

# CHINA'S REGIONAL TRADE AGREEMENT (RTA) APPROACH: THE LAW, THE GEOPOLITICS, AND THE IMPACT ON THE MULTILATERAL TRADING SYSTEM

JIANG YU, WANG\*

This paper examines China's recent movement in negotiating and signing regional trade agreements (RTAs) in the context of the regionalism versus multilateralism debate in international trade law, focusing on the China-Hong Kong Closer Economic Arrangement (CEPA) and the proposed China-ASEAN Free Trade Agreement (CAFTA). The broader background is that the potential negative effects of regional trade arrangements like CAFTA conflict with the economic goal of the multilateral trading system of the GATT/WTO regime. Countries, however, have a variety of non-economic considerations in approaching RTAs, such as regional stability and national security. Furthermore, the literature suggests that the economic benefits to members of RTAs, although they vary depending on the circumstances, are at least apparent in some cases. This paper, after introducing the content and progress in the CEPA and CAFTA negotiations, discusses the geopolitical considerations under China's CAFTA approach. It also analyzes the legal status and WTO-consistency of China's RTAs. It concludes that, while multilateralism is still serves the long-term interest of trading nations for peace and prosperity, the multilateral trading system should accommodate regionalism in a fashion that strikes a balance between the economic and non-economic concerns of the various countries and the goal of broader liberalization in global trade and investment. China, as a rising trade power with global influence, has the responsibility to promote regional integration and global trade liberalization in the interest of the aforesaid balance.

## I. INTRODUCTION

International trade is a process involving a wide-ranging, transactional, cross-border commercial exchange of goods and services between individual persons, corporate entities, and states. The body of international trade law is thus regarded as a legal regime governing the economic and commercial activities attendant to foreign trade. However, the various policy or legal aspects of trade are much more complicated than economists are wont to admit. The recent "trade and ..." phenomenon, which concerns the linkage between trade and non-trade issues, and has generated a tremendous literature, reveals the panoply of non-economic concerns.<sup>1</sup>

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\* Assistant Professor, Faculty of Law, National University of Singapore; SJD & LLM (U.Penn); MJur (Oxford); LLM (Peking); LLB (China University of Political Science and Law). This article is a revised version of a paper presented to the "International Conference on Southeast Asia and China: Global Changes and Regional Challenges" held in National Sun-Yat Sun University, Kaoshiung, Taiwan in March 2004. I would like to thank Dr. Lim Chin Leng and Michael Ewing-Chow of the Law Faculty of National University of Singapore for our lively discussions on the subject. I am especially grateful to Dr. Lim and Mr. Jeremy Leong for their meticulous editing work on this piece. All the views, errors and omissions are the author's alone.

<sup>1</sup> Jeffrey L. Dunoff. "Rethinking International Trade" [1998] 19 U.Pa.J.Int'l Econ.L 347. The "trade and ..." linkage issues, as commonly regarded, include "trade and environment", "trade and labor", "trade and competition policy", "trade and human rights", "trade and intellectual property", "trade and competition policy", and a few others. Labor and environment linkages are probably the two most debated topics in the "trade and ..." phenomenon.

Regionalism<sup>2</sup> in the international trading system, in so far as it involves the question of trade and discrimination, is linked to one of the oldest “trade and ...” problems.<sup>3</sup> Regionalism is also part of international trade activities and it therefore bears the full nature of trade which is a multifaceted issue encompassing economics, domestic politics, and national security and geopolitical factors. For this reason, an individual effort towards regional preferential trade arrangements (hereinafter “RTAs” and “RTA” when appropriate) or free trade agreements (hereinafter “FTAs” or “FTA” when appropriate)<sup>4</sup> should be carefully examined in its particular context and take into consideration the various non-economic factors underlying it.

While regionalism has been in existence for over half a century since World War II,<sup>5</sup> China jumped onto the bandwagon only very recently, embodied initially by the formation of the China-Hong Kong Closer Economic Partnership Arrangement (“CEPA”) and the China-Macao CEPA. China has also signed framework agreement for establishing free trade zones with the Association of Southeast Asian Nations (“ASEAN”), and is negotiating similar arrangements with Australia, New Zealand, and the MERCOSURE countries. The CEPAs, which are already in operation, are RTA-like arrangements between China and the two “special administrative regions” under the Chinese political sovereign, with the signatories acting as members of the World Trade Organization (“WTO”).<sup>6</sup> The proposed China-ASEAN Free Trade Area, with a nice acronym “CAFTA”, will create one of the world’s largest FTA, standing on par with the North America Free Trade Area (“NAFTA”) and the European Union (“EU”). It is also, the largest FTA made up of developing countries.<sup>7</sup>

Two fundamental questions need to be answered with regard to China’s recent RTA approaches. First, what are the motivations behind the moves? Exploration of the motives is essentially important because they decide the content, scope and all future acts of China as regards its pursuit of RTAs. Eventually, the RTAs participated in by China and in

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<sup>2</sup> Regionalism in the context of international trade was defined as “the promotion by governments of international economic linkages with countries that are geographically proximate.” See Nigel Grimwade. *International Trade Policy* (London: Routledge, 1996) at 232. However, in recent decades, regional trade agreements have been signed by countries located in different regions and even different continents, such as the *US-Israel Free Trade Agreement* and the *US-Singapore Free Trade Agreement*. To modify the traditional definition, regionalism can now be broadly characterized as the tendency towards the creation of preferential trade arrangements between a number of countries, which discriminate against third countries.

