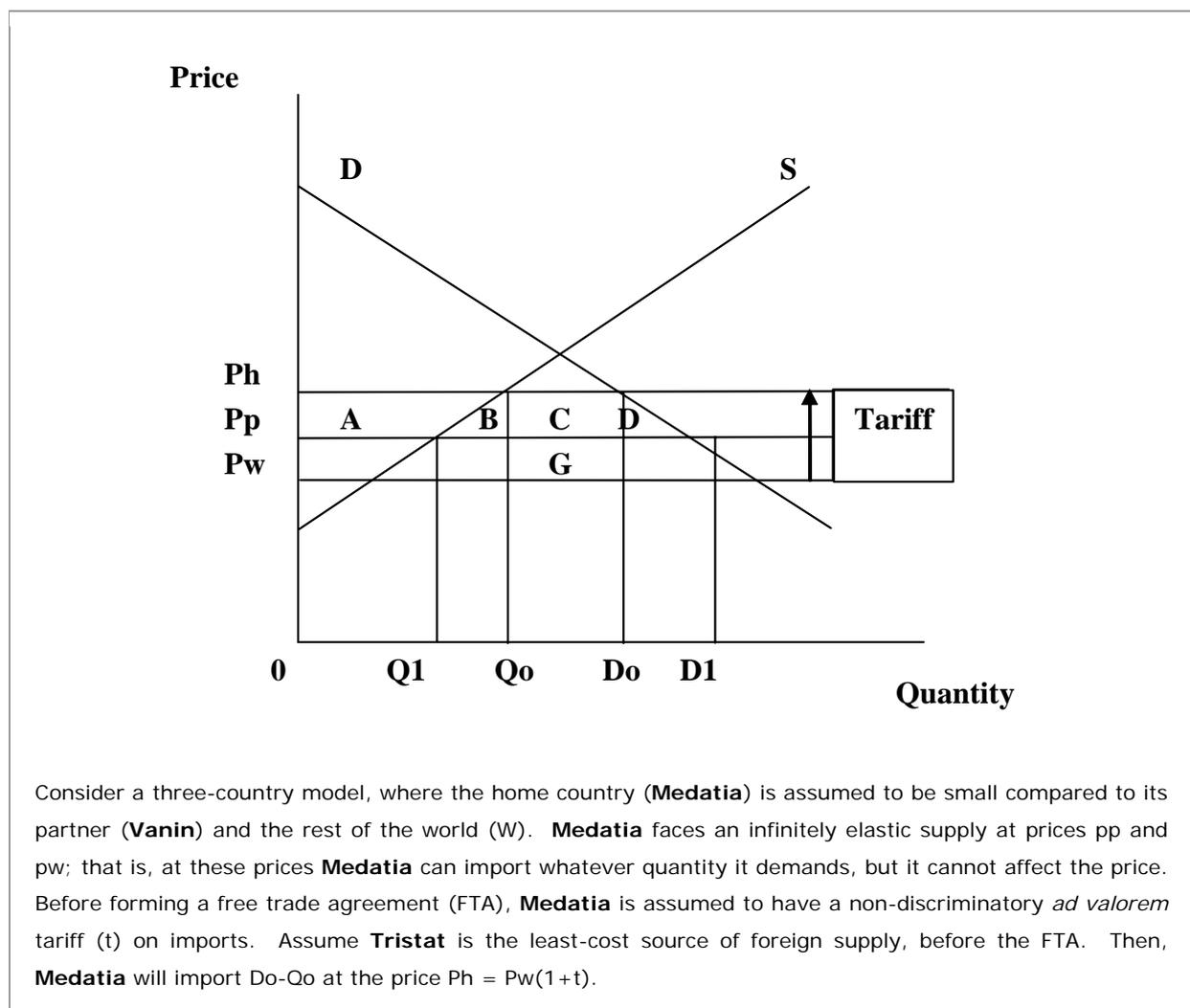
* The number includes notifications made under Article XXIV of the GATT 1994, the Enabling Clause (introduced in Module 9) and Article V of the GATT 1994.

IV.A. THE WELFARE EFFECTS OF REGIONAL TRADE AGREEMENTS (RTAS)

The reduction in intra-regional trade barriers stimulates intra-regional trade. Trade among the parties of a RTA is thus bound to increase (this is known as "**trade creation**"). To the extent that this expanded trade substitutes imports for higher cost domestic products, economic efficiency is increased. But part of the intra-regional trade expansion may be at the expense of trade from cheaper sources outside of the RTA (causing "**trade diversion**").

If the additional trade among the partners is a result of trade diversion, a country can suffer a welfare loss. **Whether a country gains or loses from entering into an RTA will depend on the balance between the trade creating and trade diverting effects of the RTA.** To know more, see the example provided in the box below.

TO KNOW MORE... REGIONAL TRADE AGREEMENTS: TRADE CREATION AND TRADE DIVERSION



Suppose now that **Medatia** and **Vanin** form a FTA. **Medatia** will now import from **Vanin**, since p_p is less than p_h (since as a result of the FTA, Medatia's goods do not pay any tariff when imported to **Vanin**). Consumers will now pay p_p and imports will rise to $D_1 - Q_1$. As a result of the FTA, overall imports increase by $Q_0 - Q_1$ plus $D_1 - D_0$ and domestic prices fall.

- Consumers gain as they can consume a higher quantity for a lower price (the area $A+B+C+D$ represents this gain).
- Producers lose (area A).
- Government loses tariff revenue (area $C+G$).

