

Gurwinder Singh

Subsidies in the Context of the WTO's Free Trade System

A Legal and Economic Analysis

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What remains unforgettable. . . .

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My personal opinion on the WTO and a few words on research: Freedom to trade and free entrepreneurship are age-old market claims, but what becomes interesting and adventurous is that every nation, big or small, developed, developing or less developed, is provided equal opportunity to trade through a free trade system, and the market system is regulated by one institution, that is, the WTO. By no stretch of imagination can I say how the great communist leaders would have reacted on the issue of farm subsidies during the Doha deadlock, but one thing is certain, that is, the leaders of the world despite so much economic disparity and social, cultural and political difference have repeatedly put their faith in this trade regulating institution, the WTO.

The book on *Subsidies in the Context of the WTO's Free Trade System, A Legal and Economic Analysis* has seen its own courses of ups and down before reaching conclusion. However, the constant motivation from supervisors and many of the administrative staff, several of them having retired, acted as a strong pillar of support.

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Before embarking upon the theme of this work, I would like to express these lines that came into my mind as I was abstractly thinking while travelling from Turku to Helsinki by train.

The values of fair trade are concepts based on morality. Fair trade is also a question of far-reaching milestones for assumptions based on economics. As a safeguard for fairness and equity, which are the universally-accepted legal values among the nations, it is natural that legal rationality will give an interpretation whenever an occasion arises to meet these objectives.¹

Gurwinder Singh

¹Quotations in this work are based on the author's own thoughts.

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List of Abbreviations

AB	Appellate Body of the WTO
ACP	African, Caribbean and Pacific Group of States
ACT	Advanced Composite Technology
AD Agreement	Anti-Dumping Agreement
AD Duties	Anti-Dumping Duties
AMS	Aggregate Measure of Support
AoA	Agreement on Agriculture
APEC	Asia Pacific Economic Cooperation
ASCM	Agreement on Subsidies and Countervailing Measures
ASEAN	Association of Southeast Asian Nations
ASI	Advertisement Research Institute
ASP	Aviation Safety
AST	Advanced Subsonic Technology
AU	African Union
B&O tax rate	Business and Occupation tax rate
BAN	Basel Action Network
BCA	Boeing Commercial Airplanes
BSES	British Steel Engineering Steels
BSplc	British Steel plc
CAFTA	Central American Free Trade Agreement
CAP	Common Agriculture Policy
CDSOA	Continued Dumping and Subsidies Offset Act
CEC	Commission for Environmental Cooperation
CES	Constant Elasticity of Substitution
CFR	Code of Federal Regulations
CFTA	Canada Free Trade Area
CITES	Convention on International Trade in Endangered Species
CKDkit	Complete Knock Down Kit
CI	Clause
CMLR	Common Market Law Report

CMO	Common Organisation
CNOOC	China's National Offshore Corporation
CNPC	China's National Petroleum Corporation
Co	Company
COM	Committee
COMECON	Council for Mutual Economic Assistance
CPC	Central Pay Commission
CREST	Core Research for Evolutionary Science and Technology
CRS	Congressional Research Service
CTE	Community Test for Environment
CUTS	Consumer Unity & Trust Society
CVA	Canadian Value Added
CVD	Currency Value Devaluation
CWP	Circular Welded Carbon Quality Steel Pipe
DIPP	Defence Industry Productivity Programme
DISC	Domestic International Sales Corporations
DOC	Department of Commerce
DOD	Department of Defence
DOL	Department of Labor
DRAMS	Dynamic Random Access Memory Semiconductors
DSB	Dispute Settlement Body of the WTO
DSTI	Directorate for Science, Technology and Industry
DSU	Dispute Settlement Undertaking of the WTO
EAAE	The European Association of Agricultural Economists
EADS	European Aeronautic Defence and Space Company
EAEC	European Atomic Energy Community
EC	European Community
ECJ	European Court of Justice
ECR	European Court Reports
ECS	Engineering and Chemical Supplies
ECSC	European Coal and Steel Community
EDF	European Development Fund
EEC	European Economic Community
EIB	European Investment Bank
EPA	Environment Protection Agency
EPZ	Export Promoting Zone
ERG	Expert Review Group
ETC	Energy Tax Credit
ETI	Extraterritorial Income Exclusion Act (US)
ETLA	Elinkeinoelämän Tutkimuslaitos (The Research Institute of the Finnish Economy)
EU	European Union
FAO	Food and Agriculture Organisation
FIT	Feed In Tariff Program