<sup>3</sup> James H. Mathis. *Regional Trade Agreements in the WTO* (The Hague: T.M.C. Asser Press, 2001) at 1.

<sup>4</sup> The coverage of regional preferential trade arrangements is broadly defined here. See *supra* note 2. Generally, RTA(s) and FTA(s) are used interchangeably in this article.

<sup>5</sup> See Grimwade, *supra* note 2, at 251-282. See also WTO Secretariat. *Regionalism and the World Trading System* (Geneva: World Trade Organization, 1995) at 25-38. Jagdish Bhagwati has observed that there have been two phrases of regionalism in the post WWII period. The first phrase occurred in the late 1950s and early 1960s, represented by the European Community (EC), the European Free Trade Area (EFTA), the Latin America Free Trade Association (LAFTA), the Central African Customs and Economic Union (CACEU) and a few others. The second wave of regionalism, an ongoing phenomenon, first occurred in 1980s. The EU and NAFTA are typical examples of FTAs concluded in this period. See *Ibid*.

<sup>6</sup> Mainland China, Hong Kong and Macao are all WTO Members. China joined the WTO in 11 December 2001, and Macao and Hong Kong obtained the Contracting Party status of the General Agreement on Tariffs and Trade (“GATT”) in 11 January and 23 April 1986, respectively, as separate customs territories under the British sovereign and Portuguese sovereign. See the “Membership” section on the WTO’s website at <<http://www.wto.org>>.

<sup>7</sup> ASEAN-China Experts Group on Economic Cooperation. “Forging Closer ASEAN-China Economic Relations in the Twenty-First Century” online: ASEAN official website <<http://www.aseansec.org>> (hereinafter the ASEAN-China FTA Report).

conformity to its strategic goals will have profound implications on the fate of the multilateral trading system currently under the auspices of the WTO. As the WTO has noted, “political considerations will inevitably feature in decisions to establish regional trading arrangements.” Political factors, especially *realpolitik*, play a role, which is by no means, less significant than economic considerations. This is especially true with regard to China’s recent RTA approach in East Asia after its accession to the WTO, engaging major countries in the region including ASEAN members, Japan, South Korea, Hong Kong and Taiwan.<sup>8</sup>

The second fundamental question concerns the complex impact of China’s RTAs on the WTO-led multilateral trade system. This involves a two-level analysis. First, are the RTAs concluded by China consistent with the existing WTO rules, especially the most-favored-nation (MFN) clause and GATT Article XXIV? On its accession to the WTO, China committed to implementing the WTO agreement as well as the annexed Multilateral Trade Agreements.<sup>9</sup> A violation of WTO obligations through RTAs will certainly cause serious concerns among other WTO members and further undermine China’s credibility in international trade. Secondly, the impact of China’s RTA approach on the future of the multilateral trade talks (currently the WTO’s Doha Round negotiation) shall be examined. As there exists a potential conflict between the proliferation of regional trading blocks, which attempts to realize regional or bilateral trade liberalization, and the WTO regime, which thrives to liberalize trade multilaterally without preferential discrimination, exponents on both sides are now engaged in an enormously heated debate regarding the orientation of the international trade system.<sup>10</sup> Ultimately, China’s sheer size of population and territory, its top-ranking economy and trade volume, as well as, its leadership position in the developing world, makes the Chinese position on regionalism versus multilateralism a crucial determinant that may alter the direction of this ongoing debate.

This article is an attempt to outline and analyze the content and implication of recent Asian RTAs and proposed RTA frameworks concerning China, with a view to evaluating WTO compliance of China-participated RTAs, as well as, their impact on the future direction of the multilateral trading system. Part II lists China’s RTA movements and briefly outlines the scope and content of each of them. Part III discusses the geopolitical factors behind China’s RTAs. Part IV examines the relevant WTO rules on RTAs and evaluates the WTO consistency of China’s RTAs. Part V analyzes the impact of China’s RTA approach on the multilateral trading system. In its conclusion, this article argues that China’s pursuit of regional and national security and great power status is both legitimate, given that there are no meaningful WTO rules prohibiting this, and beneficial to the region, considering East Asia’s troublesome geopolitical layout. However, China should be mindful of the importance of the multilateral trading system in achieving its goal. As a top trading power, China also has the responsibility to push multilateral trade liberalization rather than being obsessed with

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<sup>8</sup> The use of the term “country” or “countries” follows the Explanatory Notes to Article XVI of the Uruguay Round Agreement Establishing the World Trade Organization, which provides, “The terms ‘country’ or ‘countries’ as used in this Agreement and the Multilateral Trade Agreements are to be understood to include any separate customs territory Member of the WTO.”

