Regionalism and Trade Facilitation: A Primer

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1. Introduction

This article investigates the conditions under which trade facilitation reform should be undertaken at the regional level. Looking at both efficiency and implementation considerations, it confirms the perception that the regional dimension matters. First, investigating where efficiency gains can be made, this research explains why national markets alone fail to produce the full-scale economies and positive externalities of trade facilitation reform. Networks in transport, electronic exchange of information, and finance (especially for transit), joint administrative structures, and regulatory cooperation are important domains where regional public goods can be delivered. Competition considerations also matter.

Second, because trade facilitation policies need to address coordination and capacity failures, but also because of the operational complexity challenge, the choice of the adequate platform for delivering reform is crucial. The article concludes that regional trade agreements offer good prospects of comprehensive and effective reform and can effectively complement multilateral and national initiatives.

Examples of implementation of trade facilitation reform in regional agreements do not however, indicate that regional integration approaches have been more successful than under specific cooperation agreements, or other efforts, multilateral or unilateral. Customs unions may be an exception here, and we suggest reasons why this could be the case.

Regional trade facilitation reform is important; by investigating some of the reasons why regional intervention could make a difference this article hopes to provide policy makers with some guidance for designing regional cooperation in this area.

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Trade facilitation reform is the sum of efforts undertaken at the national, regional and multilateral level to reduce trade transaction costs. Multilateral discussions on trade facilitation have stepped up recently by being part of the WTO agenda of negotiations: until then trade facilitation was addressed in the GATT in a relatively modest fashion. Other more detailed multilateral instruments, such as the Kyoto Convention, have not mustered enough momentum for reform. Parallel to multilateral efforts, recent regional trade agreements have gradually incorporated trade facilitation dimensions (Moïsé, 2002).[1] However, to date, the majority of trade facilitation efforts are undertaken unilaterally, including by low and middle income countries that were thought to lack the capacity to do so.[2]

While multilateral, regional and national interventions might be competing to achieve identical aims, they more likely coexist because of their complementarities, and by virtue of the specific comparative advantages of each approach. However, in discussions about trade facilitation reform, the regional dimension has not been the object of as much attention as national and, recently, multilateral reform. Besides, when trade facilitation reform has been envisaged, for instance in the context of development banks regional work, or in regional trade agreements, the rationale for the regional dimension of reform is not always clearly expressed. We also suspect that in many instances a narrow focus on discrete reforms has prevailed over more holistic approaches. Of course there are exceptions.

Our working hypothesis is that in some instances regional solutions, by contrast to purely national or multilateral solutions, would offer the best prospect for meaningful trade facilitation reform. This article focuses on investigating more thoroughly how regional initiatives can contribute to trade facilitation reform. As international trade and the costs associated to it involves activities beyond a single border, the question of where the optimal level of policy intervention lies – unilateral, regional or multilateral – needs to be examined. In essence, this article explores when regional trade facilitation reform should be undertaken (the economic case), but also when or how this could be undertaken (the implementation issue). With what some perceive as the limits of multilateral trade negotiations, in particular in relation to development and implementation issues, eyes turn again towards regional solutions. This research does not put itself in this perspective, but rather aims at understanding better how regionalism – a force that cannot be denied – can ideally complement and contribute to the facilitation and liberalization of trade.

This article sets itself in the direct continuation the broad investigation into regionalism by the World Bank, a research that was summarized in Schiff and Winters (2003). The specific topic of trade facilitation, although mentioned in various outputs of this research programme, did not receive full treatment. In an earlier work the authors provide insight into the relevance of regional trade agreements for several policies, among them transport, itself an element of trade facilitation. They note, as we do in detail below, that "in the presence of economies of scale or inter-country externalities, market

[1] We should note with different motives in sight than those underpinning the WTO negotiations.

[2] An example is Senegal, which devised its own basic electronic single window system. Over 80 countries have also implemented Asycuda electronic customs modules provided by UNCTAD.

solutions are generally sub-optimal, and failing to cooperate can be very costly. However, regional cooperation is not the same as regional integration, and, indeed, there is generally rather little connection between them" (Schiff and Winters, 2002).[3]

This remark alludes to the two main dimensions of regional trade agreements investigated in this article. First, from an economic perspective, under what circumstances regional initiatives are optimal given market failures affecting the supply of trade facilitation services and regulations? Because markets are imperfect, governmental intervention is sometimes needed to deliver the optimal social outcome. When market failures cannot be remedied at the national level, addressing this becomes a transnational issue and collective action is needed; regional solutions shall be sought when the failing markets correspond to some well-defined set of nations.

Second, when do regional approaches offer better and more cost-effective prospects than other solutions (regional, unilateral or multilateral) to achieve the objective of trade facilitation reform? A "subsidiarity" test needs to be applied, by which actions to achieve a given policy objective should be taken at the lowest level of government capable of effectively addressing the problem at hand (Sauvé and Zampetti, 2000). Ideally, this level of action should correspond to the level affected by the need to provide the regional good, meaning that the political jurisdiction matches the economic domain of benefits. Thus the most appropriate participants will partake in the provision of regional trade facilitation and transaction costs will be economized (Arce and Sandler, 2002). Regional institutions also vary in nature and we examine which are more likely to promote effective facilitation of trade.

2. The Economic Case

What we mean by trade facilitation. There is no universal understanding of what trade facilitation is (Wilson *et al.*, 2002), reflecting differences, as well as some evolution, in view of what should be the reforms undertaken to reduce the cost of trading. In simple terms trade facilitation is the simplification of the trade interface between partners. This trade interface is composed, broadly, of compliance to government rules by traders, enforcement by authorities of these rules (including taxes), exchange of information, financing, insurance, ICT and legal services, transport, handling, measurement and storage. We focus therefore in the rest of this article on this broad conception of trade facilitation as the private and public interventions that help goods cross borders.

Government interventions in all these aspects of the trade interface affect the magnitude of transaction costs incurred by traders. For example, the sheer diversity of government regulations, and the replication of their enforcement, causes duplication (e.g., compliance cost with two different standards: Baldwin, 2000) and friction costs (e.g., time lost because of repeated loading and unloading of merchandise) that regional harmonisation and cooperation could conceptually help address (Schiff and Winters, 2003: 82).

[3] On the substantive differences between regional trade and cooperation agreements, see Devlin and Estevadeordal (2004).

2.1. The relevance of geography for the tangible and intangible dimensions of the supply chain

Country borders create costly obstacles to international trade. The empirical reality of the "border effect" is demonstrated by the gravity model of international trade (for a recent overview, see Anderson and Wincoop, 2002). Trade flows between pairs of countries are proportional to their gross domestic product and inversely proportional to the trade barriers between them. It is well known from this literature that trade transactions are determined by geography, and more broadly by non-policy elements that draw two countries closer. It is customary to include indicators of geographic proximity such as distance and common borders as well as broader indicators of proximity such as commonality of language, legal systems, history, etc. Some barriers to trade facilitation are associated with these "natural barriers", which have a lot to do with geography.

Components of the international trade interface are intangible (e.g., payments), and others are tangible (physical transport). Looking first at the tangible aspects of the international supply chain, it is relatively straightforward to identify components affected by geography: transport; storage; and physical inspection and presentation of documentation at border agencies. Taking the example of transport, international road shipping involves border crossing, and transit through neighbouring countries. Road and rail transporters have to meet possibly different local legal regimes and standards. Different transport standards, such as varying maximum axle loads permissible for trucks (Namibia, Zambia, Botswana),[4] or changing rail width for trains, necessitate unloading and reloading and disrupt the supply chain.[5] Compliance with different regulations at each border increases compliance costs and adds to the time spent there.

Enforcement of border agency controls is highly localized, often (though not solely) near border crossings. When crossing several borders, costs have to be incurred many times if customs do not cooperate (at the border of the originating and destination country, and of countries of transit). Arvis *et al.* (2007) talk of "triple clearance time" because of duplicating lengthy clearances on most transit corridors in least developed countries. The cost of duplication is also magnified by the number of regulations affecting trade implemented by border agencies, including entry visa requirements, technical and phytosanitary standards, security checks, tax levying, etc.[6] Such requirements involve producing paper documentation at border posts, storage in bonded warehouses and physical

[4] Röschlau (2003).

[5] Lack of regulatory interconnection of rail systems also creates disruptions. Before its collapse in 1977, the East African Community (Tanzania, Kenya and Uganda) had an integrated rail network. In the 1980s, Kenya Railways Corporation was transporting twice the volume of freight that it now carries. See <http://web.worldbank.org/external/projects/main?pagePK=64283627&piPK=73230&theSitePK=40941&menuPK=228424&Projectid=P079734> for more info.

[6] De Wulf and Sokol (2005) give this example: "the United States Customs and Border Protection enforces laws on agriculture, alien and naturalization, banks and banking, census, commerce and trade, conservation, copyrights, crimes and criminal procedures, customs duties, food and drugs, foreign relations, internal revenue, intoxicating liquors, money and finance, navigation, patents, postal service, public building and property, public land, railroads, shipping, telegraphs and telephones, territories and insular possessions, transportation, war and national defense, and international treaties, statutes, and agreements".

inspections. The tangible elements of international trade transactions therefore strongly suggest that costs are geographically localized. This may require local solutions, such as the sharing of border facilities.[7]

However, a feature of modern trade facilitation is the elimination of costly physical operations. The tangible nature of trade transactions is thus reduced: paper work is replaced by electronic documentation (de-linking the production of documentation with the physical flow of goods; National Board of Trade, 2003), while modern risk management and non-intrusive techniques reduce considerably the need for physical inspection. One consequence is that transport costs become less related to geographical distance.