The area $B + D$ represents the **welfare increase** from the **trade creation** effect of the FTA.

BUT What about the loss represented by area G ?

The area G represents the welfare loss from the trade diverting effect of the FTA.

Area G represents the additional cost of importing $D_0 - Q_0$ from the higher-priced (p_p) partner instead of the cheaper (p_w) world market.

The overall welfare effects of an FTA will depend on the difference between the increased welfare from trade creation (areas $B + D$) and the decrease in welfare from trade diversion (area G). In this example, the FTA increases overall trade, but the welfare effect is ambiguous.

Based on: World Trade Organization (WTO), World Trade Report 2007, Geneva: WTO, pages 138 – 139.

IV.B. REGIONAL INTEGRATION IN THE GENERAL AGREEMENT ON TARIFFS AND TRADE (GATT) 1994

For trade in goods, [Article XXIV](#) of the GATT 1994, complemented by the [Understanding on the Interpretation of Article XXIV of the GATT 1994](#) (the "Understanding"), contains the rules and disciplines applicable to customs unions and free trade areas, as well as to interim agreements that lead to the formation of a customs union or a free trade area.

Article XXIV:4 provides that a customs union, free trade area or an interim agreement should aim to **facilitate trade between the constituent territories and not to raise barriers to the trade of third parties**. The purposive language contained in Article XXIV:4 sets out two main requirements that the parties to an RTA have to meet in order for their agreement to benefit from the MFN derogation; the first one is an internal requirement relating to what is expected from the parties with respect to intra-trade liberalization; the second one is an external requirement relating to the avoidance of negative effects to third parties as a result of the formation of the RTA.

IV.B.1.CONDITIONS FOR THE FORMATION OF CUSTOMS UNIONS AND FREE TRADE AREAS UNDER THE GATT 1994: INTERNAL REQUIREMENTS

Conditions for the Formation of RTAs under [Article XXIV](#) of the GATT 1994: Internal Requirements

Article XXIV allows WTO Members to depart from the MFN principle in order to grant preferential treatment to their trading partners within a customs union or a free trade area subject to the following internal requirements:

- For free trade areas and customs unions: apart from a few exceptions permitted under certain other Articles of the GATT 1994 (XI, XII, XIII, XIV, XV and XX), the duties and other restrictive regulations of commerce are to be eliminated with respect to substantially all the trade between the parties of a customs union or free trade area or at least with respect to substantially all the trade in products originating in such territories (Article XXIV:8); and,
- only for customs unions: in addition, to qualify as a customs union its members should apply substantially the same duties and other regulations of commerce to trade with non-members.

[Article XXIV:8](#) states that apart from a few exceptions permitted under certain other Articles of the GATT 1994 (XI, XII, XIII, XIV, XV and XX), the duties and other restrictive regulations of commerce are to be eliminated with respect to **substantially all the trade** between the parties of a customs union or free trade area or at least with respect to substantially all the trade in products originating in such territories. In addition, to qualify as a customs union its members should apply **substantially the same duties and other regulations of commerce** to trade with non-members. In practice, this condition implies a common external tariff and trade policy.

There is no agreement as to what it is required by the parties to an RTA in order to fulfil the conditions set out in Article XXIV:8. Disagreement persists on the precise meaning of "substantially all the trade" (SAT) and on what constitutes "other restrictive regulations of commerce" since neither Article XXIV nor the Understanding defines these concepts. With respect to the latter it is clear that the RTA must eliminate restrictive trade regulations on intra-party trade, however, disagreement persists among Members on whether this list of bracketed exceptions is exhaustive or merely illustrative. In particular, the fact that Article XIV on the imposition of safeguard measures (studied in Module 5) is not included has been interpreted by some Members to mean that safeguard actions are not allowed in an RTA (and by extension neither are allowed other trade remedies such as anti-dumping). However, this view is not shared by all Members and the practice indicates that most RTA do indeed contain provisions on intra-RTA trade remedies.

With respect to the SAT requirement, there exists neither an agreed definition of the percentage of trade to be covered by a WTO-consistent RTA, nor an agreed methodology for the calculation of the SAT requirement, i.e. whether the assessment should be made on the basis of a percentage of liberalized tariff lines, trade values or both. Another issue of disagreement is whether such term would imply that no particular sector - or major sector - should be excluded; the Uruguay Round added a reference, in the Preamble of the Understanding, to the fact that the contribution of regional trade agreements to the expansion of world trade is "increased if the elimination between the constituent territories of duties and other restrictive regulations of commerce extends to all trade, and diminished if any major sector of trade is excluded". However, the practice of excluding sensitive sectors from RTA liberalization continues and the issue is yet to be resolved.

Likewise the interpretation of SAT remains outstanding in spite of some clarification with respect to the term given by the Appellate Body in *Turkey – Textiles*, where it held that "substantially all trade" is not the same as all the trade but is something considerably more than merely some of the trade (*Turkey – Textiles*, Appellate Body Report, para. 48).

The issue of interpretation and clarification of the WTO legal text on RTAs and in particular of the terms referred to earlier form the subject of discussion among Members in the context of the Doha Round of Negotiations.