<sup>9</sup> *Protocol on the Accession of the People’s Republic of China*, annex to the *Accession of the People’s Republic of China* (2001) WTO Doc. WT/L432 at Part I, art. 1(1), (2) and (3) (hereinafter China’s WTO protocol).

<sup>10</sup> See e.g., Jagdish Bhagwati. *The World Trading System At Risk* (Hemel Hempstead, Herts.: Harvester Wheatsheaf, 1991). A very good recent account of this debate is a book edited by Richard Pomfret titled *Economic Analysis of Regional Trading Arrangements* (Northampton, MA: Edward Elgar Pub, 2003), it features the masterful works of Jacob Viner, Harry Johnson, Robert A. Mundell, Paul R. Krugman, Lawrence H. Summers and many others prominent economists.

regionalism. On the other hand, it shall be realized that the quest for regional trade arrangements demonstrates many weaknesses of the WTO-led multilateral trading system. Regional movements for free trade, as currently pursued by China, shall be allowed and even encouraged to the extent that they do not create trade diversion and divergent rules from the multilateral trade system.

## II. CHINA'S RECENT RTA INITIATIVES AND THEIR CONTENTS

### A. *The CEPAs between Hong Kong, Macao and Mainland China*

The Mainland and Hong Kong Closer Economic Partnership Arrangement (“CEPA”) was signed in June 2003 by the representatives from the Chinese central government and Hong Kong Special Administrative Region of the PRC (HKSAR).<sup>11</sup> This is the first RTA for both sides. Three and half months later, the Mainland concluded a similar agreement with Macao.<sup>12</sup> Our focus will remain on the China-Hong Kong CEPA because the agreement between China and Macao is virtually modeled after the former.

#### 1. *The negotiating history of the China-Hong Kong CEPA*

The idea of forming a RTA with Mainland China was first conceived by the Hong Kong business community. In 1999, the Hong Kong General Chamber of Commerce (HKGCC), anticipating China’s entry into the WTO, initiated a project to assess the impact of China’s entry on specific industries in Hong Kong. The final report, *China’s Entry into the WTO and the Impact on Hong Kong Business* released in January 2000,<sup>13</sup> suggested that the Hong Kong government, in its efforts to help local business, should “explore the benefits of a Free Trade Area agreement with the Mainland, similar to the NAFTA type regional trade agreement, which would be in keeping with WTO rules.”<sup>14</sup> In 19 December 2001, Hong Kong’s Chief Executive Tung Chee Hwa raised the request to and successfully obtained endorsement from China’s central government. Formal negotiations were started in February 2002, immediately after China’s accession to the WTO in December 2001. On 29 June 2003, the CEPA Main Agreement was signed, witnessed by Chinese Premier Wen Jiabao. Three months later, on September 29, the six annexes were also signed, giving the main agreement workable details. CEPA and its annexes have been effective as of 1 January 2004.

CEPA consists of a Main Agreement together with six annexes, and two tables.<sup>15</sup> Briefly speaking, it covers three broad areas. They are, trade in goods, trade in services and trade and investment facilitation.

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<sup>11</sup> The official website of the China-HK CEPA is <<http://www.tid.gov.hk/english/cepa/index.html>>.

<sup>12</sup> The official website of the China-Macao CEPA is <<http://www.macao.gov.mo/cepa.phtml?lang=en>>.

<sup>13</sup> Information about the report can be found at the <<http://www.chamber.org.hk/wto/content/reports.asp>>.

<sup>14</sup> The “Executive Summary” of the HKGCC report on “China’s Entry into the WTO and the Impact on Hong Kong Business,” available at <[http://www.chamber.org.hk/wto/report/wto\\_summary.asp](http://www.chamber.org.hk/wto/report/wto_summary.asp)>.

<sup>15</sup> The Main Agreement is entitled “Mainland/Hong Kong Closer Economic Partnership Arrangement.” The six annexes under the framework of the main text are, respectively, Annex 1: Arrangements for Implementation of Zero Tariff for Trade in Goods, and Table 1 (under Annex 1): List of Hong Kong Origin Products for Implementation of Zero Import Tariff by the Mainland; Annex 2: Rules of Origin for Trade in Goods, and Table 1 (under Annex 2): Schedule on Rules of Origin for Hong Kong Goods Benefiting from Tariff Preference for Trade in Goods; Annex 3: Procedures for the Issuing and Verification of Certificates of

## 2. *China-Hong Kong CEPA on trade in goods*

In respect of goods trade, China has agreed to eliminate tariffs on imported goods of Hong Kong origin in stages. As of 1 January 2004, China undertakes to eliminate tariffs on 273 categories of Hong Kong products, representing over 4000 items.<sup>16</sup> According to the Hong Kong authority, this, together with China's commitments upon accession to the WTO, will cover 90 percent of Hong Kong domestic export to China.<sup>17</sup> For other products, China will apply zero tariff rates by 1 January 2006 upon application by Hong Kong manufacturers.<sup>18</sup> Non-tariff measures, except for safeguards, are precluded by CEPA. The Main Agreement prohibits the two sides from taking anti-dumping, countervailing, tariff rate quotas or any other non-tariff measures that are inconsistent with WTO rules to goods originating from the other side.<sup>19</sup>