Does this imply that the regional dimension does not matter for intangible aspects of international trade? Not necessarily. The border effect also holds for services (Kimura and Lee, 2006). Portes and Rey (2005) show that cross-border equity transaction flows, which, because of their intangibility, one would have presumed not to be affected by transaction costs, are subject to similar determinants as goods flows. Geography is therefore an issue. Regional proximity indeed favours better information flows between traders, shared cultural references, and importantly for trade facilitation, practices and common systems developed over time.

2.2. Implications for trade facilitation reform

What does this mean for trade facilitation reform? First, since proximity is associated with the existence of location-based transaction costs, this could imply that groups of countries who incur common local transaction costs could try to address them jointly. In a way this means that there are countries with whom it is more "natural" to cooperate with to implement trade facilitation than others. Some economies of scale are geographically dependent, such as physical transport networks.

However, the attractiveness of geographical proximity does not hold for many other aspects of international trade facilitation, and the "natural partner" may be one far away. Groups of countries that enjoy already high volumes of trade, and presumably already share good knowledge of the trade facilitation impediments arising in their trade, may well be better placed to undertake reform together than with other countries.

In summary, the relevance of proximity can be established for trade facilitation, but it provides relatively little guidance other than a general presumption that there is some role for regional intervention. Regional cooperation should then be guided by the identification of efficiency gains realized at the scale of the region.

There are two main dimensions to the benefits of transnational cooperation, corresponding to the specific market or institutional failures faced by countries: first, the realization of economies of scale, including by elimination of duplication and increasing competition; second, through the avoidance of negative and creation of positive externalities

[7] Discussed below in the text.

among neighbours. Obviously, in order to make sense from a regional economic perspective, cost reduction must either be more efficiently undertaken regionally than, say, multilaterally, or belong to costs categories that are incurred only regionally (i.e., on a geographical basis). The question of delivery of regional public goods is particularly relevant in this respect.

2.3. Realizing socially optimal economies of scale

With many interventions and parties in the international transport of goods, and possibly the crossing of several borders, there is plenty of scope for cost duplication for trade operators. An important portion of these costs being fixed, eliminating any duplication will enable efficiency gains for firms, but also allow smaller-scale operators to access export markets, an important aspect for developing countries.[8] Additionally, because some of the procedures and services that facilitate trade involve large fixed and possibly sunk costs, full economies of scale in the administrative procedures and services to international trade transactions may not be realized at the country level, especially in small and poor countries.

Duplication arises because similar requirements must be met repeatedly, but also because national rules differ, therefore also increasing search costs and associated uncertainty,[9] and creating further opportunities for rent seeking and corruption. COMESA's regional carrier's licensing system illustrates how duplication can be tackled. The regional license dispenses with the need to pay for multiple licenses (Schiff and Winters, 2003: p. 81). Likewise, inspection of goods, if carried out in different places on each side of a border delays trade. Different national regulatory requirements force traders to meet two standards instead of one: in Tanzania registration requirements for agro-chemical pesticides are burdensome and subject to high fees, despite the fact that Tanzania's market for such pesticides is small and that equivalent and more efficient products are already registered and tested in neighbouring Kenya (Tanzania DTIS, 2005).[10]

Solutions to reduce duplication costs may involve harmonization, forming a common market within a customs union, mutual assistance among authorities (an important facilitating practice for customs valuation),[11] and mutual recognition of rulings (e.g., for transit operations) and of certification and testing (e.g., for standards). Such cooperation is not necessarily regional or bilateral and can also be achieved multilaterally. It may, however, be the case that a large part of these extra costs are better addressed at the

[8] World Bank (2005: p. 85) quotes for instance the cost of certification of organic nut production in Moldova for export to Germany, which can amount to USD 18,000 per year, a not insignificant amount for firms in poor countries.

[9] Arvis *et al.*, 2007 examine the large impact associated with uncertainty along the supply chain created by non harmonised regulations.

[10] The Tanzania certification and testing agency pesticides "… charges relatively high fees to register an agro-chemical and also requires three years of field testing. It does not recognize the testing done and registration of chemicals in neighbouring countries, including Kenya. Hence, there are a broad range of newer, more effective and safer chemicals which do not get registered in Tanzania because of the high cost and which are prevented from being legally imported from Kenya or other neighbouring countries. The chemical registration revenue imperative of TPRI thus appears to take precedence over a feasible solution of mutual recognition of other (including more rigorous) testing and registration systems."

[11] For a discussion, see Chapter 8 in De Wulf and Sokol (2005).

regional level because of the political economy and complexity of such arrangements (such as mutual recognition), which means that they are most probably better managed among a limited number of countries. Also, cost reduction measures will often involve some form of regional cooperation on the ground: for example, the creation of joint border posts enables neighbouring countries to share facilities, learn from each other and carry joint inspections, thus potentially reducing cost and time spent at the border.[12]

Economies of scale can also be realized on the administrative procedures and private services delivering trade facilitation. It is, however, unclear to what extent there is a scale barrier to efficient border administration, including modern practices such as single windows and risk management. The cost of collecting customs taxes in Rwanda is relatively low, amounting to 2.5 percent of receipts in 2005, with capital costs representing only a small fraction (2.6 percent) of these costs.[13] It is also unclear to what extent compliance with new security measures imposed by large developed countries pose a new challenge in that respect. Overall, there is good evidence that customs reform projects can be self-sustaining through increase in revenues brought by facilitation (Moïsé, 2005), suggesting that economies of scale are exhausted at the country level.[14] Arguably this relates to still relatively modest levels of reform, and in particular do not involve many elements of deep integration with trading partners. Although customs operations does not seem to be overly subject to important economies of scale in most cases, one can nevertheless argue that there are important costs associated with the surveillance of borders. A motivation for Norway, Sweden and Finland to sign cross border cooperation agreements (starting in 1960) was "division of labour"; that is, to share the cost of individually manning the 1,630 km-long border between Norway and Sweden, and the 739 km-long border between Norway and Finland.[15] Small administrations may not be able to afford all the material and infrastructure necessary. For instance, in the current WTO negotiations some members have called for "small vulnerable economies" to undertake a regional approach to the implementation of some expected WTO commitments that will require capacity building, and made a specific submission for regional trade facilitation enquiry points.[16]

[12] The benefits of joint border posts should however not be overstated. Practical implementation has proven problematic as the incentives for the border agency of each country to cooperate on joint inspection may not exist as where import and export controls remain very different as incentives to control them (the emphasis is generally on imports and their contribution to tax revenue).

[13] Source: Rwandan Customs, available at: <http://www.rra.gov.rw/en/about/performance.pdf>.

[14] In Mozambique, the investments made during the initial stages of the program were recouped within 14 months from additional revenue receipts. In Peru, increased revenue collection has helped solve many funding problems of the administration.

[15] See the communication by Norway to the WTO Trade Facilitation Negotiating Group on Border Agency Cooperation, TN/TF/W/48, 9 June 2005. In 1995 Norway calculated the savings associated with the two agreements: 10 new customs offices would have had to be opened on the Norwegian side of the border. One hundred new customs officers would have had to be employed. This would have cost about USD 8 million in additional investment costs and USD 8 million in recurring annual costs for the customs authorities for new buildings, salaries, etc. Economic operators would have incurred an estimated USD 39 million additional annual costs due to longer waiting time and double stops at the border.

[16] Communication from Barbados, Fiji, Papua New Guinea and the Solomon Islands to the WTO Negotiating Group on Trade Facilitation, 7 July 2006, document TN/TF/W/129.

Beyond customs operations, many developing countries and their markets are too small to offer the full range of standards conformity assessment, and thus benefit from regional integration (World Bank, 2005: p. 90). Setting up regional accreditation bodies, or opening regional markets for accreditation bodies, could be a way to provide cheaper and better testing, building on scale economies and comparative advantage. Scarcity of technical skills[17] is indeed another reason why regional approaches can make sense for countries facing serious shortages in these skills, which for modern trade facilitation techniques can become an issue.

Backbone services provide crucial inputs in trade transactions: finance and insurance, transport and logistics, handling, measurement and communication services. The delivery of these services for trade transactions can require a scale of production beyond the national borders.[18] Insurance and financial services (letters of credit, guarantees, insurance, etc.) constitute key input into the capacity to trade internationally: national operators in developing countries may not provide them or do so at non-competitive prices. According to EBRD (2003) national banking systems do not pool enough capital[19] to underwrite trade transactions. Financial guarantees for payments are often not available for small firms to allow them to export.[20] Similarly, fixed costs and geographic factors confer natural monopoly characteristics to some modes of transport (rail and maritime particularly). Ghana's Growth and Poverty Reduction Strategy (Ghana National Development Planning Commission, 2005) envisions regional cooperation for cross-border road infrastructure development. Regional transport hubs help realize economies of scale.[21] For freight transport, the emergence of multi-modal hubs (generally located near important existing infrastructure: air, sea or rail) generate important economies of scale (through higher utilization of infrastructure), and efficiency gains (through competition between modes of transport) compared to point-to-point routes (Müller-Jentsch, 2002). Transport hubs depend as much, and probably more, on the liberalization of regional transport services (such as liberalization of cabotage or air traffic rights) than the availability of infrastructure. Indeed, transport hubs tend to be geographically mobile, suggesting the secondary importance of infrastructure as a determinant of their location.