IV.B.2.CONDITIONS FOR THE FORMATION OF CUSTOMS UNIONS AND FREE TRADE AREAS UNDER THE GATT 1994: EXTERNAL REQUIREMENTS

Conditions for the Formation of RTAs under Article XXIV of the GATT 1994: External Requirements

Article XXIV allows WTO Members to depart from the MFN principle in order to grant preferential treatment to their trading partners within a customs union or a free trade area subject to the following external requirements:

- For free trade areas: the duties and other regulations of commerce imposed on third – parties at the formation of the free trade area or an interim agreement leading to it should not be higher or more restrictive than those existing prior to its formation (Article XXIV:5(b)); and,
- for customs unions: the duties and other regulations of commerce shall not on the whole be higher or more restrictive than the general incidence of the duties and other regulations of commerce applied prior to its formation (Article XXIV:5(a)).

As mentioned earlier, Article XXIV:4 provides that the purpose of a customs union or of a free trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other Members. In *Turkey – Textiles*, the Appellate Body interpreted that Article XXIV:4 informs the other relevant paragraphs of Article XXIV, including paragraph 5 (*Turkey – Textiles*, Appellate Body Report, para. 57). The Understanding on [Article XXIV](#) explicitly reaffirms this purpose and states that the constituent members should "to the greatest possible extent avoid creating adverse affects on the trade of other Members".

For customs unions, the Understanding provides that the comparison under Article XXIV:5(a) of the level of protection shall be based upon an overall assessment of weighted average of tariff rates and of customs duties collected prior to, and at, the institution of the customs union or the interim agreement leading to the customs union. For this purpose, the duties and charges to be taken into consideration shall be the applied tariffs. For other regulations of commerce, whose quantification and aggregation may be difficult, the examination of individual measures, regulations, products covered and trade flows affected may be required.

IV.B.3.OTHER REQUIREMENTS FOR THE FORMATION OF CUSTOMS UNIONS AND FREE TRADE AREAS UNDER THE GATT 1994

In addition to the conditions set out in Article XXIV:8 and XXIV:5, **other requirements include provisions on interim agreements and transition periods, tariff renegotiations in the context of the formation of a customs unions, and transparency provisions** (see below).

With respect to the former, Article XXIV:5(c) states that an interim agreement must include a plan and schedule for the formation of a customs union or a free trade area within "a reasonable length of time," defined by paragraph 3 of the Understanding as not exceeding 10 years except in exceptional circumstances.

As for tariff renegotiations in the context of the formation of a customs unions, Article XXIV:6 provides that in cases where, in the context of the formation of a customs union, a Member proposes to increase any bound rate, the procedures for modification of schedules set forth in [Article XXVIII](#) shall apply. As clarified by the Understanding, the following requirements apply:

- The process of negotiation must be commenced before tariff concessions are modified or withdrawn upon the formation of a customs union or an interim agreement leading to a customs union (paragraph 4);
- the negotiations will be entered into in good faith with a view to achieving mutually satisfactory compensatory adjustment (paragraph 5);
- affected Members shall take due account of reductions of duties on the same tariff line made by other parties of the customs union. Only if such reductions do not provide the necessary compensatory adjustment, the customs union would provide compensation, which may take the form of reductions of other tariff lines (paragraph 5); and,
- where an agreement cannot be reached within a reasonable period, the customs union shall be free to modify or withdraw the concession and affected Members shall then be free to withdraw substantially equivalent concessions (paragraph 5).

Paragraph 12 of the Understanding states that the provisions regarding **dispute settlement** may be invoked with respect to any matters arising from the application of those provisions of [Article XXIV](#) relating to customs unions, free trade areas or interim agreements.

TO KNOW MORE...INTERPRETATION OF THE SCOPE OF THE EXCEPTION TO MFN PROVIDED BY ARTICLE XXIV OF THE GATT 1994 REGARDING CUSTOMS UNIONS: TURKEY-TEXTILES

In *Turkey - Textiles*, the Appellate Body reviewed the Panel's finding that Article XXIV did not justify the imposition by Turkey of quantitative restrictions on imports of certain textile and clothing products from India upon the formation of a customs union with the European Union.

According to the Chapeau of Article XXIV:5, the provisions of the GATT 1994 shall not prevent, as between the territories of contracting parties, the formation of RTAs that comply with the requirements provided therein.

In this regard, the Appellate Body held in this case that Article XXIV can justify the adoption of a measure which is inconsistent with certain other GATT 1994 provisions only if (paras. 58-59):

- (i) The measure is introduced upon the formation of a customs union that fully meets the requirements of sub-paragraphs 5(a) and 8(a) of Article XXIV; and,
- (ii) only to the extent that the formation of the customs union would be prevented if the introduction of the measure were not allowed.

IV.C. REGIONAL INTEGRATION IN THE GENERAL AGREEMENT ON TRADE IN SERVICES (GATS)

[Article V](#) of the GATS provided for the formation of "Economic Integration Agreements" and it is modelled to a large extent on [Article XXIV](#) of the GATT 1994. Article V:4 of the GATS states that any agreement liberalizing trade in services must be designed to "**facilitate trade between parties**".

CONDITIONS FOR THE FORMATION OF ECONOMIC INTEGRATION AGREEMENTS UNDER ARTICLE V OF THE GATS

Conditions for the Formation of Economic Integration Agreements under [Article V](#) of the GATS

Article V allows WTO Members to enter into an agreement to further liberalize trade in services, provided that such an agreement meets the following conditions:

- Substantial sectoral coverage- in terms of number of sectors, volume of trade affected and modes of supply. In particular, there should be no a priori exclusion of any mode of supply (Article V:1(a) and footnote 1);
- absence or elimination of substantially all discrimination among the parties - in the sectors it covers, by eliminating existing discriminatory measures and/or preventing the introduction of new or more discriminatory measures (Article V:1(b)); and,
- the agreement should not result in new trade barriers to other WTO Members - it shall facilitate trade between the parties and shall not raise the overall level of barriers to trade in services in respect of any WTO Member outside the agreement within the respective sectors or sub-sectors compared to the level applicable prior to such an agreement (Article V:4).