FNCE	French Conseil d' Etat
FSC	Foreign Sales Corporation
FSRI	Farm Security Rural Investment Act
GATS	General Agreement on Trade on Services
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Products
GOES	Grain Oriented flat rolled Electrical Steel
GSM	General Sales Manager
GSP	Generalized System of Preference
GTZ	German Technical Corporation (Deutsche Gesellschaft für Technische)
HIID	Harvard Institute for International Development
HPCC	High Performance Computing and Communications
HS System	Harmonized Commodity Description and Coding System
HSR	High Speed Research/Computing Technology
IBRD	International Bank for Reconstruction and Development
ICT	Information and Communication Technology sector
IFAD	International Fund for Agriculture Development
IFPRI	International Food Policy Research Institute
IMF	International Monetary Fund
Inc	Incorporation
INSEAD	Institut Européen d'Administration des Affaires or <i>European Institute of Business Administration</i>
Int Law Rev	International Law Review
IOI	Industrial Oxygen Incorporated
IP	Intellectual Property
IRB	Industrial Revenue Bond
ISBN	International Standard Book Number
ISP Collection	Independent Study Project Collection
ITO	International Trade Organisation
JSTOR	Journal Storage
KFW	Kreditanstalt für Wiederaufbau (Deutsche Airbus)
LA/MSF	Launch Aid, Member State Financing
LCA	Large Civil Aircraft
LDC	Less-Developed Countries
LDP	Local Development Programme
LTD	Limited
LWR	Light Walled-Rectangular pipe and tubes
LWS	Laminated Woven Sacks
MC	Marginal Cost
MEA	Multilateral Environment Agreement
MEMO	Memorandum
MET	Multilateral Environment Treaties
MFN	Most Favoured Nation

MOFCOM	Ministry of Commerce China
MOISA	Markets Organisations Institutions and Stakeholders Strategies
MR	Marginal Revenue
M RTP	Monopolies and Restrictive Trade Practices Act
MVTO	Motor Vehicle Tariff Order
NAEX	Net Agricultural-Exporters
NAFTA	North America Free Trade Agreement
NAIM	Net Agricultural-Importers
NASA	National Aeronautic and Space Administration
NBER	National Bureau of Economic Research
NFEX	Net Food-Exporters
NGO	Non-Governmental Organisation
NME	Non-Market Economy
NPRO	Non-Preferential Rules of Origin
NRCS	Natural Resource Conservation Service
NTN-I	National Treasury Note-Series-I (Brazil)
OECD	Organisation for Economic Co-operation and Development
OH	Ohio
OJ	Official Journal (Eur Lex)
OLCC	Online Computer Library Centre
OTR	Off-the Road Tires
PCB	Poly-Chlorinated Biphenyls
PME	Palm-Methyl Ester
POP	Persistent Organic pollutants
PROEX	Programa de Financiamento às Exportações (Brazil)
PTC	Production Tax Credit
PV energy	Photovoltaic energy
QAT	Quiet Aircraft Technology
R&D	Research and Development
R&TB	Research and Technology Base
R&TD	Research and Technology Development
REEP	Research and Educational Expedition Programs
RIRDC	Rural Industries Research and Development Corporation
RSPO	Roundtable on Sustainable Palm Oil
RSPO	Roundtable Sustainable Palm Oil
S.A. de C.V.	Sociedad Anonima de Capital Variable (Spanish to English: a variable capital corporation)
SAA	Statement of Administrative Action
SAIL	Steel Authority of India Ltd
SAM	State Aid Modernisation initiative
SC	Steel Committee (on steel making)
SCGP	Supplies Credit Guarantee Programme
SCM Agreement	Subsidies and Countervailing Measures Agreement
SDI	Ship Decommissioned Industry

SDT	Special and Differential Treatment
SECOFI	Secretaría de Comercio y Fomento Industrial (Secretariat of Commerce and Industrial Development)
SIDS	Small Island Developing States
SKDkit	Semi Knock Down Kit
SME	Small and Medium Enterprise
SOCB	State Owned Commercial Banks
SPS	Sanitary and Phytosanitary Measures
SRO	Special Remission Order
SSG	Special Agriculture Safeguard
SSJ	Shandong Shouguang Jianyuanchun Co., Ltd (People's Republic of China)
STE	State Trading Enterprises
TEC	Treaty Establishing European Community
TED	Turtle Excluding Device
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of European Union
TNC	Trade Negotiating Committee
TPC	Technology Partnership Canada
TRIPS	Trade Related Aspect of Intellectual Property Rights
UES	United Engineering Steels Limited
UK	United Kingdom
UN	United Nations
UNCTAD	United Nation Conference on Trade and Development
UNDP	United Nations Development Programme
US	United States
US.C.C.P.A	United States Court of Customs and Patents Appeal
USC	United States International Trade Commission
USCA§	United States Code Annotated
USDA	United States Department of Agriculture
USDOC	United States Department of Commerce
USIRC	United States Internal Revenue Code
USLCA	United States Large Civil Aircraft
USSR	Union of Soviet Socialist Republic
VCLT	Vienna Convention on the Law of Treaties
VSP	Vehicle System
WFP	World Food Programme
WGTC	Working Group on Trade and Competition Policy
WISCO	Wuhan Iron and Steel (group) Corporation
WTO	World Trade Organisation