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[17] An essential piece of the architecture for the enforcement of technical regulations and SPS measures in international commercial exchanges is accreditation, which offers an internationally recognized guarantee that national processes of standards conformity assessment can be relied on. Holmes *et al.* (2006) offer a good overview of the question). In Sub-Saharan Africa there was until recently only one accredited expert, located in South Africa, able to grant this accreditation. Now three additional experts have been trained, still in South Africa. This confirms the view by ILAC-UNIDO (2003) that markets for accreditation and certification bodies in many developing countries may be too small.

[18] Arvis *et al.* (2007) for instance report how advanced logistics services are inhibited by lack of trade facilitation: it is often impossible, note the authors, to maintain multi-country inventories or to dodge first clearance and then re-export to the gateway country.

[19] Payment guarantee systems require less working capital than payments in advance (which are required when there is no guarantee) and thus help smaller agents to access international trade.

[20] This has prompted the EBRD and the IFC to create international risk sharing funds in order to provide small enterprise with access to trade finance. The risk sharing funds help international banks (confirming banks) cover the political and commercial risk faced by local issuing banks when they cover international trade transactions.

[21] For instance air transport hubs avoid having empty cargo on incoming or outgoing freight, a problem for small non-diversified economies.

Last, regional approaches to trade facilitation can also aim to create competition. First, among regional operators in the international trade transport and logistics chain; this will reduce the cost of trading and increase the availability of services to exporters and importers, thus contributing to trade creation. Arguably, better than regional competition is global competition. There are nevertheless arguments in favour of a regional approach. First, it does not have to be discriminatory. Also, as seen earlier, transport competition is increased by the establishment of regional hubs. The negotiation of bilateral liberalization agreement in air and maritime transport is more straightforward than multilaterally. Mattoo and Fink (2002) indeed find that more efficient bargaining may be possible in a plurilateral context than in the multilateral context for services: there is less concern that outsiders will be able to free-ride on the reciprocal exchange of concessions than if there were a general MFN obligation. Increased competition in trade related services is also largely dependent on some level of regulatory cooperation, which is generally more feasible and in many cases more desirable among a subset of countries than globally. Competition dimensions matter particularly in the context of transit corridors.

Coastal countries can be placed in a situation of monopoly for transit services: an example is the transport of oil products to Uganda by Kenya Pipeline Corporation, which in the absence of rail and road transport competitors can charge excessive prices (Uganda DTIS, 2006).[22] Competition among transit corridors is also desirable and regional agreements between more than two countries can create the conditions for the establishment of transit agreements competing against each other. The World Bank (2005) reports that unilateral or bilateral frameworks often govern transit agreements and such arrangements are not conducive to competition. Participants in "tour de role" and 50–50 sharing type agreements oppose regional agreements because they want to stave off competition.

Competitive pressures also hold for government agencies. By offering institutional mechanisms through which border agencies can exchange information and benchmark each other's performance, regional agreements offer more transparent regulatory competition that can foster more efficient border management. However, this is to be balanced with the other consideration that economies of scale and specialization justify one approach for the region.[23]

2.4. Regional negative and positive externalities

Regional agreements can serve as a policy coordination mechanism to help prevent individual countries from adopting national strategies that fall short of optimal global outcomes. For instance, countries of transit trade are often tempted to use trade restricting policies, such as seeking to set revenue maximizing fees on transit, imposing compulsory

[22] Until 1996 this monopoly was even reinforced by government regulation forbidding the transport of petroleum by road operators. This restriction is now lifted.

[23] The Tanzania DTIS (2005) raises this question about having regional accreditation organizations. In this case, the benefits of joint approach seem high enough to justify foregoing regulatory competition.

transit routes and check points, or mandatory securitized convoys. Fees and requirements will be above the cost of services provided (this includes the use of roads, provision of security, etc.) or strictly necessary for secure transit.[24] In the worst cases the motives behind these policies are protectionist; often, this is the outcome of non-consideration[25] of negative externalities imposed on neighbours. Such risk is particularly important when alternative transit routes are few, as often in Africa.[26] Domestic transport infrastructure constraints often have regional implications, justifying from an economic perspective port or regional airport hubs. Landlocked countries depend on the quality of their neighbours' infrastructure.[27]

A finding from the diagnostic on transport and trade facilitation in Uganda (Uganda DTIS, 2006) is that the most important transport and trade facilitation issues are outside the country's direct control. Tanzania and Kenya, its coastal neighbours, offer poor trade facilitation: the port of Mombasa, where 95 percent of Uganda's external trade traffic is handled is congested, transit bond regimes are financially burdensome, rail transit does not offer a competitive alternative to poor road transport and expensive pipeline transport.[28] As Schiff and Winters (2002) note, this type of externality is often asymmetric, with landlocked countries standing to gain a lot from better transit, when the gains for the coastal partner are much smaller (improved access to the internal market). In practice, landlocked countries have not gained much from participation in regional trade agreements, and this is likely because important trade obstacles have remained (Yang and Gupta, 2005).

Once again, standards and phytosanitary measures provide a further example of possible market failure. Weak or absent enforcement of SPS in one country can mean that negative consequences spill over to neighbours, as is the case with Tanzania, where highly contagious bovine diseases are not fully under control. In this context Tanzania has agreed with SADC neighbours to a five-year programme of vaccination, surveillance and control of animal movements (Tanzania DTIS, 2005).

As well as getting rid of negative externalities, creating positive externalities such as network effects may substantiate regional intervention. Transport, electronic and other information networks play an increasingly important role in trade facilitation reform. There are positive externalities for neighbouring countries to join existing networks

[24] McTiernan (2006), for instance, reports that Benin and Togo charge very high fees for transit, which causes transport from Lagos to Accra to be done by ship.

[25] Not merely oversight or neglect, but lack of incentives on the country of transit to internalise the costs of more efficient transit.

[26] A counter example is Bolivia, which has several access roads to the sea (Schiff and Winters, 2002).

[27] For instance poor road conditions and border crossing procedures between Kenya and Uganda at Malaba have made rail and water transport across Lake Victoria a competitive alternative; or because the route between Durban and Kampala is more reliable, some traders of high-value goods prefer it to much shorter routes to Dar Es Salaam or Mombasa (Caron and Reichert, 2001).

[28] Arvis *et al.* (2007) add that because of poor rail performance and unpredictability (Tanzania Railways Corporation has an error margin of four to five days predicting the arrival of any shipment), road transit from Kenya to Northern Tanzania has increased by 20 percent over the past five years. This also explains why 75 percent of Rwandan trade transits through Kenya while 50 percent transited through Tanzania only three years ago.

rather than develop their own systems or multiply bilateral channels of communication and information exchange. The European Union has developed several network initiatives around electronic transit systems (NCTS), satellite information (GALILEO), or Trans-European Networks on Transport. This concern is also reflected in trade action plans in developing countries, such as in the Uganda's recent DTIS which puts emphasis on the use of EDI interchange at the regional level, the development of a regional cargo tracking system, and the interconnection of East African Community's customs electronic systems (Uganda DTIS, 2006). The same issue of interconnection is noted in the case of Mozambique. Mozambique's proprietary customs electronic system is incompatible with Asycuda++, used by Mozambique's Southern African neighbours, and on which they intend to build their exchange of electronic information on transit cargo (Mozambique DTIS, 2004). Transport hubs, mentioned earlier, also create positive externalities, such as access to multi-modal transport platforms.

Box 1. How Regional Cooperation can Help: DTIS Recommendations About SPS for Tanzania

The 2005 Diagnostic Trade Integration Study conducted in Tanzania under the Integrated Framework finds that a regional approach and cooperation for SPS and quality standards can:

- increase trade through harmonization of standards and mutual recognition of conformity systems (avoiding *duplication*);
- spread knowledge and good practices (creating positive information *externalities*);
- manage more effectively trans-boundary risks (avoiding negative *externalities*);
- serve to realize *economies of scale* and scope in the delivery of conformity assessment;
- better enable regional enterprises to comply with extra-regional standards where collaboration facilitates international accreditation.

The DTIS recommendations prioritize the following areas of regional cooperation:

- Streamlining of regulations (simplification and improved transparency) and mutual recognition;
- Resource pooling ("centres of excellence" for the testing, registration or other monitoring of inputs or outputs for specific products such as pesticides, condoms or cosmetics);
- Multi-country collaboration for problem solving (surveillance and contingency planning, but also research, pilot programmes and training).

Source: Tanzania DTIS (2005: pp. 91-98) and author.