Article V:3 provides some flexibility in favour of developing countries parties to an economic integration agreement (EIA) in evaluating whether all conditions by a given agreement are met. In particular Article V:3(a) provides flexibility with respect to the requirements contained in paragraph 1, and in particular with respect to the absence or elimination of all discrimination between the parties. Article V:3(b) grants flexibility in the case of RTA involving only developing countries with respect to the requirements of Article V:6 on "substantive business operations".

Articles V:5 and V:8 state that if the establishment of the RTA, or its subsequent enlargement, leads to a party in the agreement to withdraw its specific commitments set out in the Schedule, this party shall enter into negotiations to provide compensation to other Members (non-parties in the agreement). However, no compensation is due from non-parties for trade benefits they gain from the agreement.

In addition, [Article Vbis](#) relates to, and provides similar legal cover for, agreements on labour markets integration. Its main condition is that citizens of parties to the arrangement should be exempt from residency and work permit requirements.

IV.D. REGIONAL TRADE AGREEMENTS (RTAS) AND THE MULTILATERAL TRADING SYSTEM

RTAs and the Multilateral Trading System

The issue relating to whether RTAs are "**stumbling blocs**" or "**building blocks**" to the MTS is still subject to hot debate.

On one hand, by their very nature, RTAs are discriminatory: they are a departure from the MFN principle, a cornerstone of the MTS. There is the risk that RTAs may promote trade diversion rather than trade creation (see box on RTAs: trade creation and trade diversion). In addition, they may reinforce vested interests to maintain preferences margins.

Furthermore, the increase in RTAs has produced the phenomenon of overlapping membership - the coexistence in a single country of differing trade rules applying to different RTA partners. This can hamper trade flows merely by the costs involved for traders in meeting multiple sets of trade rules. Moreover, the proliferation of RTAs, especially as their scope broadens to include policy areas not regulated multilaterally, increases the risks of inconsistencies in the rules and procedures among RTAs themselves, and between RTAs and the multilateral framework. Finally, the proliferation of RTAs may crowd out negotiating resources necessary to achieve further multilateral liberalization.

On the other hand, RTAs can complement the MTS and serve as a catalyst for further liberalization. They may act as laboratories of international cooperation, reducing political opposition to multilateral liberalization at the domestic level. RTAs have allowed groups of countries to negotiate rules and commitments that go beyond what was possible at the time multilaterally. Some of these rules have paved the way for agreement in the WTO. Services, intellectual property, environmental standards, investment and competition policies are all issues that were raised in regional negotiations and later developed into agreements or topics of discussion in the WTO. However, it must be noticed that there are certain important areas in international trade that cannot be addressed through RTAs (e.g. the elimination of export subsidies).

An RTA's effects on global trade liberalization and economic growth are not clear given that the regional economic impact of RTAs is *ex ante* inherently ambiguous. Their net economic impact will certainly depend on its own architecture and the choice of its major internal parameters (in particular, the depth of trade liberalization and sectoral coverage).

To ensure that RTAs be building blocks rather than obstacles to the MTS, they should help trade flow more freely among the countries in the group without barriers being raised on trade with the outside world.

Based on: World Trade Organization (WTO), World Trade Report 2007, Geneva: WTO, p. 312 – 320.

IV.E. REGIONAL TRADE AGREEMENT (RTAS) AND TRANSPARENCY

As part of the negotiations in the Doha Round of Negotiations, the General Council adopted the Decision on a "**Transparency Mechanism for Regional Trade Agreements**" ([WT/L/671](#)) on 14 December 2006.

The adoption by the General Council of a new Transparency Mechanism for Regional Trade Agreements (TM) has resulted in a number of important procedural changes in the treatment of RTAs within the WTO framework. The TM, which applies to all RTAs whether notified under [Article XXIV](#) of the GATT 1994, [Article V](#) of the GATS or the Enabling Clause, is being implemented on a provisional basis in accordance with paragraph 47 of the Doha Ministerial Declaration, and will be replaced by a permanent mechanism to be adopted as part of the Doha Round of Negotiations. An explanation of the key elements of the TM, together with an assessment of its first year of operation, is outlined below.

The TM clarifies existing transparency requirements as contained in the WTO provisions on RTAs such as notification of RTAs, consideration of the RTA by the WTO, and subsequent notification and reporting. It also adds new elements such as the early announcement requirement for RTAs either under negotiation or signed, but not yet in force. With respect to notification, the TM strengthens existing provisions on notification by stipulating that notification is to take place "as early as possible ... and ... before the application of preferential treatment between the parties" (emphasis added).

The most notable development, however, is the responsibility given to the WTO Secretariat to prepare factual presentations of all notified RTAs covering trade in goods or services. The factual presentation, which replaces the standard format furnished by the parties to an RTA, is a detailed summary of an RTA and contains data on the trade environment of the RTA parties, a description of the RTA's regulatory features, and details of the tariff, trade and regulatory liberalization envisaged over the transition period of the RTA. It is prepared on the Secretariat's own responsibility, in full consultation with the parties, and cannot be used as a basis for dispute settlement procedures or to create new rights and obligations for Members. The purpose of the factual presentation is to produce objective, homogenous reports containing no value judgement which are used by Members in their "consideration" of an RTA under review. With respect to "subsequent notification and reporting", the TM supplants the largely dysfunctional RTA biennial reporting schedule by providing that the required notification of changes affecting the implementation or operation of an RTA should take place as soon as possible after changes occur. At the end of the RTA's implementation period, the parties should submit a short written report on the realization of liberalization commitments in the RTA.