Chapter 1

Regulating Free Trade from the WTO Perspective

Abstract The international legal framework plays a significant role in regulating business, not only within nations but also across national boundaries. No country in the world is sufficient in itself and so everyone has to depend upon each other. It is widely presumed that international trade helps a nation to satisfy the demands of their consumers and supply the surplus to other nations in efficient and economical ways. As the laws relating to trade and commerce can influence the economic, political and social aspects of an individual and society, the Developing and Developed nations considered that the regulation of trade, required some well-developed organization. All the visionary ideas, goals and experiences from earlier discussions took place at the erstwhile GATT, from 1986–1994. During the Uruguay Round, based on the preliminary work and based on formative discussions, it led to the formation of the WTO. This organisation, the WTO began to function, on 1st January 1995. The discussion in this chapter briefly deals with cross border trade issues, the background information preceding the WTO trading system and then formally in the context of the WTO. Within these discussions, a brief reference to the WTO institutional set up, policy mechanisms, promotion of free trade among the Member State and the links established through provisions that forms part of one trading system is covered.

Free trade promotes private entrepreneurship, hence allows each country to specialize in producing the product in regard to which it has a comparative advantage. The free trade market system promoted by the WTO covers both industrial and agricultural sectors of any economy. Along with the promotion of free trade as a key trading principle, creation and generation of wealth by the nations, through procedural checks and balances is a matter of shared concern between the Member States. These concerns are derivatives of fair trade principles. The discussion in this chapter also attempts to figure out historical link for the present day challenges in the matters of trade across borders and between Developed, Developing and the Less Developed countries. The past connection with the issues lead to the formation of the WTO objectives. The study of subsidies is one such key issue. The area of discussion in the chapter briefly touches the specific issue of subsidies which is one of the key subject area of the international trading system based on the principle of free trade.

How far have the forces unleashed by promoting free trade, helped in bringing distributive fairness. . .

1.1 General Discussion on Trading Activity from the Historical and Modern Perspective

Trade between business units is regulated by executives as a part of their collective responsibility, whereas between nations, it is a matter of large-scale economic activity. This explains why there are institutions established by the treaty agreements to regulate trade according to the agreed rules. Presently, it is the WTO that acts as the international-trade regulatory institution.¹ For the promotion of free trade, the WTO is based on the premise for the creation of a market environment through an approach of cooperation among the nations.

The WTO more or less operates on a self-election basis. Respecting the sovereign status of the Member States, institutions like the IMF classify nations as Developed, Developing and Less-Developed. Characterising their status from the WTO perspective, the nations, which are ahead in the use of technology are referred to as the Developed countries and the nations depending mainly upon a rural economy are called Less-Developed countries, while those in between are referred to as Developing nations. This can be better explained by economic reasoning. The underlying, economic rationality that suggests the link between productivity, efficiency, and wealth has been explained by several economists. Robert Solow's point of view, for instance is that "... [i]mprovement in productivity can make a nation richer on a per capita basis, it is not how much capital a country has that makes it rich, rather it is how productive that capital is, and according to him the key to productivity is technology."² While making this point, he further asserts that the United States and other Western countries are not rich because of their natural resources or because of capital gained from somewhere, but rather that they are rich because of the continual improvement in the technological sector. This can also be explained by taking into account the historical facts. The industrial achievements that we see today are due to the perpetual efforts of humans in acquiring knowledge and making practical use of it. The first step started with the concepts of mechanics, next came the age of electronics and today it is the age of computers. All this is the result of group efforts. Nowadays, we have attained the position where human skills, manufactured products, resources, raw materials, have all become a part of trading activity among the nations.³

¹Beinhocker (2007), p. 269.

²Robert Selow quoted in Eric Beinhocker's book (Beinhocker 2007, p. 41).

³R. Selow referred to in, "Technology and International Differences in Growth Rates." Fagerberg (1994), pp. 1147–1175.

As a matter of fact, technology leads to a greater productivity from resources and capital investment, enhances profits, and promotes methods for more savings and greater capital formation. Without technological advancement, capital can only have a restricted growth in proportion to the population. The progressive use of scientific knowledge in the production sector primarily requires a conducive environment and the unhindered economic support that can be provided by the institutions. This is one of the key reasons that in the pursuit of innovation and technological progress, the TRIPS⁴ agreement is included in the WTO. In addition to this it is also worth mentioning, that from the perspective of equity based principles, along with technological advancement, the fundamentals of the WTO are also based on features supporting long-term progressive and welfare policies for the Member States through free trade.

1.2 Previous Trade Regulating Institutions Before the WTO, the ITO and GATT

The foundations of the WTO, which began to function on 1st January 1995, were laid down in 1986–1994. The negotiations termed as the *Uruguay Round* started in the preceding trade institution known as GATT. GATT was established in 1947 and lasted until 1994. GATT as an institution was created specifically, for trade-related issues, and for the economic co-operation among the Member States.