Positive externalities – beyond the mere realization of economies of scale described earlier – also arise from the provision of international finance and insurance. International provision of such services offers the possibility to mutualize risks across a region, and contribute to positive network effects, such as linking banks that usually do not do business with each other and diffusing skills through the network. The principle of mutualization is applicable for other trade related financial instruments specifically relevant to trade facilitation and transit such as guarantees for payment of taxes and insurance. COMESA introduced the Yellow Card or Third Party Regional Motor Vehicle Insurance scheme that allows traders to purchase insurance covering transport in the region (Arvis, 2005). The region also plans to set up a regional transit bond scheme. Regional guarantees (to secure the payment of duty and taxes) can address the failure of national organizations to set up such systems, because they often do not have the sufficient size, only have access to underdeveloped national financial services, and because international insurers are not willing to face the political and commercial risks of developing markets. In Uganda, the cost of customs bonds is estimated to add up to 4 percent to import and export costs and a recommendation of the integrated framework diagnostic study is to use a regional approach to reduce their incidence (Uganda DTIS, 2006). Arvis (2005) argues that the lack of a regional customs guarantee explains why transit initiatives to replicate the success of the European TIR system have failed so far.

We conclude this section by noting that there is a risk for regional initiatives to create their own negative externalities. This, for instance, can occur when countries take part in RTAs with policies going against trade facilitation objectives. The obvious example is the need for rules of origin in the absence of a common external trade regime, which represent specific difficulties for customs enforcement (World Bank, 2005: p. 68). Another problem can be created by the incentives to harmonize RTA members' practices, ending up in adopting higher standards than strictly necessary.[29] Third, there is also the risk of incoherence with trade facilitation objectives of the policies agreed when signing the RTA: when adopting the East African Community common external tariff, Uganda had to raise its tariff on vehicles from 9 percent to 25 percent (customs duty and import commission), which increases the cost of transport in Uganda (Uganda DTIS, 2006). Finally, regional trade facilitation should not result in trade diversion effects. There are two ways in which this can happen. The most serious one is when trade facilitation measures have their own discriminatory effect. For most trade facilitation measures this is not the case, but it is nevertheless a possibility for several important policies, such as mutual recognition and transport infrastructure policies, in the latter case if the improvement of one mode of transport (road for instance) is privileged over others. More benignly, in a second best world, trade facilitation may simply augment existing distortions if these are left untouched.

[29] This is a question that is difficult to assess in practice, but if one takes the example of regional trade agreements signed by the European Union, they make clear reference to harmonization to European standards (see Maur, 2005). Otsuki, Wilson and Sewadeh (2001) give an example of how European SPS measures can be particularly burdensome.

3. Which Platform to Deliver Regional Trade Facilitation?

3.1. A public good perspective

The benefits from regional trade facilitation display public or quasi-public goods properties. Public goods indeed vary in their degree of "publicness" (Sandler, 2006) and thus display different properties. One reason why it is important to understand these properties is because this has a bearing on understanding better how the benefits from regional trade facilitation reform ought to be delivered.[30]

A public good gives rise to two distinct market failures. The first failure arises because of non-excludability: providers of the good cannot prevent others from free-riding by consuming it at no cost. The second failure is caused by non-rivalry: the consumption of one unit of the good does not diminish the quantity available for consumption to others, meaning that once a public good is provided, all can enjoy it at no or very low cost.

A quick examination then tells us that most of the benefits provided by regional trade facilitation are not pure public goods. They are indeed almost all characterized by near total excludability. This is clearly the case for transit corridors, transport infrastructure, financial and communication infrastructure, networks, authorized traders regimes, and collocation of customs services. The only dimension of trade facilitation that seems to be a pure regional public good relates to communicable diseases. For the other dimensions the full exclusion characteristic has actually positive implications. Excludability indeed means that fees can be charged to finance their supply. It seems also that once provided, trade facilitation goods are mostly non-rival in nature: new and improved procedures or systems can be enjoyed by all at little or no marginal cost (although in some specific cases, discrimination might still have to be borne in mind). In essence regional trade facilitation is mostly a "club good".

Second, depending on the type of public good, the capacity of countries, individually or as a group, to affect the supply of the public good varies: what in the literature is called aggregation technology (Hirschleifer, 1983). In the case of trade facilitation, the specific difficulties for the delivery of regional trade facilitation goods are quite varied. In the first instance, a regional good could in theory be provided by any country within a region, and thus it is desirable for countries to coordinate over this, otherwise one risks having too much of one good. Airports and ports hubs, and cost duplication elimination are two cases where coordination is optimal.[31] A second, different example is the integrity of a customs union, which depends on the customs enforcement capacity

[30] The growing literature on regional public goods offers a general discussion of this. See Sandler (1998; 2006); Estevadeordal, Franz and Nguyen (2004); Cook and Sachs (1999); Ferroni (2002); Arce and Sandler (2002); Kaul *et al.* (2003), and Kanbur *et al.* (1999). Stålgren (2000) offers a review of the literature. See, also, Rufin (2004) on transport and communication infrastructure, and Holmes *et al.* (2006) on standards.

[31] "Best shot" and "better shot" categories in Kanbur *et al.* (1999) typology.

of the weakest member (discussed below).[32] In this case, the failure is linked to lack of capacity. Incentives are big for customs union members to provide the weakest link with the technology to enforce customs disciplines at the higher standard. Third case in hand: networks, but also many other aspects of regional trade facilitation, are affected by the sum of efforts of the countries participating.[33]

In all these cases, the contribution of each country to the supply of regional trade facilitation is to some extent substitutable for the contribution of others and thus creates free-riding incentives. These have to be addressed if undersupply is to be avoided, and requires some form of institution building (Arce and Sandler, 2002). However, the type of aggregation technology matters as contributions to the total effort are not necessarily equally distributed, which alters the free-riding incentives of each country. An implication is that despite having in common the need for regional intervention, various components of trade facilitation reform cannot be delivered using similar approaches. An important remark in this respect is that the role of individual countries belonging to a region will vary depending on the type of regional public good that needs to be delivered.

3.2. The nature of regional initiatives

The regional dimension of the various aspects of trade facilitation reform suggests that regional initiatives are in a unique position to help tackle trade facilitation issues (World Bank, 2004, 2005). There are numerous institutional public and private arrangements that have the ability to deliver these regional goods. The most common are regional trade integration agreements and regional cooperation agreements. But other arrangements can also supply regional public goods, such as public-private partnerships (in several transit corridors), regional development institutions, or NGOs (Sandler, 2006). The focus here is primarily on regional trade agreements, which for reasons discussed below, but also more generally in the literature (Devlin and Estevadeordal, 2004), appear to offer the greatest potential for efficient delivery. Because trade facilitation involves a wide range of regulatory activities, it makes sense to concentrate on institutions that are largely public, such as regional cooperation agreements, when we discuss alternatives to regional trade integration.

It is a fact that regional trade agreements (except for customs unions) have not included much in the way of trade facilitation efforts (Moïsé, 2002), at least until recently; Bin (2008) note that the number of agreements covering trade facilitation in Asia and the Pacific has risen significantly in recent years and that 34 out of 102 signed RTAs now include some trade facilitation provisions. The institutional setting of regional agreements seems well suited to conduct a trade facilitation reform agenda. Trade facilitation indeed

[32] "Weakest link" and "weaker link" categories (Kanbur *et al.*, 1999).

[33] This is to build the network. Note, however, that the integrity of the network is affected by the contribution of its weakest link.

requires not only the elimination of distortionary and inefficient rules and practices, but above all an ambitious and positive agenda of reform by implementing internationally compatible modern legislation, systems and skills. In essence, trade facilitation is about deep integration.

3.3. How RTAs can facilitate trade facilitation

The World Bank (2005) lists several areas of facilitation for which it views RTAs as a potential vector of reform: alignment of customs codes with international standards; simplification and harmonization of procedures (e-documents and single document); alignment of tariff structures with the HS; transparency; effective implementation of the WTO valuation agreement; joint work towards customs integrity; establishment of joint border posts; and joint training centres. A regional approach to some of the items in this list (alignment with international standards, transparency) does not obviously stem from the economic advantages discussed above, implying that there is not necessarily a direct correspondence between the economic optimal level of intervention and the jurisdictional one: the subsidiarity question. The interest of taking such reforms forward in regional agreements is thus not only because of pure economic reasons, but also that regional trade agreements offer specific advantages over other forms of international agreements (multilateral or other regional forms of cooperation) and unilateral initiatives.

We examine the following characteristics of RTAs: (i) a forum to exchange concessions across a broad array of sectors; (ii) a mode of access to mechanisms of cooperation, including in some instances financial transfers and capacity building; (iii) a mechanism for political commitment; and (iv) a more efficient approach to harmonization and implementation.