Under the new Mechanism, the CRTA is the responsible body for RTAs notified under [Article XXIV](#) of the GATT 1994 or [Article V](#) of the GATS. RTAs in trade in goods concluded among developing countries only may be notified under either Article XXIV of the GATT 1994 or the Enabling Clause. Regional Trade Agreements (RTAs) notified under the Enabling Clause are the responsibility of the Committee on Trade and Development (CTD), convening in dedicated session (which will be explained in Module 9).

NOTE

To know more about the **TM and the factual presentations prepared** by the WTO Secretariat, please refer to: http://www.wto.org/english/tratop_e/region_e/trans_mecha_e.htm

EXERCISES

7. What is the purpose of RTAs according to Article XXIV:4 of the GATT 1994?
8. Explain briefly the conditions applicable to the formation of FTAs under Article XXIV of the GATT 1994.
9. What is the difference between "trade creation" and "trade diversion"? Why are these terms related to RTAs?
10. Explain the main objectives of the TMs for RTAs.

V. BALANCE-OF-PAYMENTS (BOPS) EXCEPTIONS

IN BRIEF

Under WTO rules, Members are allowed under certain circumstances and subject to specific conditions, to adopt import restrictions otherwise inconsistent with the WTO rules in order to **safeguard their external financial position and their balance-of-payments (BOPs)**.

V.A. BALANCE-OF-PAYMENTS (BOPS) IN THE GATT 1994

[Article XII](#) and [Article XVIII:B](#) of the GATT 1994, together with the [Understanding on Balance-of-Payments Provisions of the GATT 1994](#) allow WTO Members to take measures in order to safeguard their external financial position and their balance-of-payments. While the basic condition for invoking Article XII is to safeguard the Member's external financial position and its BOPs, Article XVIII:B refers to Members (within the scope of paragraph 4) experiencing BOPs difficulties arising mainly from efforts to expand their internal markets as well as from the instability in their terms of trade. In this regard, paragraph 2 of Article XVIII:B refers to the need of these Members to safeguard their external financial position and to ensure a level of reserves adequate for the implementation of their programmes of economic development. **Article XII can be invoked by all Members and Article XVIII:B only by developing country Members.** Article XVIII:B contains less stringent criteria than Article XII.

Article XII:2 – which can be invoked by all Members- states that import restrictions "shall not exceed those necessary: (i) to forestall the imminent threat of, or to stop, a serious decline in its monetary reserves"; or, (ii) "...in the case of a Contracting Party with very low monetary reserves, to achieve a reasonable rate of increase in its reserves". Instead, Article XVIII:B:9 – which can be invoked by developing country Members only - omits the word "imminent" from the first condition and refers to an "inadequate" level rather than a "very low" level of reserves ("adequate" is defined as "adequate for the implementation of its programme of economic development"). Both Articles require Members to progressively relax the restrictions as conditions improve, and eliminate them, when conditions no longer justify their maintenance.

In general, measures taken for BOPs purposes have to be temporary, preferably price-based, administered in a transparent manner and apply to the general level of imports (i.e. avoid sectoral specificity).

Who determines when there is a serious decline in a Member's monetary reserves?

The CONTRACTING PARTIES in reaching their final decision in cases involving the criteria set forth in paragraph 2 (a) of Article XII or in paragraph 9 of Article XVIII, shall accept the determination of the International Monetary Fund (IMF) as to what constitutes a serious decline in the contracting party's monetary reserves, a very low level of its monetary reserves or a reasonable rate of increase in its monetary reserves, and as to the financial aspects of other matters covered in consultation in such cases.

TO KNOW MORE... UNDERSTANDING ON THE BOPS PROVISIONS OF THE GATT 1994

In the Understanding on BOPs, the Members have confirmed the following main commitments:

- **Announce publicly**, as soon as possible, time schedules for the removal of restrictive import measures taken for BOPs purposes and to explain why, if they do not do so (paragraph 1);
- give preference to those measures which have the **least disruptive effect on trade** - such measures are referred to as **price-based measures** and can be applied for BOPs purposes notwithstanding the provisions of Article II of the GATT 1994 – Schedule of Concessions- (paragraph 2);
- **justify why price-based measures are not adequate** if they have chosen to impose QRs, as well as not apply more than one type of restrictive trade measure to the same product (paragraph 3); and,
- **not to apply restrictive import measures in excess of what is necessary** to address the BOPs situation, as well as administer restrictions in a transparent manner (paragraph 4).

Members are required to **notify** to the General Council the introduction of, or any changes to, restrictive import measures introduced for BOPs purposes, as well as any modifications in time schedules for the removal of such measures, no later than 30 days after their announcement. **Consultations** with the Committee on BOPs Restrictions are expected immediately after taking action or, in circumstances in which prior consultation is practicable, before doing so ([Articles XII:4](#) and [XVIII:12](#)). A Member maintaining such restrictions is required to consult annually or biennially. A Member adversely affected by these restrictions may initiate consultations if they are inconsistent with the WTO relevant provisions on BOPs.