The origin of GATT can be traced to the US Government's proposals for the expansion of World Trade and Employment. The proposal was published in December 6, 1944 and subsequent to the publication of the proposal at the first meeting of the Economic and Social Council (ECOSOC) of the United Nations (UN) in 1946, the United States introduced a resolution calling for an international conference on trade and employment.⁵ The resolution was unanimously adopted and the ECOSOC appointed a preparatory committee. During the same time interval, the US government also developed a Suggested Charter for an International Trade Organization (hereafter, Suggested Charter) and circulated it to the preparatory committee. The first meeting of the preparatory committee, except for adding a chapter on *economic development*, essentially adopted most of the US draft. The Developing countries including India criticised the Suggested Charter, as lacking a development agenda for the Developing countries and considered that it was rather designed mainly to support the policies of the industrial countries.⁶

⁴TRIPS:- "Agreement on Trade-Related Aspects of Intellectual Property Rights." The TRIPS agreement is Annex 1C of the Marrakesh Agreement Establishing the World Trade Organization, signed in Marrakesh, Morocco on 15 April, 1994.

⁵Srinivasan (2009), p. 9.

⁶Srinivasan (2009), pp. 9–10.

The negotiations that led to the formation of GATT and the discussions on a draft charter for the ITO were conducted simultaneously at the second meeting in Geneva. The meeting that was held for the preparatory committee of the Havana conference.⁷ The aim was to create the ITO at the UN Conference on Trade and Employment in Havana, Cuba in 1947.⁸ However, in the draft charter for the ITO, the authorisation for negotiating a tariff reduction delegated by the US congress to the president was restrictive. The power delegated did not authorised the US president to negotiate an agreement to establish an international organisation with the United States as a member. Thus ITO could not came into function.

As a result of all these ups and downs, it was decided that GATT was only to be a multilateral agreement and not an organisation although, it was designed to operate under the umbrella of the ITO once it came into being.⁹

As the ITO practically could not came into existence, the combined package of trade rules and tariff concessions in the ITO Charter, that Member Nations had negotiated exclusively, led to the working of a General Agreement on Tariffs and Trade (GATT). GATT's basic legal principles remained the same as they were in the previous ITO.

The formation of GATT was like an attempt to establish a forum, so as to take preliminary steps in the direction of finding economic and political solutions to the problems of the nations by negotiations. The basic objectives of GATT was to promote trade among the nations and provide technical assistance for the development of the nations and an upliftment of the standards of citizens.¹⁰

From its very inception, GATT brought together a diverse group of countries. Its wider scope of objectives and procedural effectiveness supported the common goal of *multinational trade liberalisation* and encouraged the new countries to join this trade-regulating institution. In the decades that followed, the momentum of trade liberalisation led to an exponential trade growth within the Members States, surpassing the consumer demand. This made it clear that despite its heterogeneity, the Member State's ability to trade with each other and to share the benefits of trade was established. GATT succeeded in reducing tariffs to lower levels. Nevertheless, a series of economic recessions in the 1970s and early 1980s, forced the governments to devise other forms of protection for sectors facing increased foreign competition.

Since, the Bretton Woods International Monetary System,¹¹ there have been substantial changes in trading patterns and the basic conditions of the economy of

⁷Srinivasan (2009), p. 10.

⁸United Nations Conference on Trade and Employment. Final Act and the related Documents. New York. April, 1948 https://www.wto.org/english/docs_e/legal_e/havana_e.pdf.

⁹Srinivasan (2009), pp. 10–11.

¹⁰Mavroidis (2005), p. 3.

¹¹Bretton Woods Conference, officially called the United Nations Monetary and Financial Conference was held on July 1–22, 1944. The Bretton Woods system was the world's most recent experiment with a fixed exchange rate regime. Although it was originally designed as an adjustable peg, it evolved in its heyday into a de facto fixed exchange rate regime. The architects of the

nations. The emerging economies of the world, often categorised as Developing and Less-Developed have experienced these sudden changes and also the unexpected effects of market buoyancy. Undoubtedly, these changes have generated high hopes for some nations, but on the other hand, there are many nations that consider themselves trapped in this vicissitude due to many factors.