3.4. RTAs as a forum of issues

First, deep RTAs offer the possibility of comprehensive trade facilitation, involving reform in several sectors of the economy that can be incorporated in the new generations of RTAs. Deep integration agreements present the opportunity to include sectors that are not well covered multilaterally, while also providing efficient enforcement mechanisms (see below). The wider remit of RTAs compared to multilateral approaches is reflected in initiatives such as APEC, which uses of a broader definition of trade facilitation reform compared to the relatively narrow approach taken in the WTO (Wilson *et al.*, 2002). By incorporating policies for which there is no actual or possible prospect of multilateral liberalization, some regional agreements offer increased scope for meaningful trade facilitation reform. A good illustration of this is the adoption of flexible and harmonized policies on visas and the opening of services, dimensions usually out of reach of a multilateral agreement, but which can be part of regional discussions; ECOWAS, for instance, suppressed visas between member countries. The political economy of RTAs makes it easier to deal with migration issues because countries can exchange commitments on natural persons movements (whereas this is not possible in GATS).[34]

By tackling many dimensions of trade facilitation at the same time, regional trade agreements also give scope for exploiting natural complementarities between the different elements of trade facilitation reform.[35] A particular challenge of reform is to get all the agencies involved in border control to work to a common objective of facilitating trade. This is often not happening. Having the policy areas implemented by these agencies (such as SPS and standards) covered in the same trade agreement offers scope for agreeing to common aims linking these policies. In theory the WTO could offer similar advantages, but there the multiplicity of diverging country interests behind each issue makes any attempt at defining a coherent approach difficult and reduced to the common high level principles of non-discrimination, transparency or due process. This is still a far cry from delivering coherent implementation of these policies.

Conceivably all the facets of trade facilitation reform could equally be included in either RTAs or specifically designed cooperation agreements. However, RTAs generally offer scope for a wide spectrum of policies across which various concessions could be traded-off (Devlin and Estevadeordal, 2004), including non-economic dimensions.[36] Besides, because their scope, regional trade agreements can also guarantee better commitment. In theory any attempt to deny a trade facilitation concession by the imposition of other trade barriers (e.g., tariffs) should be more complicated, as these are part of the agreement. By the same token, enforcement of trade facilitation measures will be guaranteed by the possibility for partners to withdraw any other concession. Obviously there are many limits to this happening in practice, starting with the fact that despite being broad in scope, many existing regional agreements are more shallow than deep, thus still offering quite a lot of opportunity to members to escape enforcement.

3.5. Redistribution

Regional trade agreements are not infrequently complemented by sharing of resources and redistribution mechanisms among partner countries, including the supply of financial and technical assistance. Trade facilitation reforms can be demanding, both in expertise and material.[37] Regional efforts offer in addition the possibility of benchmarking

[34] Although this is only likely when partner countries have similar levels of development and patterns of comparative advantage that make movement of natural persons relatively balanced. Bin and Misovicova (2007) find that provisions on mobility of businesspersons are present in about one third of RTAs containing trade facilitation provisions in Asia and the Pacific.

[35] For instance, regional guarantee systems help establish global standards for documentary credity (EBRD, 2003) and thus generate information that can be used for other purposes.

[36] At the same time this increases the complexity of negotiating across a wide range of issues.

[37] This question is the subject of some debate: it is argued that developing countries are actually more advanced than commonly thought and that a large share of essential trade facilitation measures would not be that costly and that the main hurdle is political. This is, for instance, the conclusion reached by McLindern (2006), arguably in the narrow context of WTO negotiations. However, there is also evidence that ambitious customs reform (often as part of revenue reform) mobilises very significant donor support over several years as in the instance of South Eastern Europe.

(e.g., the regional programme for trade and transport facilitation in South-eastern Europe: De Wulf and Sokol, 2005: p. 137) and the sharing of good practice. Several regional agreements have a programme of regional capacity building. This is the case of APEC and COMESA.

The European Union devotes rather considerable sums and efforts to assisting neighbour countries with which it signs association agreements (OECD, 2005). APEC has developed a programme of technical assistance for which members have drawn both a collective and individual Country Assistance Plans covering 16 areas.[38] Regional capacity building also takes place in South-South regional agreements such as COMESA. The South African Revenue Service provides direct technical assistance to regional trade partners.[39] In particular, as discussed earlier, when the provision of better trade facilitation at the regional level is impaired by the lack of capacity of a few members, with implications as a whole for a regional system, regional groupings can assist the delivery of joint assistance (acting as a coordination mechanism and sharing the costs among members).

Even in the absence of redistribution arrangements, RTAs potentially create beneficial access to external financial resources as they may increase the credibility and ability of the regional group to offer loan collateral for instance (Devlin and Estevadeordal, 2004). Regional guarantee systems would benefit from this.

3.6. Trust and institutions

It is also well known that regional trade agreements act as trust building mechanisms, favouring interactions between officials and exchange of information (Schiff and Winters, 1998). Trust is a vital aspect of trade facilitation cooperation, as it helps mitigate risk (and thus reduce physical constraints on the transport of goods such as inspections or requirements to abide to certain requirements such as compulsory routes) through increased confidence in shared information and systems. While regional trade agreements have a good track record in enabling trust building across partner countries' administrations, attempts to involve businesses, for instance through public-private partnerships, have been much less successful: for instance the European Union has tried to build ambitious public-private partnerships in the context of its European transport network policy, with mixed success.[40]

In the context of regional trade agreements, customs cooperation committees are often established to discuss enforcement issues and also help to diffuse disputes (World

[38] APEC Sub-Committee on Customs Procedures (2006). CAP Assessment/Evaluation Matrix. September 2006; available at: <http://www.sccp.org/sccplibrary/Meas_Eval/capeval_0206.htm>.

[39] SARS (2007) reports assistance to other African administrations in building capacity in the form of: "providing policy, legal and operational assistance; Hosting study visits to share best practices with other administrations; Providing training interventions either at the SARS Academy or in other countries; and seconding SARS officials to other administrations and hosting officials seconded by other administrations."

[40] Another way to create ownership with businesses is by giving them access to dispute settlement under the RTA, as NAFTA and CAFTA do for investment. Similar solutions could be envisaged in relation to trade facilitation, offering the possibility for the private sector to challenge governments that illegitimately restrict their business.

Bank, 2005: p. 89). More informal expert groups have also been established in a regional integration context, such as the EU Florence process on infrastructure, which has been influential for promoting reform (Rufin, 2004). Also, through harmonization of instruments and increased transparency, it becomes easier to understand what trade partners are up to. The establishment of trust is central in achieving devolution of responsibilities to partner countries (such as in mutual recognition and regional guarantee schemes) but also in establishing shared facilities. Trust not only matters at the technical level, but of course also at the political one. An illustration of the link between trade facilitation and international trust, albeit not in the context of an RTA is given by the recent decision by India and China to reopen trade through the Himalayan pass of Nathu-La, after four decades of military tension.[41] The trust dimension takes an added importance with enhanced concerns about security after the terrorist attacks of 11 September in the United States. Better security involves better border control, which can benefit from regional cooperation.

Regional trade integration implies the building of regional institutions that can take forward some policies on behalf of its members. The RTAs offer a cost-saving institutional architecture (Devlin and Estevadeordal, 2004; Sandler, 2006) through which the demand for regional public goods can be more easily aggregated. The redistribution mechanisms discussed above, and the cooperation mechanisms established through a RTA, both contribute to cooperation (limiting free-riding in particular) and capacity, all central criteria for the delivery of public goods. It is also often thought that regional institutions are better placed to carry forward international harmonization agendas (World Bank, 2005; Consilium Legis, 2003 also make this argument in the case of transit corridors). Regional representation can also be a way to increase the bargaining power of its constituents in international negotiating forums such as standard-setting organizations (an example of this is discussed in EC (2001) in relation to air and maritime transport standards). Finally, as discussed above, pooling scarce resources can mean that regional institutions become more efficient.

3.7. Incentives for regional reform: are RTAs natural complements of trade facilitation?

RTAs require more sophisticated trade facilitation measures. Administration of border formalities becomes more complex because of the need to discriminate between preferential and non-preferential trade (De Wulf and Sokol, 2005). It takes more time to process goods covered by regional agreements (Roy and Bagai, 2005). Thus, while making trade more complex, regional agreements have created new trade facilitation needs with the enforcement of preferential rules of origin. All this probably explains why most RTAs, tend to focus on questions of origin (Moïsé, 2002) and their enforcement. Similarly, customs valuation enforcement becomes more important as an element of determination of preferences.

[41] See <http://news.bbc.co.uk/1/hi/world/south_asia/5093712.stm> and <http://economictimes.indiatimes.com/articleshow/1661459.cms>.

Other dimensions included in such RTAs aim at simplifying the job of the customs authorities when dealing with goods under preferential access. This includes transparency requirements with frequent reference to GATT Article X (Moïsé, 2002), the adoption of documentation standards (such as the Single Administrative Document in the EU) to facilitate access to information and cooperation between customs authorities for fact finding. Harmonization is not much on the agenda, except for better mutual understanding of day-to-day operations.

On the other hand there are regional initiatives where customs and border issues are taken further. Europe views customs (and probably border processes in general) as an important tool in favouring regional integration and promotion of preferential links (EC, 2003). The objective of maximizing the trade creation effects of regional agreements, raises the salience of other aspects of regional cooperation (World Bank, 2005: p. 92) such as trade facilitation. We must, however, add that trade diversion may as well diminish the relative importance of trade with the excluded parties to the regional agreement. It is indicative that the trade facilitation policies of Europe have been largely inward looking until most recently. This is not so much an issue when the trade volume complementarity operates with trade facilitation policies that are not discriminatory in essence (such as international harmonization). However it could become a problem where policies of cooperation and mutual recognition or adoption of standards exclude certain categories of traders.