V.B. BALANCE-OF-PAYMENTS (BOPS) IN THE GENERAL AGREEMENT ON TRADE IN SERVICES (GATS)

[Article XII](#) of the GATS allows Members to introduce restrictions on trade in services, as an exceptional measure and notwithstanding any specific commitments they have assumed, in order to safeguard their BOPs position. This provision can be invoked in the event of serious BOPs and external financial difficulties, or if there is a threat of such difficulties. Such restrictions may include restrictions on payments or transfers which would otherwise be prohibited by [Article XI](#) of the GATS (payments and transfers).

It is recognized that particular pressures on the BOPs of a Member in the process of economic development or economic transition may require the use of restrictions to ensure, *inter alia*, the maintenance of a level of financial reserves adequate for the implementation of its programme of economic development or economic transition.

Any Member invoking Article XII and introduces restrictions to safeguard its BOPs, must meet the following conditions (Article XII:2): (i) not discriminate among services and service suppliers of different Members; (ii) be consistent with the Articles of the Agreement of the International Monetary Fund (IMF); (iii) avoid unnecessary damage to the commercial, economic and financial interests of other Members and not exceed the

level necessary to address the BOPs situation; and, (iv) be temporary, and be phased out progressively as the BOPs improves.

Finally, as with the GATT 1994, Members are required to **promptly notify** the restrictions to the General Council of the WTO, if they adopt restrictions to safeguard its BOPs under the GATS. They shall also **consult** promptly with the Committee on BOPs on restrictions adopted (Article XII:5).

VI. WAIVERS

As we have presented in Module 1, in "exceptional circumstances", a WTO Member may be authorized by the other Members to derogate, for a specific time and under certain conditions, from a provision contained in the Agreement Establishing the WTO or any of the Multilateral Trade Agreements. These derogations, called "waivers", are applicable to trade in goods, trade in services and TRIPS. Waivers are governed by [Article IX:3](#) of the Agreement Establishing the WTO. A waiver is normally used when there are no other provisions which would allow a Member to derogate from a WTO principle or a specific provision.

While there is no need to negotiate before adopting a general exception under [Article XX](#) of the GATT 1994 or [Article XIV](#) of the GATS, waivers shall be granted by three fourths of the Members, through a decision of the Ministerial Conference (see Module 1). Consequently, in contrast to such exceptions, a waiver may be viewed as a "negotiated right".

Waivers are temporary so, when they are granted, a definite time-period is set for termination. Moreover, if granted for more than a one-year period, a waiver must be reviewed annually to establish if the exceptional circumstances warranting its grant still exist.

EXERCISES

11. What is the difference between a "waiver" and the other exceptions studied in this Module?

ILLUSTRATION

SCENARIO

Suppose that Vanin and Tristat are WTO Members. Recently, Vanin promulgated a regulation which imposes a ban on cars with fuel efficiency below 12.5 miles per gallon (mpg).

Tristat exports cars to Vanin, its major importer. Most of the cars Tristat produces are with fuel efficiency below 12.5 mpg. Vanin does not produce cars with fuel efficiency below 12 mpg.

Tristat considers that Vanin's regulation is inconsistent with Article XI of the GATT 1994 (General Elimination of Quantitative Restrictions).

Vanin argues that its measure is aimed at protecting human, life and health as well as reducing air pollution.

QUESTION

Assume you are a legal expert on WTO Law, what defences or WTO exception(s) may Vanin invoke and what arguments could this country make under such exception(s)?

PROPOSED ADVICE

Vanin can invoke [Article XX](#) of the GATT 1994 (General Exceptions) to justify its measure in case it is found inconsistent with Article XI of the GATT 1994 (General Elimination of Quantitative Restrictions) – studied in Module 3.

Under Article XX, Vanin must establish first, that its regulation is provisionally justified under Article XX(b) and/or Article XX(g); and second, that the application of the regulation complies with the Chapeau of Article XX.

[ARTICLE XX](#) OF THE GATT 1994 – GENERAL EXCEPTIONS

ARTICLE XX (B) - "NECESSARY TO PROTECT HUMAN, ANIMAL OR PLANT LIFE OR HEALTH"

Vanin needs to establish that: 1. the policy in respect of the measures for which the provision was invoked falls within the range of policies designed to protect human, animal or plant life or health, and, 2. the inconsistent measures for which the exception is being invoked is "necessary" to fulfil such policy objective - "necessity test" - ([US – Gasoline](#), Panel Report, para. 6.20).

Accordingly, Vanin may claim that its regulation is *pursuing the objective of protection of human health by reducing vehicle emissions*. As you studied in this Module, the "necessity test" involves a process of weighing and balancing a series of factors, in particular: i. the contribution made by the measure to the achievement of its objectives, that is, the protection of human, animal or plant life or health; ii. the importance of the interests or values at stake; and, iii. the trade-restrictiveness of the measure (*Brazil - Retreaded Tyres*, Appellate Body Report, para. 178).

In this regard, Vanin may argue that the measure makes a contribution to the objective since its application is reducing pollution in forms of emissions posing risk to human life or health. In addition, Vanin may argue that the ban is applied to preserve human life and health, considered of a value both "vital" and "important in the highest degree" (*EC- Asbestos*, Appellate Body Report, para. 172).