## 3. *China-Hong Kong CEPA on trade in services*

CEPA grants market access to the mainland to a total of eighteen Hong Kong services industries. Those concessions, according to commentators, constitute "the most significant component"<sup>20</sup> of the CEPA pact, covering amongst others, management consulting, convention and exhibition, advertising, accounting, banking, securities, insurance, logistics, movie industry, construction, shipping and value-added telecommunications services.<sup>21</sup>

Compared with China's commitments to other WTO Members States in its accession protocol,<sup>22</sup> CEPA gives Hong Kong businesses a "first move" advantage. In the prescribed eighteen industries, Hong Kong service providers can enjoy preferential treatment ahead of China's WTO timetable. For example, in the management consulting industry. According to China's WTO commitments, wholly foreign owned enterprises (WFOE) will not be permitted before 11 December 2007. CEPA, however, allows Hong Kong service providers to establish WFOE as from 1 January 2004.<sup>23</sup> Certain preferential forms of treatment extended to Hong Kong businesses even go beyond China's WTO obligations. In banking, for example, China's WTO commitments mandate a minimum asset requirement of US\$ 20 billion for an overseas financial institution for establishing a branch and US\$ 10 billion for a subsidiary in China. For a Hong Kong entity, the minimum asset requirement is, instead,

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Origin, and Form 1 (under Annex 4): Certificate of Hong Kong Origin (CEPA); Annex 4: Specific Commitments on Liberalization of Trade in Services, and Table 1 (under Annex 4): The Mainland's Specific Commitments on Liberalization of Trade in Services for Hong Kong, and Table 2 (under Annex 4): Hong Kong's Specific commitments on Liberalization of Trade in Services for the Mainland; Annex 5: Definition of "Service Supplier" and Related Requirements; and Annex 6: Trade and Investment Facilitation. The full texts of CEPA are available on Hong Kong's official website for CEPA at <<http://www.tid.gov.hk>>.

<sup>16</sup> See *ibid.*, art. 5(2) of the Main Agreement, and arts. 2 and 3 of Annex 1.

<sup>17</sup> Hong Kong Trade Development Council. "CEPA and Opportunities for Hong Kong" (20 October 2003) online: <<http://www.tdctrade.com/econforum/tdc/tdc031002.htm>>.

<sup>18</sup> See *supra* note 15, the Main Agreement, art. 5(3) and Annex 1, art. 5.

<sup>19</sup> See *supra* note 15, the Main Agreement, arts. 6, 7 and 8.

<sup>20</sup> Matt Pottinger. "Hong Kong Fleshes Out Its Chinese Trade Accord, Giving Multinational Hope" *Wall Street Journal* (30 September 2003) at A18.

<sup>21</sup> See *supra* note 15, Table 1 (under Annex 4).

<sup>22</sup> See *supra* note 9.

<sup>23</sup> See *supra* note 15, Table 1 (under Annex 4).

only US\$ 6 billion in comparison.<sup>24</sup> In logistics services, although China has made no commitments in its WTO accession agreements, CEPA allows Hong Kong residents to establish WFOEs in the Mainland as of 1 January 2004.<sup>25</sup> In legal services, although China gives little concession to other WTO Members, Hong Kong law firms are allowed to establish representative offices in China to operate in association with Mainland law firms, albeit that the association cannot take the form of a partnership. Chinese law firms can employ Hong Kong barristers or solicitors, while Hong Kong permanent residents with Chinese citizenship are permitted to sit the bar examination in the Mainland and acquire Chinese legal professional qualifications.<sup>26</sup> This is far beyond China's commitments in its WTO services schedule.

#### 4. *China-Hong Kong CEPA on trade and investment facilitation*

In Articles 16 and 17 of the Main Agreement and Annex 6, the two sides agree to pursue trade and investment facilitation through greater transparency, standardization, and enhanced information change,<sup>27</sup> especially in trade and investment promotion, customs clearance, quarantine and inspection of commodities, food safety and quality assurance, electronic commerce, transparency in law and regulation, small and medium-sized enterprises, and in respect of the trade in Chinese medicine and medical products.<sup>28</sup> Pursuant to Article 3 of Annex 6, China and Hong Kong have established a Joint Steering Committee for the overall coordination of CEPA affairs.

#### B. *The China-ASEAN Free Trade Agreement (CAFTA) Proposal*

##### 1. *The negotiating process of CAFTA*

At the ASEAN-China Summit in November 2000, Chinese Premier Zhu Rongji put forward a basket of proposals on strengthening cooperation in East Asia, including, "seen in the long run", China and ASEAN should explore the possibility on the formation of an FTA.<sup>29</sup> At his suggestion, a China-ASEAN Experts' Group on Economic Cooperation ("Experts' Group") was established to look into the possibility of establishing a free trade area between the two sides.<sup>30</sup> In its final report issued in October 2001, the group suggested the construction of a "WTO-consistent ASEAN-China FTA within ten years".<sup>31</sup> It noted the profound implication of CAFTA as follows:

[T]he establishment of a FTA between ASEAN and China will create an economic region with 1.7 billion consumers, a regional GDP of about US\$ 2 trillion and total trade estimated at US\$ 1.23 trillion... [T]he removal of trade barriers between

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<sup>24</sup> *Ibid.*

<sup>25</sup> *Ibid.*

<sup>26</sup> *Ibid.*

<sup>27</sup> See *supra* note 15, Main Agreement, art. 16.