However, it is widely presumed that international trade helps a nation to satisfy the demands of their consumers and supply the surplus to other nations in efficient and economical ways. As the laws relating to trade and commerce can influence the economic, political and social aspects of an individual and society, the Developing and the Developed nations¹² considered that the regulation of trade required some well-developed organisation. This organisation was to consist of experts that could work beyond political considerations, and its goal would not be, simply short-term perspectives rather it could make objective analyses whenever required. As a part of regulatory measures these experts were to be capable of interpreting and enforcing treaties and agreements and can penalise in the case of aberrations. All the visionary ideas, goals and experiences from earlier discussions took place at the erstwhile GATT as a discussion form, from 1986 to 1994. During the Uruguay Round this led to the formation of the WTO. This organisation, the WTO began to function, on 1st January 1995.¹³

1.3 What Is the WTO?

The WTO is a multilateral trading system that developed from GATT. Despite several odds in the beginning, it has striven for its objectives and has kept its members in a progressive framework towards liberal trading principles. The system, developed over the years both in terms of membership and issue coverage, culminating in the establishment of the WTO in 1995.¹⁴

From an international law perspective, the WTO/GATT are treaty-based organisations, in the light of the fact that all the WTO agreements and treaty provisions are binding on the Member States.¹⁵ When signing the Uruguay Round Agreement, all the parties agreed that the WTO treaty agreement was to be accepted in a

Bretton Woods system wanted a set of monetary arrangements that would combine the advantage of the classical gold standards (i.e. exchange rate stability) with the advantage of floating rates (i.e., independence to pursue national full employment policies). They sought to avoid the defects of floating rates (destabilising speculation and competitive beggar thy-neighbor devaluations). Bordo and Eichengreen (1993), pp. 3–5. <http://www.nber.org/chapters/c6867>.

¹²Developing and Developed nations based on the WTO classification.

¹³Bossche (2008), p. 77.

¹⁴World Trade Report (2007), p. xxx. www.wto.org.

¹⁵WTO Agreement Art II. (2).

comprehensive manner, which is also designated as a single undertaking.¹⁶ After attaining membership, a Member State has an inherent obligation to ensure the conformity of its domestic legal system and the related statutory provisions and regulations with the WTO agreements.¹⁷ Nevertheless, exceptions are allowed depending upon the economic and political situation of the nations.

The ability of the GATT/WTO system, to accommodate the different needs of Member States, has been an important factor in its success. All the decisions concerning the rules for framing new provisions are taken collectively by the Members as a whole, either by ministers, who gather at least once every 2 years or by their ambassadors or delegates who meet regularly in Geneva. There are two modes of decision-making in the WTO, the consensus method and the voting method. Decisions are deemed to be decided by consensus, if none of the Member State present at that meeting objects to the proposal. Where a decision cannot be taken by consensus, the decision in the ministerial conference is taken by a majority of the votes cast, unless otherwise specified in the WTO agreement.¹⁸ Although, there is a possibility to choose voting in the WTO system, in a situation where a consensus cannot be reached, however, the preference to resolve issues through consensus remains the priority. On the contrary, GATT 1947 covered mainly the voting method and there was no explicit reference of the word consensus in this previous institution.¹⁹

The WTO is specifically a trade-regulatory organisation, however, it is different from the other organisations. Structured in such a way that it virtually covers both legal and economic issues of international trade, which is also evident from the procedural aspect followed by the DSB. Briefly, the WTO can also be regarded as a set of rules and agreements negotiated by a group of the world's trading nations.

With the formation of the WTO, the discussions on the unsettled issues among the Member States remains ongoing. The primary function of the WTO as a multilateral organisation is to regulate trade amongst the Member States, and this also means a forum for the discussion of many crucial matters such as subsidies.

In comparison to other global institutions, the WTO has distinct objectives; the main objectives of the WTO are to promote free trade, and create fair opportunities for development among its Member States.

¹⁶Article XI, 1. The contracting parties to the GATT 1947 as of the date of entry into force of this Agreement and the European Communities, which accept this Agreement and the Multilateral Trade Agreements and for which Schedules of Concessions and Commitments are annexed to GATT 1994 and for which Schedules of Specific Commitments are annexed to GATS shall become original Members of the WTO.

2. The least-developed countries recognised as such by the United Nations will only be required to undertake commitments and concessions to the extent consistent with their individual development, financial and trade needs or their administrative and institutional capabilities.

¹⁷WTO Agreement Art XVI.4.

¹⁸Matsushita et al. (2003), p. 12.

¹⁹Ehlermann & Ehring (2005), pp. 51–75.

1.3.1 From the Perspective of the WTO Objectives

The WTO was formed after the Uruguay round, 1986–1994, and based on earlier negotiations held during GATT conferences resulting in the following core objectives being adopted.

First, to liberalise trade among Member States.

Second, to ensure that Developing nations and the Less Developed countries obtain a level of share in the growth of international trade.

Third, that due importance should be given to sustainable development, sustainable development is important for the protection and preservation of the environment along with the overall economic growth of countries.²⁰

Fourth, after signing the TRIPS agreement, a minimum standard for various forms of intellectual property (I.P) regulations has to be maintained by the Member States.²¹

However, it must be highlighted that the overarching role of this multilateral institution cannot be confined to these objectives only. WTO policies take into account the specific needs of Developing and Less-Developed countries, and also considers other matters of primary concerns such as, raising standards of living, creation of jobs, creating economic prosperity, equitable distribution of resources, placing a check on environmental degradation and the protection of public health. The fulfilment of the WTO objectives is a step-by-step process, which also requires an understanding of the market forces in the Member States.