With respect to possible alternative measures (less trade restrictive) that Tristat might propose, Vanin would have to show that these alternatives do not contribute equivalently to the achievement of the objective pursued (protection of human health by reducing vehicle emissions). In order to qualify as an alternative, a measure must be not only be less trade restrictive than the measure at issue, but should also "preserve for the responding Member its right to achieve its desired level of protection with respect to the objective pursued" (*US – Gambling*, Appellate Body Report, para. 308). In addition, depending on the alternative measures proposed by Tristat, Vanin may argue that such measures impose an undue burden on it, e.g. prohibitive costs (*US – Gambling*, Appellate Body Report, para. 308).

ARTICLE XX (G) "RELATING TO THE CONSERVATION OF EXHAUSTIBLE NATURAL RESOURCES"

Under XX(g), Vanin has to demonstrate that the measure at issue: 1. is concerned with the conservation of exhaustible natural resources, 2. "relates to" the conservations of exhaustible natural resources, and, 3. the measure is made effective in conjunction with restrictions on domestic production or consumption.

Vanin can claim that its regulation is *concerned with the conservation of exhaustible natural resources since it is aimed at the conservation of clean air*, a policy that falls within Article XX(g) (see *US – Gasoline*, Panel Report, para. 6.37). Vanin also needs to demonstrate that the measure at issue exhibits a "substantial relationship" with, and is not merely "incidentally or inadvertently aimed at", the conservation of clean air (*US – Gasoline*, Appellate Body Report, page 19). Furthermore, to comply with the third requirement, Vanin will have to show that a similar restriction applies to cars produced in Vanin.

CHAPEAU OF ARTICLE XX OF THE GATT 1994

Vanin also has to demonstrate that its regulation satisfies the requirement of the Chapeau. In this respect, Vanin shall demonstrate that its regulation is not applied in a manner that constitutes: 1. arbitrary or discrimination between countries where the same conditions prevail; 2. unjustifiable discrimination between countries where the same conditions prevail; or, 3. a disguised restriction on international trade.

A measure would be considered to be applied in a manner that constitutes "arbitrary or unjustifiable discrimination between countries where the same conditions prevail" if: 1. the application of the measure results in discrimination; 2. the discrimination is arbitrary or unjustifiable in character; 3. this discrimination occurs between countries where the same conditions prevail (*US – Shrimp*, Appellate Body Report, para. 150).

VII. SUMMARY

In certain circumstances, WTO Members are allowed to adopt measures that will otherwise be inconsistent with their WTO obligations, subject to certain conditions.

The **general exceptions** as set out in [Article XX](#) of the GATT 1994 and [Article XIV](#) of the GATS allow Members to take measures necessary to protect legitimate policy objectives such as the protection of public morals, the protection of human, animal or plant life or health or the conservation of exhaustible natural resources. In this regard, it has been recognized that the WTO rules are not intended to impede Members from pursuing such legitimate objectives or to choose the appropriate level of protection. However, the measures adopted for the protection of such objectives have to comply with the requirements provided in Article XX of the GATT 1994 and Article XIV of the GATS, respectively. In general, such measures must have a nexus with the objectives pursued (the degree of connection and conditions differ according to each provision in Article XX and XIV), as well as not lead to arbitrary or unjustifiable discrimination between countries where the same conditions prevail or constitute a disguised restriction to international trade (conditions set by the Chapeau of both Articles).

In contrast to the general exceptions, the **security exceptions** apply not only to goods and services, but also to trade-related aspects of intellectual property (TRIPS). According to the security exceptions, a WTO Member can take any action necessary for the protection of its essential security interests despite the inconsistency of such action with its obligations under the GATT 1994, the GATS or the TRIPS.

In addition, under Article XXIV of the GATT 1994 and Article V of the GATS, WTO Members are allowed to depart from the MFN principle in order to provide preferential access to their trading partners under RTAs – "customs unions" or "free trade areas" (for trade in goods) or economic integration arrangements (for trade in services). The formation of such RTAs is subject to some internal and external requirements, including to facilitate trade between the constituent territories and not to create trade barriers toward other Members (third-parties) higher or more restrictive than those existing before the formation of the RTA. Other requirements comprise provisions on interim agreements and transition periods, tariff renegotiations in the context of the formation of a customs unions, and transparency provisions (including the Transparency Mechanism for RTAs).

In addition, Members are allowed to apply import restrictions in order to safeguard their external financial position and for BOPs reasons. Finally, in exceptional circumstances, a WTO Member may be authorized by the other Members to derogate for a specific time and under certain conditions, from a provision contained in the Agreement Establishing the WTO or any Multilateral Trade Agreement. These derogations called "waivers" are applicable to trade in goods, trade in services and TRIPS.