<sup>28</sup> *Ibid.* at art. 17.

<sup>29</sup> "Zhu Rongji chuxi di sici Zhongguo-Dongmeng lingdaoren huiwu" (Zhu Rongji attends the fourth China-ASEAN Summit) Xinhua News Agency (25 November 2000).

<sup>30</sup> ASEAN Secretariat. "ASEAN Annual Report 2000-2001" online: ASEAN website <<http://www.aseansec.org>> at 10.

<sup>31</sup> See the ASEAN-China FTA Report, *supra* note 7 at 36.

ASEAN and China will lower costs, increase intra-regional trade and increase economic efficiency. The establishment of an ASEAN-China FTA will create a sense of community among ASEAN members and China. It will provide another important mechanism for supporting economic stability in East Asia and allow both ASEAN and China to have a larger voice in international trade affairs on issues of common interest.<sup>32</sup>

The report also recommended that China and ASEAN adopt a comprehensive and forward-looking framework of economic cooperation, so as to forge closer economic relations in the 21<sup>st</sup> century. In November 2001, the Seventh China-ASEAN Summit endorsed the ideas envisaged by the Experts' Group and initiated the negotiation progress.<sup>33</sup> At the Eighth China-ASEAN Summit in Phnom Penh, Cambodia in November 2002, ASEAN and Chinese leaders signed the "Framework Agreement on the Comprehensive Economic Co-Operation between ASEAN and China" (hereinafter the "FA"). Having come into force on 1 July 2003, it provides the groundwork for the eventual formation of the CAFTA by 2010 for the six older ASEAN members and 2015 for the newly admitted members (Cambodia, the Lao PDR, Myanmar and Viet Nam).<sup>34</sup> The FA was amended by a Protocol signed on 6 October 2003 by China and ASEAN at their 2003 annual summit in Bali.<sup>35</sup> The FA represents the first FTA initiative of both ASEAN (as a group) and China (outside the Greater China Area<sup>36</sup>).

## 2. *Scope and measures for economic cooperation under the FA*

With a view to establishing the CAFTA before 2010, the parties to the FA agree to strengthen cooperation and to "progressively liberalize and promote trade in goods and services as well as create a transparent, liberal and facilitative investment regime."<sup>37</sup> This suggests that the proposed CAFTA will cover trade in goods and services, as well as, trade and investment facilitation. In addition, the FA opens the door for the parties to "explore new areas and develop appropriate measures for closer economic co-operation."<sup>38</sup> Specific measures towards the realization of CAFTA, which will be implemented progressively in the coming years, include the following:<sup>39</sup>

- (a) *Elimination of tariffs and non-tariff barriers in substantially all trade in goods;*
- (b) *Liberalisation of trade in services with substantial sectoral coverage;*
- (c) *Establishment of an open and competitive investment regime that facilitates and promotes investment within CAFTA;*

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<sup>32</sup> *Ibid.* at 2.

<sup>33</sup> ASEAN Secretariat. "ASEAN Annual Report 2001-2002" online: ASEAN website <<http://www.aseansec.org>>.

<sup>34</sup> *Framework Agreement on Comprehensive Economic Co-Operation between the Association of South East Asian Nations and the People's Republic of China* (5 November 2002) online: ASEAN Secretariat <<http://www.aseansec.org>> [hereinafter the FA].

<sup>35</sup> *The Protocol to Amend the Framework Agreement on Comprehensive Economic Co-operation Between the Association of South East Asian Nations and the People's Republic of China* (6 October 2003) online: ASEAN website <<http://www.aseansec.org>> [hereinafter the *Protocol*].

<sup>36</sup> The Greater China Area includes Mainland China, Hong Kong, Macao, and Taiwan.

<sup>37</sup> FA, *supra* note 34, art. 1(b).

<sup>38</sup> *Ibid.* at art. 1(c).

<sup>39</sup> *Ibid.* at art. 2.

- (d) *Special and differential treatment and flexibility to the newer ASEAN Member States, including Cambodia, the Lao PDR, Myanmar and Vietnam;*
- (e) *Flexible measures to allow the parties in CAFTA negotiations to address their sensitive areas in the goods, services and investment sectors with such flexibility to be negotiated and mutually agreed based on the principle of reciprocity and mutual benefit;*
- (f) *Trade and investment facilitation measures, such as simplification of customs procedures and the development of mutual recognition arrangements;*
- (g) *An open attitude toward further liberalization in new areas/sectors; and*
- (h) *The establishment of appropriate mechanisms for the effective implementation of the FA.*