Secondly, when RTAs involve two geographically contiguos partners, the question of transit management is raised. If three countries grant each other preferential access, goods exchanged between any two members must be able to transit through the third one without added charges and impediments to trade that undo the preferential treatment. Thus regional trade agreements provide a strong incentive to implement transit agreements, either within the RTA itself or in parallel. As discussed in section 4.1 below, despite abundance of provisions on transit, implementation remains an issue.

The third facilitation-related element historically prominent in RTAs deals with rules on technical standards and phytosanitary requirements. On some occasions, such as within the European Union and the Mercosur, an ambitious regulatory agenda has been pursued. However, in most cases standards provisions have been much more modest, including RTAs among advanced economies. In the case of the European Union, beyond the upward harmonization for the internal market, the most ambitious attempts regarding standards have been through standalone mutual recognition agreements (such as the one with the USA) and are limited to conformity assessment. One lesson that seems to emerge from regional cooperation on standards is that its nature depends on the specific capacity of the trade partners, such as preparedness to perform conformity assessments, and the institutional setting of the agreement. Depending on how strong institutions are, more or less active harmonization or recognition routes can be followed (World Bank, 2005: p. 88).

The recent generation of regional trade agreements seems nevertheless increasingly to incorporate additional trade facilitation content. Evidence of this is reported for regional agreements in Asia that include provisions covering transparency of laws and rulings, use of ICT and e-commerce, freedom of transit, mobility of business people, facilitation of transport and logistics, and facilitation of payment and trade finance (Bin 2008).

Thus the complementarity between RTAs (and what is often their first main objective, the reduction of tariffs and quotas) and trade facilitation reform create an incentive to bring trade facilitation cooperation under the umbrella of an RTA rather than in a standalone agreement. As noted by Devlin and Estevadeordal (2004), this complementarity is likely to increase with commercial integration, thus expanding the scope of trade facilitation intervention in the context of RTAs. This aspect is highlighted by the case of customs unions.

3.8. The special case of customs unions

Arndt *et al.* (2007) suggest that a benefit of opting for a customs union model over a simple free trade agreement could be to register more progress on "deep integration" issues such as trade facilitation or liberalization of services. We find that this is most likely to be indeed the case for trade facilitation.

The preservation of tax revenues is very much at the forefront of customs and other trade facilitation-related concerns in regional trade agreements. This is a notable difference between cooperation agreements (which are not necessarily signed in the context of tariff reductions) and RTAs. For developing countries and, even more the least developed countries, trade taxes are a big share of all government revenue (Keen and Simone, 2004). This is why emphasis has most often been only on the few aspects of customs that secure trade tax revenues while allowing preferential trade.

The incentives related to optimizing revenue collection are modified in a customs union, which we first define broadly as a regional trade agreement with a common external tariff and no tariffs among its members.[42] In a "true" customs union, revenues will be collected at the initial port of entry in the customs union, that is revenue collected by each member on behalf of the union and subsequently either redistributed or spent by common institutions. This substantive difference between customs unions and other regional trade agreements has important consequences for the scope of trade facilitation reform at the regional level.

First, customs unions do not require the implementation of rules of origin among members.[43] They also either eliminate or diminish the need for transit bond regimes for goods destined to markets within the union. Both are significant facilitations of trade. Further, forming a customs union implies further incentives for trade facilitation reform in member countries to harmonize their regime, starting with adopting common customs legislations, classification, and tariff rates.

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[42] The World Customs Organization (1995) defines a customs union as the union of two or more customs territories sharing a common tariff, where customs duties and restrictive regulations of commerce have been abolished within the customs union.

[43] At least for "true" customs unions that collect revenue at entry.

Like in any other preferential trade arrangement there are incentives for trade deflection in customs unions, to take advantage of borders in the region where protection is the lowest. Because tariffs are uniform, the cause of trade deflection is solely due to non-tariff barriers, therefore putting a specific emphasis on them. Among them, lack of trade facilitation in one partner provides incentives for private operators to concentrate their trading operations in the most efficient member of the union: "port shopping" is what happened in Europe (EC, 2003). Another characteristic of customs unions is that there is no possibility to change unilaterally the external tariff applied to third countries, so as to eventually compensate tariff revenue losses caused by trade deflection. Such revenue losses are one of the chief motives for governments to take action.[44] Additionally when revenue is collected by individual members on behalf of the Union, and then shared under some revenue-sharing agreement (as it is in SACU) implies that there is mutual confidence in the enforcement capacity of other union members: trade facilitation measures and upgrading of union members' border management is an element of confidence building.

Therefore, in order to preserve the integrity of a union, members have a strong incentive to take a joint approach to issues and build capacity at the weakest points of entry of the customs territory.[45] These "race to the top" incentives can promote facilitation reform in some members. This also means that the prognosis for the provision of weakest link-type public goods is increased in customs unions, which is confirmed by their generally more ambitious trade facilitation undertakings.[46] Members of the COMESA have for example adopted several regional trade facilitation initiatives, including a single document for customs, and are in the process of establishing a regional bond system (see Box 2 for further examples in COMESA).

Deeper integration within the customs union adds to incentives for trade facilitation. In the context of more integrated markets such as the EU single market, the removal of internal borders has meant not only a transfer of sovereignty for tariff revenue collection to the Union, but also of all other border controls, and thus a transfer of authority at the European Commission level, as well as further incentives to build the capacity of the weakest members in the absence of national border controls for goods transiting through other members of the Single European Market (EC, 1989).

The incentive is rather one of harmonization and enforcement than facilitation of trade in the strict sense. In this context there is a clear distinction between trade among members and trade with third countries. While intra-union trade is most likely to see more benefits from the removal of controls, the harmonization of regulatory requirements, and mutual cooperation, effects are likely to be much more ambiguous

[44] Ineffective protection of the domestic industry is the other reason why regional agreement members want to avoid trade deflection. One can, however, assume that governments will be looking after their direct interests (tax collection) very closely in any case.

[45] See Keen (2003).

[46] According to Arce and Sandler, regional institutions are already well placed to provide weakest link-type public goods compared to global institutions because being closer to the problem they can identify more easily the "laggards". As the weakest link problem is one of capacity, the idea seems here that for implementation purposes, regional institutions will be more efficient.

with countries outside the Union. Border reform under a customs union is only synonymous with genuine trade facilitation to the extent that it makes trade easier among customs union partners and with external partners. It is true that the adoption of a unique rule within the union creates immediate benefits to third countries, such as: an automatic reduction of duplication costs for transiters and trading partners dealing with more than one union member, and access to a broader market once the fixed costs associated to border control (such as accessing information about customs procedures) are paid. However, there is a distinct risk that the process of cooperation among union members in implementation of their procedures (such as MRAs) would give their economic agents an added competitive edge against traders outside the union without access to these facilitation tools. Another risk of discrimination is the adoption of higher standards and stricter procedures by union members on trade from third parties, leading, for instance, to standards harmonization and added controls at the border to guarantee integrity on behalf of other union members.

Box 2. COMESA's Regional Initiatives on Trade Facilitation

The Common Eastern Market for Eastern and Southern African States (COMESA) was formed in 1981 and the COMESA free trade area launched in October 2000. The 20 member countries of COMESA now plan to launch the COMESA Customs Union in December 2008.

Trade facilitation has been an important aspect of regional integration in COMESA. The following trade facilitation measures have been developed (not necessarily in all member states):

- Common tariff nomenclature
- Common valuation system
- Protocol on rules of origin
- COMESA single customs declaration document (COMESA-CD)
- Protocol on transit and trade facilitation introducing licensing of transit carriers and harmonization of axle load controls
- Regional customs bonds guarantee scheme launched in 2006 to enable the payment of a single bond for the region
- Licensing of clearing agents and formation of a regional Freight Forwarder Association
- Protocol of third party motor vehicle insurance scheme (Yellow Card scheme, in which 13 countries participate)
- Joint border controls (Chirundu port for Zambia–Zimbabwe; Malada border for Uganda–Kenya)
- Implementation of common standards
- Capacity building with development of customs training modules

Source: COMESA (2005).

One should also note that most customs unions do not follow the model of collection of revenues at the port of entry, but rather according to the final point of consumption. Arndt *et al.* (2007) survey nine customs unions and find that only the EU and SACU collect revenue at entry. This means for the other customs unions the use of complex bond procedures to ensure that goods entering the customs union are indeed taxed at their point of destination, as well as possibly rules of origin.[47] Trust and more developed institutions are also much less a feature of such arrangements, as are incentives to cooperate to upward harmonization.

4. Trade Facilitation Reform Through RTAs: A Suitable Option?

Bergsten (1997), referring to APEC, lists trade facilitation as one of the five possible definitions of "open regionalism". Trade facilitation measures are indeed rarely preferential in nature, except when they provide lower customs fees, simplified origin marking requirements and mutual recognition agreements of conformity (Moïsé, 2002). Other reforms undertaken in the name of trade facilitation in RTAs are *de jure* non-discriminatory and thus their benefit should also extend to non-RTA trade partners (Schiff and Winters, 2003; Maur, 2005). The possibility however remains that through the adoption of specific standards, an artificial advantage is granted to parties better acquainted than others with such standards (a hidden motive behind upward harmonization claims promoted by developed countries). This is an issue for technical barriers and phytosanitary standards, although probably less for harmonization of customs procedures, essentially modelled on internationally agreed standards (Moïsé, 2002). Nevertheless, implementation issues and necessary cooperation, including mutual recognition of practices raise the spectrum of discrimination against countries outside the regional trade agreements.