PROPOSED ANSWERS

1. In this Module, we studied the main horizontal exceptions applicable to the GATT 1994, the GATS and the TRIPS Agreement. These are:
 - General Exceptions ([Article XX](#) of the GATT 1994 and [Article XIV](#) of the GATS) - Right to take measures, for example, necessary to protect human, animal or plant life or health. Such measures cannot constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on international trade. There are no general exceptions as such under the TRIPS Agreement;
 - Security Exceptions ([Article XXI](#) of the GATT 1994, [Article XIVbis](#) of the GATS and [Article 73](#) of the TRIPS) - Right to take measures to protect essential national security interests;
 - Regional Trade Agreements (RTAs) ([Article XXIV](#) of the GATT 1994 and [Article V](#) of the GATS) - Right to depart from the MFN principle in order to grant preferential treatment to goods (GATT 1994) or service suppliers (GATS) to trading partners within a customs union or a free trade area (for goods) or an economic integration agreement (for trade in services) without extending such treatment to all WTO Members. This right is subject to certain conditions;
 - Balance-of-Payment (BOP) (Articles XII & XVIII of the GATT 1994 and Article XII of the GATS)– Right to take measures to safeguard a Member's external financial position and its BOPs; and,
 - Waivers ([Article IX](#) of the Agreement Establishing the WTO) - Temporary waiver granted with the authorization of the other Members, in exceptional circumstances;
2. Article XX comprises ten sub-paragraphs and an introductory clause (the Chapeau). Accordingly, Article XX provides a *two-tier test*: A. The measure at issue must fall under one or another of the particular exceptions – sub-paragraphs (a) to (j) - listed under Article XX - each sub-paragraph concerns different objectives and contains different requirements; and, B. the measure must also satisfy the requirements imposed by the Chapeau of Article XX. The order of the two tests cannot be reversed.
3. According to the Appellate Body, the "necessity test" under [Article XX \(b\)](#) & (d) involves in every case a process of weighing and balancing a series of factors which prominently include: A. the contribution made by the measure to the achievement of its objective; B. the importance of the interests or values at stake; and C. the trade-restrictiveness of the measure at issue. In addition, the measure has to be compared with possible available alternative, which may be less trade restrictive while providing an equivalent contribution to the achievement of the objective pursued.

As the "necessity test", the "relating to" test under Article XX(g) also requires the assessment of the relationship between the measure at issue and the objective pursued. The "relating to" test is less stringent than the "necessity test". A measure will qualify as relating to the conservation of natural resources if the measure exhibited a substantial relationship with, and is not merely incidentally or inadvertently aimed at the conservation of exhaustible natural resources.
4. In principle, the answer is NO (unless there is an objective justification for making such distinction- see also *Brazil-Retreaded Tyres*, Appellate Body Report, para. 225-230). According to the Chapeau, measure under Article XX must not be "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 to international trade.

5. The object and purpose of the Chapeau is generally the prevention of abuse of the exceptions of [Article XX](#). It serves to ensure that Members' rights to avail themselves of exceptions are exercised in good faith to protect interests considered legitimate under Article XX, not as a means to circumvent one Member's obligations towards other WTO Members. It does not concern the questioned measure or its specific content as such, but rather the manner in which that measure is applied.
6. A WTO Member is allowed to take any action which it considers necessary for the protection of its essential security interests (such as those relating to fissionable materials; or traffic in arms, ammunition and implements of war; or those taken in time of war or other emergency in international relations); or in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security. Furthermore, Members are not required to furnish information, the disclosure of which would be contrary to their essential security interests.
7. Article XXIV:4 of the GATT 1994 provides that the purpose of a customs union or of a free trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other Members. The Understanding on Article XXIV explicitly reaffirms this purpose and states that the constituent members should "to the greatest possible extent avoid creating adverse affects on the trade of other Members".
8. [Article XXIV](#) of the GATT 1994 allows the formation of free trade agreements under certain internal and external requirements: 1. With regard to the internal requirements, Article XXIV:8 states that apart from a few exceptions, the duties and other restrictive regulations of commerce are to be eliminated with respect to "substantially all trade" between the parties or at least with respect to substantially all the trade in products originating in such territories; and 2. with regard to the external requirements, the duties and other regulations of commerce imposed on third-parties at the formation of the free trade area or an interim agreement leading to it should not be higher or more restrictive than those existing prior to its formation (Article XXIV:5(b)).

In addition to the conditions set out in Article XXIV:8 and XXIV:5, other requirements include provisions on interim agreements and transition periods , as well as transparency provisions.

9. Trade creation refers to the increase in trade within RTAs due to the reduction in intra-regional trade barriers. To the extent that this expanded trade substitutes imports for higher cost domestic products, economic efficiency is increased. However, the formation of RTAs may also cause trade diversion, which takes place when the most efficient suppliers of goods or services from outside the RTA are replaced by less efficient sources coming from parties to the RTA. Thus, if the additional trade among the partners is a result of trade diversion, a country can suffer a welfare loss. Whether a country gains or loses from entering into an RTA will depend on the balance between the trade creating and trade diverting effects of the RTA.
10. The transparency mechanism, adopted by the General Council on 14 December 2006, provides for early announcement of any RTA and type of information to be submitted by the parties to the WTO. The mechanism, which applies to all RTAs, is being implemented on a provisional basis in accordance with paragraph 47 of the Doha Ministerial Declaration. Members will consider the notified RTAs on the basis of a factual presentation prepared by the WTO Secretariat on its own responsibility and in full consultation with the parties. The purpose of the factual presentation is to produce objective, homogeneous reports containing no value judgement which are used by Members in their consideration of an RTA under review.

11. There are four main differences between a waiver and other horizontal exceptions:

- Negotiated exception - Waivers are granted by the WTO Membership, through a decision of the Ministerial Conference. Consequently, a waiver may be viewed as a "negotiated right", whereas there is no need to negotiate to take a general exception under Article XX of the GATT 1994 or Article XIV of the GATS (the latter are however subject to the conditions set forth in each provision);
- not disputable - While a provision of the general exceptions may be invoked to justify a measure otherwise inconsistent with the GATT 1994 or the GATS, a waiver should generally not be disputed unless the Member fails to comply with the conditions of the waiver;
- subject to a limited time - Waivers are usually temporary so, when they are granted, a definite time-period is set for termination; and,
- subject to annual review - If granted for more than a one-year period, a waiver must be reviewed annually to establish if the exceptional circumstances warranting its grant still exist.