### 3. *Early-Harvest Programme (EHP) for trade in goods under the FA*

In addition to obligations to enter into negotiations for the ultimate free trade pact, the FA also establishes an Early Harvest Programme (hereafter, “the EHP”). Implemented as of 1 January 2004, it is aimed to reap the immediate concessions offered by the parties, mainly China. The EHP allows the reduction of tariffs on certain products before the onset of CAFTA. Initially, it aims to implement tariff reduction on these products over three years: to 10 percent before 2004, to 5 percent before 2005, and to zero tariffs no later than 1 January 2006.<sup>40</sup> A distinctive feature of the EHP is that China has also given unilateral concessions to ASEAN members who feel they would not benefit as much from the EHP. These concessions cover over 130 agricultural and manufacturing products.<sup>41</sup> In essence, it “allows ASEAN products to be exported to China at a significant concessionary rate so that ASEAN countries can actually benefit from the benefits of a free trade agreement even before the agreement itself is finalized.”<sup>42</sup> In return, the ASEAN countries agree to give tariff concessions to China under the Harmonized System (“HS”) on tariffs for agricultural products including meat, fish, fruit, vegetables and milk.<sup>43</sup> In total, the EHP has targeted a host of some 600 products listed in Chapters 1-8 of the HS, mostly agricultural products which are to be unilaterally liberalized by China.<sup>44</sup> In addition, China agrees to grant WTO benefits (mainly MFN treatment) to ASEAN members which are not official WTO members yet.<sup>45</sup>

Initially the FA took a multilateral approach to tariff reduction. Namely, that the tariff concessions under the HS approach shall be multilateralized to all parties (i.e. all ASEAN members and China) provided that the same products are included in their EHP. But, because the Philippines and China failed to establish an EHP scheme, other countries in the region subsequently considered that this would therefore allow the Philippines to “free ride”. In addition, fear that some ASEAN countries like Thailand, which have more efficient farm sectors, could suppress the growth of the agricultural sector in others has also deterred ASEAN members from implementing a multilateral approach under the EHP. Malaysia was amongst the first to negotiate a clause in 2003, allowing it to offer lower agriculture tariffs

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<sup>40</sup> Annex 3 of the FA, Part B. A slightly different schedule is used for the newer ASEAN members.

<sup>41</sup> Annex 2 of the FA.

<sup>42</sup> “ASEAN, China Launch First Stage of Free-Trade Plan” *AFP* (7 October 2003).

<sup>43</sup> *Ibid.*

<sup>44</sup> China, however, has excluded from EHP some agricultural products such as rice and palm oil, which are said to be major exports from ASEAN countries. These products are to be negotiated in the coming years.

<sup>45</sup> FA, art. 9. Currently Cambodia, Vietnam and the Lao PDR are not WTO Members.



only to China in return for the latter's concessions under the EHP.<sup>46</sup> This practice has since been consolidated in the 2003 Protocol, which replaces the original Article 6(3)(b)(i) of the FA with a new provision. The new provision recognizes that a party may accelerate its tariff reduction and/or elimination under the EHP to the rest of the parties "on a unilateral basis."<sup>47</sup> Meanwhile, one or more ASEAN members are still allowed to conduct negotiations and enter into acceleration arrangements with China so as to fast-track their tariff reduction or elimination. However, this shall only be done on a "bilateral or plurilateral" basis. In other words, no conditional or unconditional MFN status is granted under the EHP except to Brunei and Singapore.<sup>48</sup>

A good example of a tariff acceleration arrangement is the *China-Thailand Agreement on Accelerated Tariff Elimination under the Early Harvest Programme*,<sup>49</sup> which prescribes that China and Thailand shall eliminate tariffs on all vegetable and fruit products no later than 1 October 2003 (ahead of the EHP effective date of 1 January 2004, as well as, the targeted zero tariff date of 1 January 2006).<sup>50</sup>

#### 4. *Negotiation agenda for goods, services, investment and other areas to complete CAFTA*

Goods not covered by the EHP are subject to further negotiation within specified timeframes. The FA categorizes these goods into two tracks. The first, the "Normal Track", contains products tariff rates which shall be gradually reduced or eliminated in accordance with specified schedules (to be mutually agreed by the Parties) over a period from 1 January 2005 to 2010 by the ASEAN 6 and China, and from 1 January 2005 to 2015 for the newer ASEAN members.<sup>51</sup> The "Sensitive Track" represents a second category of products specified by an individual Party on its own accord in respect of which, a timeframe is not imposed on further liberalization. Parties are merely required to reduce (or eliminate when applicable) tariffs on Sensitive Track products "in accordance with the mutually agreed end rates and end dates."<sup>52</sup> In addition to tariffs, the negotiations shall also include, among others, rules of origin, out-quota-rates, re-negotiation of concession schedules, non-tariff measures, trade remedy laws, trade facilitation measures, as well as, trade related intellectual property protection.<sup>53</sup> In terms of the timeframe, the FA prescribes that the goods negotiations shall commence in early 2003 and be concluded by 30 June 2004.<sup>54</sup>

The FA, however, does not have a mandatory timeframe for the negotiations on services and investment, except that negotiations shall commence in 2003 and be concluded "as expeditiously as possible for implementation in accordance with the timeframes to be

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<sup>46</sup> "Malaysia Early Harvest Clause a Way out for RP" *The Manila Times* (7 April 2003) online: The Manila Times <<http://www.manilatimes.net/national/2003/apr/07/business/20030407bus4.html>>.