1.4 International Law Norms and the WTO

The WTO, being a treaty-based organisation, specifically formed to regulate trade among Member States, is in principle part of international law, as any other international organisation. As an international institution, the WTO derives legality from the general principles of international law and treaty agreements which is clear from the working procedure of the dispute settlement body. Even though the establishment of this organisation has created a new system of international trade,

²⁰In fact, within the WTO framework, there is no specific agreement dealing with the environment. The objectives of Sustainable Development and Environmental Protection are stated in the preamble to the Marrakesh Agreement establishing the WTO. The Doha Round of the WTO negotiations has linked certain aspects of trade with the environment and also assigned some task to a regular environment committee.

²¹Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS), is an international agreement administered by the World Trade Organization that sets down minimum standards for many form of intellectual property regulation. It was negotiated at the end of the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) in 1994.

so as to promote free trade among its Member States, nevertheless, the general treaty rules of international law²² are still the legally-binding rules.²³

The WTO is part of the international legal system, therefore the peremptory norms of international law have the same non-derogatory status in the WTO system. These norms cannot be violated by any Member State either through international treaties or local or special customs, nor can an interpretation be made in clinical isolation from public international law.²⁴ An alternative explanation might be that the relevance of peremptory norms, i.e., *jus cogens*, carries the same significance as it has with other international organisations.²⁵ Certain norms are considered as the basis of international law, so there is customary prohibition against any violation of *jus cogens*.²⁶ However, it is difficult to conceive the real status of *jus cogens* and demarcate its boundaries. The DSB of the WTO, with the primary objectives of settling trade disputes between the Member States, accepts the status of *jus cogens*. As the human rights aspects are part of the general principles of international law (*jus cogens*), so on several occasions, they become linked to international trade issues.

Occasionally, human-right dogmas are quite widely interpreted, thus creating normative crisis because of the conflict of interest, for examples the issue of child labour, women's rights and several other similar issues. So far as the legal eligibility of entertaining a plea for the settlement of a trade dispute is concerned, litigation on the grounds of human rights violation cannot be entertained in the WTO dispute settlement body,²⁷ nevertheless, it is expected that the interpretation of the WTO provisions should be made in good-faith and consistent with human rights treaties. As a matter of fact, the WTO members do not appear to have granted any responsibility to the dispute settlement body for adjudicating matters concerning human

²²Article 3.2 of the DSU: The Dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system. The members recognise that it serves to preserve rights and obligations of members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law. Recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements.

²³Article 26, Vienna Convention on the Law of Treaties. *Pacta sunt servanda*.

²⁴In the case of *United States—Standards for Reformulated and Conventional Gasoline, WT/DS2/AB/R*, (see page no 17, of the AB report) AB in the matter before it, concerning the interpretation of Article XX by the Panel, in relation to the baseline establishment rule applied by the US for the conservation of natural resources, stated, the general rule of interpretation has attained the status of a rule of customary or general international law. As such, it forms part of the customary rules of interpretation of public international law which the Appellate Body has been directed, by Article 3 (2) of the DSU, to apply in seeking to clarify the provisions of the General Agreement and the other covered agreements of the Marrakesh Agreement Establishing the World Trade Organization. This direction reflects a measure of recognition that the General Agreement is not to be read in clinical isolation from public international law. The Appellate Body observes that the Panel Report failed to take adequate account of the words actually used by Article XX in several paragraphs.

²⁵See preamble of the WTO.

²⁶Gabrielle (2002), pp. 753–814.

²⁷Abbott et al. (2006), p. 188.

rights. Issues such as human rights are seen more as value based.²⁸ In the case of a normative conflict, *jus-cogens* often enjoys primacy, either through binding obligation by adopting interpretation of provisions of the agreements in harmony with- *jus cogens*, or, by invalidating a conflicting WTO provision.”²⁹ The prevalence of this feature can be seen in various WTO conferences where issues, such as labour standards, the banning of child labour and so on, are discussed.

Another debatable issues, involving normative interpretation, that needs to be discussed here can be classified as (1) the choice between trade and social values and (2) the interaction of MEA with the WTO aims of free trade. Environmental issues are relevant to the protection of nature. The protection of nature requires that there should be value based trade policies. With regard to trade between Developed and Developing countries, it is important to highlight these issues as well, because often the environmental conditions are tampered with due to trade benefits. International law governs both the WTO Agreement and its interaction with Multilateral Environment Agreements, (MEAs). In cases where an Appellate Body or panel has to establish priorities between the MEA and the WTO provisions, the panel and Appellate Bodies for applying fairness as a regulatory measures, attempt to strike a harmony between free trade and fair trade values. The concept of free trade does not prevail over other values. **Article XX of GATT, lists certain exceptions to free trade.**³⁰ The question of a balance between legal principles promoting free trade

²⁸Value-based here means, that; the concept and realization of human rights are relative for the different societies.