4.1. What channel for regional trade facilitation? RTAs and cooperation agreements

As noted by Arvis *et al.* (2007) the lack of reform is not due to lack of legal instruments. Regional dimensions of trade facilitation can be addressed through sector-specific bilateral or plurilateral cooperation agreements rather than cross-sectoral RTAs (thus confirming the view that RTAs are not a technical necessity per se, cf. Hoekman and Kostecki, 2000). Regional transit agreements are an example of such cooperation agreements.[48] Transit arrangements between countries are numerous. Taking the case of Africa, N'Guessan (2003) points out that transit systems are particularly deficient. Only 30 percent of the regional transit in WAEMU is conducted under the regional transit agreements, the

[47] I thank Matthew Stern for drawing my attention to this fact. For instance in the EAC, a transitory regime will ensure that collection of taxes is first made at the final port of destination, as opposed to the port of arrival (Uganda DTIS, 2006).

[48] There are several other examples of (generally bilateral) sector-specific agreements to facilitate trade: customs cooperation agreements and mutual recognition agreements, for instance.

remaining 70 percent being subject to bilateral rules. Regional corridor agreements in Sub-Saharan African are largely not operational for most of the transit traffic, and are superseded by national, non-harmonized, overlapping and discriminatory provisions such as: compulsory customs escort, non-harmonized transit charges, or specific country documentation for transit. Administrative burden adds to the regulatory burden, with lack of coordination between different agencies in charge of controlling transit goods (customs, police, sanitary controls). The inefficiency of these agencies multiplies the costs. The conclusion thus seems that neither bilateral sectoral agreements nor regional agreements in the context of regional integration have delivered trade facilitation benefits in Africa.

One reason why bilateral transit cooperation agreements have not delivered could be the absence of incentives for countries to internalize regional externalities: the asymmetry of incentives for landlocked and border countries noted by Schiff and Winters (2002). However, and more importantly, the lack of political commitment of individual countries behind market-based reforms probably remains the biggest impediment. An example is absence of liberalization in the transport sector, thus denying the benefits of better transport links and corridors. Poor procedures in individual countries of transit, linked to weak political incentives to reform, remain often the main obstacle to an efficient regional transit regime. An interesting case in hand is Djibouti, which has made important port infrastructure investments to increase its capacity to serve neighbouring countries from its hinterland. To date, the capacity of the port terminals remains in some instances largely underutilized. The reason is not lack of demand: the Djiboutian port authority has had to increase its dry port capacity to store increasing amounts of cargo laying in waiting. Slow border clearance from neighbouring Ethiopian authorities is the explanation. Cargo ships have to stay longer than necessary, preventing full utilization of the terminals. Slow clearance from Ethiopian authorities creates a negative externality on port activities in Djibouti, probably an important source of revenue for its small economy. This incidentally demonstrates that the policies of landlocked countries can also impact negatively on coastal neighbours.

The political commitment problem can be better addressed in the broader setting of RTAs, than in other regional institutional settings. The anchoring of reform can be stronger, and the cost of non-implementation of one obligation can jeopardize the agreement as a whole, and thus is much higher. Dispute settlement measures tend to be stronger in regional trade agreement than in sectoral agreements Aldaz-Carroll (2006) finds that dispute panels in cooperation agreements only tend to have a mediation role, whereas in RTAs they have a stronger arbitration role. This could explain why the alternative to incorporating transit processes into or in parallel with regional agreement seems to have gained credence in the past decade, when several agreements have been signed with provisions on regional transit.[49] Indeed, many regional agreements have incorporated rules and developed instruments to facilitate transit, such as the EAC, COMESA or SADC. Yet, actual transit facilitation has been disappointing mainly because of poor implementation

[49] Most regional trade agreements incorporate transport and trade facilitation agreements (World Bank, 2005).

(Arvis, 2005; quoting UNCTAD, 2001). With the exception of the European TRIE agreement (Transit Routier Inter Etats), most fail to address implementation problems and have confined themselves to broad policy recommendations.

The poor record on transit illustrates the more general failure of most regional institutions to deliver tangible trade facilitation reform (the EU and, to a lesser extent, the APEC being among the exceptions). In Africa, McTiernan (2006) reports that only COMESA and the trans-Kalahari corridor (an ad hoc transit cooperation agreement) have provoked changes in customs practice.[50] Interestingly, COMESA, the EU and APEC are three non-traditional cases compared to other RTAs. The poor performance of RTAs may seem unexpected: since RTAs have clearly not tried to take a rule-setting role (left to international organizations)[51] they could have been expected to take a more active role in implementation. Moreover, that RTAs have kept clear of the trade facilitation standard setting agenda is a good thing as it guarantees MFN treatment: the modern standards adopted are accessible to all. Because they are defined internationally, and thus one can presume that domestic interests are not influencing their design, international standards should also guarantee national treatment.

The fact that RTAs have not delivered reform in practice therefore requires further examinations. A first remark is that the role of binding rules for implementation is perhaps overstated. Finger (2006) reminds us that there is not necessary a need for legal obligation to spark trade facilitation reform, as many countries have already shown willingness to do so. One may, however, wonder whether the willingness to undertake regional initiatives is the same. APEC has no enforcement mechanism and commitments are entirely voluntary. APEC has emphasized its focus on policy integration and common principles of reform, while organizing the delivery of technical assistance.

A second observation relates, as discussed earlier, to the revenue preservation incentives in regional integration. Policies in the transit country are likely to be motivated by tax revenue preservation and, since revenue collection is often not perceived as complementary to trade facilitation, a plethora of controls will be the preferred option. Weak regional institutions also mean that implementation does not necessarily follow transit agreements that have been negotiated. On the contrary, in a true customs union, where revenues are collected on behalf of the union, transiting countries have some incentives this time to facilitate transit trade for countries that collect part of their revenue.

Another difference with customs unions is often the strength of the latter's institutions, which allows them to carry out more ambitious reforms. Looking at the examples of the EU and COMESA it is certainly the case that bold regional facilitation initiatives have been tabled, such as the regional bond scheme in COMESA, implemented in 2006; numerous policies in Europe such as transnational information and transport networks; or standards harmonization. Whether such policies have resulted in effective facilitation

[50] Although the trans-Kalahari corridor progress have been hampered by a unilateral decision by Botswana to increase road user fees, which resulted in a decrease of traffic (World Bank, 2005).

[51] The World Customs Organization's Kyoto Convention for Customs, the International Civil Aviation Authority (ICAO), the International Road Transport Union (IRU), the International Maritime Organization (IMO), etc.

of trade is a question that is difficult to answer. While many of these initiatives seem desirable, their implementation remains largely unstudied and so is their impact. Besides, there is also some evidence that these policies have been more complex to implement that initially thought (e.g. transit in COMESA), and that, in the case of the European Union, many of the higher international standards remain to be implemented.

A last remark is the presence of large advanced countries as a driving force (both political and material) behind reform: APEC (Japan, Australia), SADC (South Africa), and, of course, European countries. As Schiff and Winters (2003) argue, trade facilitation as a dimension of policy integration requires much more than non-discrimination. It needs the rapprochement of policies and enforcement; it also needs effective implementation. Making policies more compatible undoubtedly involves strong political will to fight against the vested interests in border agencies.[52] It also requires a different institutional setting than the classical exchange of trade concessions. In short, stronger and more permanent institutions than those of multilateral trade negotiations are needed because implementation of trade facilitation reforms will require at least coordination, and more likely, as discussed, harmonization and mutual recognition of rulings. Regional cooperation agreements and RTAs seem more likely to deliver institutions that will foster integration, mostly because transaction costs are smaller among a few countries than multilaterally (and in general for the delivery of public goods: Devlin and Estevadeordal, 2004; Sandler, 2006); in particular regional agreements seem to offer the flexibility needed for the design of such institutions and for informal cooperation. The RTAs further offer, compared to sector-specific trade facilitation agreements, the benefit of stronger political commitment and linkages with several policies facilitating trade. Finally, RTAs offer enforceability and resources for implementation. Enforceability of reform commitment does not seem to be such an issue in the case of trade facilitation, as shown by the example of voluntary commitments in APEC.[53] Implementation of reform, on the other hand, seems a major challenge for most countries, including richer countries. Availability of funds, time and expertise is required for the most ambitious reforms. Again, RTAs including advanced countries seem well suited to capacity-building needs, provided they offer the right mix of financial assistance and expertise.

4.2. The complementarity of regional solutions with multilateral and national solutions

Regional solutions to trade facilitation should not always be thought as a substitute to multilateral, national or other regional interventions, but also as a complement. Transit corridors will probably gain from the involvement of regional trade agreements on top

[52] This is, for instance, a clear finding from a recent study on the needs, priorities and costs for the implementation of a future WTO trade facilitation agreement (McLinden, 2006).