<sup>47</sup> The *Protocol*, *supra* note 35, art. 2.

<sup>48</sup> *Ibid.* Only Brunei and Singapore will, subject to conformity with specified requirements, automatically become parties to any arrangements that have been agreed on or will be agreed to between China and any other ASEAN state under the EHP. See *ibid.* at Annex 2. Singapore has already become a Party to the China-Thailand EHP arrangement.

<sup>49</sup> Text of the agreement is available on China's Ministry of Commerce website at <<http://www.mofcom.gov.cn>>.

<sup>50</sup> *Ibid.* at art. 1.

<sup>51</sup> The FA, art. 3(4)(a)(i).

<sup>52</sup> *Ibid.* at art. 3(4)(b).

<sup>53</sup> *Ibid.* at art. 3(8).

<sup>54</sup> *Ibid.* at art. 1(1).

mutually agreed.”<sup>55</sup> Substantive negotiations in these two areas have already started for the conclusion of the framework texts and the first packages of commitments are set for the second half of 2004.<sup>56</sup> The negotiations on services seek to progressively eliminate substantially all discrimination and to prohibit new discriminatory measures with respect to trade in services between the Parties.<sup>57</sup> The FA also seeks to expand the depth and scope of liberalization in trade in services beyond those undertaken by China and ASEAN Members under the GATS.<sup>58</sup> This could result in an acceleration of China’s WTO commitments on services for ASEAN, not unlike what China has done for Hong Kong and Macao. As for investment, the FA aims, through negotiations, “to obtain commitments on liberalizing the investment regime, increasing market access as well as commitments on protection of investment in the China market.”<sup>59</sup>

Besides trade and investment, China and ASEAN have also identified five priority sectors for strengthened cooperation, including agriculture, information and communications technology, human resources development, investment, and the Mekong River basin development, as well as, eleven other activities, including standard mutual recognition and harmonization, electronic commerce, technology transfer, and specific projects such as the acceleration of the railway project linking Singapore and China’s southern city Kunming.<sup>60</sup> All these efforts indicate that the FA is indeed a herald for an all-embracing pact of economic cooperation.

### C. Other RTA Proposals involving China

After the bold proposal for CAFTA, China has also reached out to a number of countries for free trade arrangements. China has engaged in a series of bilateral talks with the MERCOSUR (the South American Common Market) countries. The two sides have agreed in September 2003 to start with bilateral agreements in specific areas and mechanisms to increase integration and facilitate trade.<sup>61</sup> In May 2004, it has also agreed with Singapore and the Gulf Cooperation Council (GCC) countries to start bilateral FTA negotiations.<sup>62</sup> Another major move is being pushed on China’s western front, under the auspices of the Shanghai Cooperation Organization (SCO) comprising China, Kazakhstan, Kyrgyzstan, Russia, Tajikistan and Uzbekistan. The SCO was originally a pure political group formulated in 1996 to improve regional stability and counter the influence of Islamic fundamentalism in central Asia. Prompted by China, premiers of the five member states of the SCO signed a multilateral economic cooperation Framework Agreement, on 23 September 2003 in Beijing, to “deepen” the economic connections between member states and “improve the investment environment”.<sup>63</sup> More significantly, Chinese Premier, Wen Jiabao had made three

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<sup>55</sup> *Ibid.* art. 8(3).

<sup>56</sup> *ASEAN-China FTA Factsheet*, Ministry of Trade and Industry (MTI) of Singapore, available at <<http://www.mti.gov.sg>>.

<sup>57</sup> The FA, art. 4(a).

<sup>58</sup> *Ibid.* at art. 4(b).

<sup>59</sup> MTI of Singapore, *infra* note 62.

<sup>60</sup> The FA, Annex 4.

<sup>61</sup> “From the Regions: China Intensifies Regional Trade Talks” *Bridges Weekly Trade News Digest* Vol. 7, No. 32, (1 October 2003) available online: <<http://www.ictsd.org>>.

<sup>62</sup> See Laurel Teo. “FTA Talks with China in November” *The Straits Times* (15 May 2004). And see “GCC States Eye Trade Pact with China” *Xinhua News Agency* (9 May 2004).

<sup>63</sup> Shanghai Cooperation Organization, News Release, “Joint Communiqué of the Premiers Meeting of Shanghai Cooperation Organization” (23 September 2003) available online: <<http://www.fmprc.gov.cn>>.

proposals concerning economic cooperation within the SCO, the most surprising being the long-term objective to establish a free trade area within the SCO.<sup>64</sup> This proposal has been consolidated into a Framework Agreement.