²⁹Gabrielle (2002), pp. 753–814.

³⁰Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on international trade, nothing in this agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:

- 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 and 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, trademarks and copyrights, and the prevention of deceptive practices;
- e) relating to the products of prison labour;
- f) imposed for the protection of national treasures of 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 and consumption;
- h) undertaken in pursuance of obligations under any intergovernmental commodity agreement which conforms to the criteria submitted to the contracting parties 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 issues of sustainability arose in the case of **United States-Standards for Reformulated and Conventional Gasoline**,³¹ and in the **United States-Import Prohibition of Certain Shrimp and Shrimp Products**.³² It is likely that the Article XX exception clause is circumvented for protectionism and the issue in the first case was somewhat like this. The Appellate Body in this case followed an approach of *lifting the veil* and stated “disguised restriction on free trade is like disguised discrimination.” Further, the Appellate Body added that if a Member State allowed the imports on a conditional basis, that the environment criteria should be fulfilled; however, this can be justified only if the same environment standards are applied to similar domestic products, thus fulfilling the national treatment criteria and giving equal treatment to the imported products.

This matter concerned the protection of an endangered species. Finally, the Panel in (United States-Import Prohibition of Certain Shrimp and Shrimp Products) urged “Malaysia and the United States to cooperate fully, in order to conclude, an agreement which would permit the protection and conservation of sea turtles to the satisfaction of all interests involved and taking into account the principle that states have common goals but differentiated responsibilities to conserve and protect the environment.”³³

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- 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 contracting parties 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 them have ceased to exist. The contracting parties shall review the need for this sub-paragraph not later than 30 June 1960.

³¹In the case between, US and Brazil, WT/DS2/9, para 6.39, the Appellate body partly upheld the panel’s decision and directed modification to the rest. The Panel, referring to the Herring and Salmon case, stated that as the preamble of Article XX indicates, the purpose of including Article XX (g) in the General Agreement was not to widen the scope for measures serving trade policy purposes but merely to ensure that the commitments under the General Agreement, do not hinder the pursuit of policies aimed at the conservation of exhaustive natural resources. Para.6.40, the panel then proceeded to examine whether the baseline establishment methods can be linked to “primarily aimed at” achieving the conservation objectives of Gasoline rule.

³²Case between Malaysia and U.S: See WT/DS58/RW.

³³Appellate Body stated in its report, para 156, turning then to chapter XX, “we consider that it embodies the recognition on the part of WTO members, of the need to maintain a balance of rights and obligations between the right of a member to invoke one or another of the exceptions of Article XX, specified in paragraphs (a) to (j) on the one hand, and the substantive rights of the other members under the GATT 1994, on the other hand. Exercise by one Member of its rights to invoke an exception, such as Article XX (g) if abused or misused, will to that extent, erode or render naught the substantive treaty rights in, for example, Article XI:1, of other Members. Thus, a balance must be struck between the right of a Member to invoke an exception, under Article XX and the duty of that same Member to respect the treaty rights of the other members. To permit one member to abuse or misuse its right to invoke an exception would be effectively to allow that member to degrade its own treaty obligations as well as to devalue the treaty rights of other members.”

The decisions in these cases made the position clear that the WTO as an institution promoting trade between the nations also acts as a regulatory organisation within the parameters of the general principles of international law. The significance of this organisation can be objectively measured as it takes into account other issues beyond free trade. These issues seem to be value based and can be termed as an approach towards fair trade values, hence, more or less pursuing the principles of “free and fair trade complementing each other.”

1.4.1 The WTO and the Domestic Legal System

International institutions expect compliance of the treaty provisions and this requires a legal support base. With regard to creating legal certainty, states are bound by the provisions of Article 26, 27, 28 and 31 of the Vienna Convention on the Law of Treaties. Article 26 covers the principle of *Pacta sunt servanda*. Practically for the application of these treaties, the WTO provisions have to face differing legal systems,³⁴ within the Member States before a treaty is finally adopted or harmonised, which, indeed, is a complicated process. On the basis of a general comparison with the existing legal systems of the Member States, it is presumed that the domestic policies of Member States may not be conducive for accomplishing the WTO objectives of free trade during the initial phases. Member States may be required to make changes in their internal legal system, so that treaty provisions are in harmony with their domestic legal system. The different methods for implementation depend upon the constitutional structure adopted for treaty implementation and has been described in detail by international law theories on Monoism³⁵ and Dualism.³⁶

1.4.2 Flexibility at the Normative Level, an Economic Necessity

The issue of normative flexibility, in international law, has again arisen as a matter of debate after the formation of GATT/WTO. The primary objective of this organisation is to deal with the problems of the international trade of its Member States, which makes it a system of choices and arrangements. When tested as regards new situations, the existing defined area of international legal norms cannot

³⁴Sauve & Grastek (2006), pp. 837–864.

³⁵Monoism maintains that national legal rules and international law rules or treaty obligations that a state has accepted can be directly applied.