[53] Another enforcement issue is between government and private operators: the need to have fair and consistent enforcement of rules, and the right to appeal procedures for traders.

of corridor specific institutions, such as regional management committees, and more national arrangements (Consilium Legis, 2003).

It is also a fact that, in order to become operational, regional cooperation has to rest on international rules and institutions. This is due to the need for guarantees extending beyond the regional level. We gave earlier the example of accreditation, which needs to be guaranteed internationally by one of two global organizations: the International Accreditation Forum and the International Laboratory Accreditation Organization (Holmes *et al.*, 2006). Likewise, the integrity of the TIR system is guaranteed by the UN Economic Commission for Europe and the International Road Transport Union (Arvis *et al.*, 2007).

Another dimension of the complementarity of regional integration agreements and donor organizations is illustrated by the Trade and Transport Facilitation in South East Europe programme, a joint venture between the EU, the World Bank, and bilateral donor countries.[54] Of course, the private sector, already mentioned, whether operating nationally, regionally or globally, is another desirable stakeholder.

4.3. Which RTA? how the size of partner countries matters

Many aspects discussed so far are country-specific. Country or country-grouping characteristics have therefore significant implications for regional trade facilitation. Least developed countries face a set of constraints that require particular attention. First, economic size, meaning that economies of scale are less likely to be internalized at the national level, thus suggesting that small countries should team up to deliver regional trade facilitation instruments (witness the regional enquiry point proposed by Barbados). Size also implies that the bargaining position of small countries with more powerful neighbours leads to sub-optimal outcomes for them. The obvious example is transit. The LDCs are over-represented among landlocked countries. A solution to this size asymmetry would perhaps be for the small country to trade-off concessions in an RTA context by offering market access (in the services sector, for instance) against facilitated transit and better enforcement of rules, so that transit is not discriminated against (this includes competition in transport). Over-dependence on tax revenues is another characteristic of LDCs compared to more advanced developing and developed countries. This dependence creates strong incentives against trade facilitation, and in particular against sharing any border responsibility with neighbouring countries. In this respect, an asymmetric regional cooperation may be an advantage, as partnering with a large country that is less dependent on trade tax revenue will mean more political support for trade facilitation reform.

This raises the question of whether there are specific partners with whom to preferably implement trade facilitation reform? There is the complementarity between some aspects of trade facilitation and the volume of goods trade: transport infrastructure springs to mind. Modernization of trade procedures involves one-off fixed costs that will

[54] See <http://www.seerecon.org/ttfse/>.

be recouped more easily over larger volumes of trade. This obviously applies to the case of transit for landlocked countries, where often a few transit routes will represent a very large proportion of all external trade.

The volume of trade criterion however may fail to address the geographically determined dimensions of trade facilitation, as for many countries trade with neighbours is actually too low, thus shifting the focus of regional trade where transaction costs are already low, and possibly reinforcing existing distortions (Schiff, 2001).[55] A trade potential criterion makes more sense and thus incorporates the geography determinants of trade facilitation discussed.

A different question is whether regional cooperation would not be better with partners representing a large proportion of world trade? This complementarity can arise for some norm-based dimensions of trade facilitation reform: it makes more sense to harmonize standards with big world traders as this also means harmonization with this partner's trade partners. In the context of the positive externalities described earlier, it may make sense to integrate with hubs at the centre of large trade networks.[56] In a world where production processes become more fragmented, this seems the path to follow.[57] The share of world trade criteria points developing countries towards seeking trade facilitation reform in the context of agreements with Northern economies. This presents the added benefit of access to higher modern standards, technical assistance and capacity building: an important consideration for weak link-type public goods. Actually, evidence suggests that RTAs involving developed economies contain more detailed and sophisticated trade facilitation provisions (Bin 2008).

The above arguments need however to be qualified with the possible negative effects of RTAs mentioned earlier, in particular if trade facilitation measures boost trade diversion effects. This seems to reinforce in our view the importance of promoting regional trade facilitation measures in the context of regional trade agreements that are not trade-diverting to start with: an additional argument for choosing partners with a large share of the world's trade.

Finally, there is also the risk that countries with low capacity may not be able to share much with countries with sophisticated policies in place, or be invited to implement measures beyond what is strictly necessary for them.

Disentangling these dimensions is difficult. There is yet no clear prescription as to whether benefits might arise from selecting individual partners for reform. This suggests that a better framework for addressing trade facilitation issues might be to look more broadly and rely on complementarities of approaches: either a multilateral approach with

[55] See, for instance, Al-Atrash and Yousef (2000) on Arab trade. Another example is the share of trade between India and its neighbours.

[56] As pointed out by one reviewer, does it make sense for Mercosur to have an agreement on multi-modal transport (signed in 1994) among its countries but none with the EU and the United States, its main trade partners?

[57] This echoes a point made by Devlin and Estevadeordal (2004), who suggest that such "hub-and-spoke" arrangements enable greater geographical reach and economies of scope in the delivery of similar multiple public goods to different regions.

regional extensions or a hub-and-spoke approach such as that envisaged in the European Partnership Agreements.

5. Conclusions and Directions for Further Research

5.1. Regional interventions matter

Regionalism, specifically regional trade agreements, has undoubtedly a role to play in trade facilitation reform. We find several reasons why this should be the case:

- The existence of regional public goods, because of the presence of economies of scale and externalities at the regional level, for instance in the exchange of electronic information, or the mutualization of guarantee systems and transit.
- The "local" nature of several elements of the trade logistics chain and the inherent efficiency of reforming them at the regional level.
- The adequacy of regional trade agreements, if appropriately designed, for implementation of regional tools facilitating trade: this is because they are well designed to address both coordination and capacity constraints facing the provision of regional trade facilitation public goods. This means that regional trade agreements can deliver several, different, and complementary trade facilitation public goods.
- Another advantage of regional trade agreements is that they can incorporate deep integration dimensions. They are better suited to addressing complex regulatory liberalization. In addition, because they can be broad in scope across many policies, trade-offs between the many components of the trade logistics chain can be made, and offer better safeguards against violations of commitments.

5.2. Regionalism can deliver more

This said, there is yet scant evidence of success of regional agreements promoting effective trade facilitation. The reasons why this is the case are still not well identified and would warrant further research. Political economy considerations certainly play a very important role here; one of the reasons behind low political will could well be the reliance on trade tax revenue, a very sensitive issue for poor countries especially. There might thus be strong resistance to facilitating trade with regional partners. Incentives for better transit arrangements are quite difficult to address in this respect.

5.3. What scope for regional cooperation?

The RTAs need to shift focus from reciprocity to policy integration and from a narrow vision of border enforcement to a policy of integration into world markets. This entails a broader coverage of trade facilitation issues as a whole (recent trade agreements seem to move in that direction).

In particular, trade facilitation objectives should be integrated in RTAs with a clear objective to make them also more open to third-country trade. As we know too well, trade diversion means that regional trade agreements are not necessarily guaranteeing welfare gains for participants in the agreement, and are likely to generate welfare losses for countries excluded. Regionalism is also not necessarily a stepping-stone to multilateral trade liberalization. Trade facilitation reform can be a force for good in this context if it reduces trade transaction costs on trade from all origins. While we offer no clear conclusion as to whether facilitation is itself a stepping-stone, it indeed looks like a useful and relatively straightforward policy (probably easier to implement from a political point of view than tariff reform) to moderate the trade diversion effects of preferential tariff reduction.[58]

We also saw that the need for regional trade facilitation reform is going to differ depending on the absolute and relative size of countries under consideration. While some criteria helping to discern how regional trade facilitation could be delivered were identified, further work is needed to understand when the political economy incentives (in a way the demand for regional public goods) can be satisfied so as to result in optimal supply of regional public goods.[59]

There is also little evidence about the impact of the most successful regional integration agreements to guide policy makers on which regional trade facilitation policies may be desirable. In particular, the study of existing regional agreements could provide some lessons on whether there is a case for gradual approach, prioritizing specific trade facilitation regional public goods, leaving others for later and building upon that basis, as seems to have been the case in Europe.

5.4. Strong institutions are required

The crucial role played by institutions governing regional trade liberalization efforts must be emphasized. Their role seems to matter as much – if not more – in the implementation of the soft law aspects of reform than of hard rules. We emphasized the importance of cooperation and joint regulatory design to deliver regional trade facilitation solutions. This also highlights an area of comparative advantage of regional approaches over multilateral approaches. Additionally, weak institutions are not well equipped to manage heavy implementation challenges.

[58] Helping the RTA to maintain the level of trade with third parties to its pre integration level, otherwise known as the Kemp-Wan (1976) proposition.

[59] For instance, how exactly is coordination delivered? What makes countries that would compete with each other for the supply of trade facilitation infrastructure change their mind?

Regional institutions also need to be strong enough to push what are difficult reforms: customs unions seem relatively more efficient. Emphasis should be shifted from rules to implementation, with flexibility in mind, and possibly complementarity with other national or multilateral approaches. This may mean strengthening regional specialist organizations, eventually in partnership with the private sector, which have tended to be more successful in cooperation agreements or maintaining working groups of experts. Finally, customs unions have fared better than other forms of regional cooperation in many respects. Admittedly, customs unions are few, and forming a customs union requires a serious amount of political will on all sides: these are naturally good conditions for regional trade facilitation reforms.

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