³⁶In the case of dualism, international agreements are brought into a domestic legal system for implementation after harmonizing them with national law. This means that an act of parliament has been passed on the matter.

provide the appropriate level of support to the social, political, and economic basis, in order to meet the WTO objectives, as they are based on old propositions. The nature of the existing normative system seems to be facing deficiencies in reaching the appropriate conclusions, and this often leads to a debate about the relevancy of the existing norms. With the specific objectives of the WTO i.e., to promote free trade market principles, at an equal level, among all the nations despite their diversity, this will undoubtedly demand the potential for an evolution of new rules at the normative level. The need to create flexibility at the normative level and can be marginalised after has to be faced, while interpreting and applying both domestic law and international law for the fulfilment of the WTO objectives.

1.5 The Political Economy Dimension

The WTO is also viewed as an outcome of globalisation, and in this regard, an outlook from a political and economic perspective also takes account of the realities, such as, sovereignty, drawing a balance between globalisation and domestic policies, the relationship between Developed, Developing and Less-Developed countries, and between the IMF and the WTO. The extent of the influence on the state's political system, subsequent to acquiring membership of the WTO also necessitates consideration from the political perspective. The issue of political economy has become a topic of debate among constitutional lawyers, as to test whether the constitutional concepts of sovereignty remains at the same level after the ratification of the WTO, as before. During the WTO conference negotiations, it is often noticed that the position of the advanced economies is dominant. At times, the dominant economic position of the advanced nations within the WTO impinges on the present sovereign status of smaller nations. This has become a source of political and economic debate. In the strict constitutional sense, the term sovereignty has been interpreted as non-interference in the matters of nation-state, but, it often occurs that the WTO tries to create an order of the nations based on economic groups such as the G8, G8+5, G 14 and G 20 and by this means influences the policies of smaller economies. In the wake of economic globalisation, there are several instances where the market measures adopted by one nation influences the policies of other nations.

The contribution of the newly formed market mechanism to economic growth has proved significant. Subsequent to the Member States signing the WTO Agreement, it is hard to imagine that any process of substantial development could be accomplished without these market liberalization policies. The role of the constitutional mechanism however cannot be sidelined. After attaining membership, Member States are expected to reduce tariffs, complimented by non-discriminatory practices to like products from other Member States. This new feature of the market system is characterized by treaty based norms. In addition to this norm, there has been an institutionalization of development norms. These Development norms support flexibilities being extended to the Developing and Less-Developed countries. The

development objectives also have constitutional support base within the Member States. The multilateral norms supporting market liberalization policies are different in character from the development norms supported by constitutional objectives, reason being that the constitutional objectives are based on the rights of the individuals.

It is often the case that the market liberalization agenda is heavily supported by the Developed countries. The interface between the normative aspects, multilateral and the domestic agenda based, often create complexities, as the domestic issues are compelled to a bargain, such as in the matters of food security, subsidies for development, product standards, and several others.

The concept of sovereignty also gets challenged internally within a Member State, as a free market requires a decentralised decision-making process so as to counter protectionist policies, risk of monopolies, actions by some political or economic (governmental or non-governmental) entities, as these can challenge the accomplishment of the objectives of the WTO.³⁷

Despite the promotion of free trade, nations need to exist within the political reality that trade agreements reduces market barriers, but political barriers still remain. These political barriers cannot be ignored, as in the absence of state structures, the GATT/WTO based market concepts cannot work. Globalisation in political terms requires the right kinds of policies to maintain the balance between the objectives of the WTO and the national interest of the Member State. Using international agreements as a commitment device for increasing the market size in order to ascertain bargaining power, are less likely to motivate smaller nations to be part of multilateral-trading system, as there are high risks of losses for the Developing and Less-Developed countries.

The primary objective of economic globalisation is the removal of protectionist measures and also creating possibilities for economic development. This idea is basically-an outcome of neo-liberalism.³⁸

In order to establish any assumed level of International market environment, the removal of trade barriers is required, no matter how gradually. Moreover, the economic globalisation is based on the assumption that market forces and commercial activities are efficient methods for producing and supplying goods and services. By adopting liberal trade policies, this will create an environment of competition at the production level, and eventually resolve production in an efficient manner on a natural basis. Concisely, it can be said that free trade can possibly help to secure the exchange of different goods, at the real value market price.

³⁷Hudec and Southwick (2002), p. 29. www.cambridge.org/9780521813198.

³⁸Neo-liberalism comprises two notions “neo” and “liberal” meaning free from government intervention. Adam Smith advocated the abolition of government in economic matters so that trade could flourish and first introduced liberalism in mid-1770. Sue L.T. Mc-Gregor, Janice Doull and Larry Fisk, “Neoliberalism, Microbes, and Peace: A human ecological perspective,” p. 1. <http://www.kon.org/archives/forum/14-1/McGregor.html>, forum paper.