China has also extended invitations to Australia and New Zealand which are regarded by China as part of the Western world and long-term US allies.<sup>65</sup> On 25 October 2003, during the state visit of Chinese President Hu Jintao to Australia, China and Australia signed a Trade and Economic Framework Agreement, which is regarded as “the first steps towards a free trade agreement worth billions of dollars”.<sup>66</sup> A few days later, the Chinese leader also reached a consensus with his New Zealand counterpart to start negotiations for a free trade deal between the two countries.<sup>67</sup>

### III. THE MOTIVATIONS BEHIND CHINA’S RTA APPROACH: POLICY AND GEOPOLITICS

#### A. *The Primary Motivations: Economics or Geopolitics?*

Cooperation through free trade arrangements is, by definition, economic in nature. It is difficult, however, to conclude that China’s recent RTA moves were only economically driven. They are, at least, not for immediate and short-term economic benefits, though immediate unilateral concessions from China to other parties involved in the RTAs are immense. To use the CEPAs as an example, although Hong Kong and Macao will be China’s first choice to supply products and services with a high value-added dimension to the Mainland Chinese market and thus reap immediate, as well as, long term trade and employment-creation rewards,<sup>68</sup> the immediate economic gain to the Mainland is not so obvious. That is probably why Hong Kong leaders have said that “[t]his agreement has given us an opportunity that our neighboring countries can only dream of.”<sup>69</sup> The Wall Street Journal further noted that “the [CEPA] pact contains almost no concessions to China, because Hong Kong is already one of the freest economies in the world and doesn’t impose import tariffs except on a handful of goods and services.”<sup>70</sup> China’s RTA framework agreement with ASEAN, especially the EHP, demonstrates a similar feature of unilateral

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<sup>64</sup> *Bridges Weekly*, *supra* note 61. See also “Shanghai Zezuo Zuzhi Chengyuan Guo Zongli Huiwu: Wen Jiabao Ti San Changyi [SCO Premiers Submit: Wen Jiabao put forward three proposals]” *China News Agency* (23 September 2003) available online: <<http://news.sina.com.cn>>.

<sup>65</sup> In November 2003, at the annual ASEAN PLUS THREE (China, Japan and Korea) Summit, then Chinese Premier Zhu Rongji proposed to form a FTA with Japan and South Korea. The responses he received from the two countries were hardly positive. So far, there has been no substantive negotiation for a China-Japan-Korea FTA. The three countries, however, have agreed to start the feasibility study. As David Wall of the Royal Institute of International Affairs in London notes, “There is not much chance of a trilateral FTA in Northeast Asia for now then. Which is why Roh and Hu could only agree to leave it to academics to chew over, endlessly.” See David Wall, “East Asia FTA? Dream On!” *Japan Times* (2 July 2003).

<sup>66</sup> Steve Lewis, John Kerin & Negel Wilson. “China: New Economic Era Begins” *The Australian* (25 October 2003).

<sup>67</sup> Fran O’Sullivan. “Chinese Minister Says Free Trade Deal Likely” *The New Zealand Herald* (13 January 2004) available online: <<http://www.nzherald.co.nz>>.

<sup>68</sup> See Hong Kong Trade Development Council. *CEPA and Opportunities for Hong Kong* (20 October 2003) and Hong Kong Trade Development Council. *CEPA’s Opportunities Beyond WTO* (2 October 2003) available online: <<http://www.tdctrade.com>>.

<sup>69</sup> “Hong Kong and China Sign Free Trade Deal” *Financial Times [Asian Edition]* (29 June 2003).

<sup>70</sup> Matt Pottinger. “A Back Door to China Opens Wider – Hong Kong Fleshes Out Its Chinese Trade Accord, Giving Multinationals Hope” *Wall Street Journal* (30 September 2003) at A18.

concessions to open up first, embracing the other countries' exports to China. Ultimately, experts believe that the long-term benefit of CAFTA might be enormous to both sides.

China's RTA approach, as a strategic movement, must be viewed in a larger context embracing both economic and geopolitical considerations, with the latter playing a relatively more important role at this stage. It is a part of China's regional and global strategy in light of China's its national interests. As its economy and global influence grows, China has now acquired the confidence to proactively employ a variety of tactics and moves to achieve its interests. But as the following sections will aim to demonstrate, although China's ultimate goal is not yet clearly manifested, its rhetoric and actions so far indicate that it is a pragmatic, constructive partner rather than a destructive player concerned only with pushing its interests unilaterally.

#### B. *Supporting Hong Kong, Role Model for Taiwan, and the Construction of the "Greater China Economic Circle"*

From the outset, the China-Hong Kong CEPA has been viewed as an arrangement "devised by China to bolster Hong Kong's battered economy after a prolonged downturn."<sup>71</sup> According to the *Wall Street Journal*, the considerations for supporting the incumbent Hong Kong administration chaired by Chief Executive, Mr. Tung Chee Hwa (who, it is said, was handpicked by Beijing) far exceed that of economic benefit, making CEPA almost a unilateral gift to Hong Kong.<sup>72</sup> Hong Kong's economy, since the former British colony's return to China, has been in the doldrums. As the *Asia Times* observed, "since Tung became chief executive in 1997, the city has suffered two recessions that have seen property prices fall by 60 percent. Unemployment is running at 8.3 percent – something unheard of in this once-vibrant financial hub."<sup>73</sup> On 1 July 2003, the Sixth Anniversary of the change of sovereignty in Hong Kong, half a million local residents marched along the streets to protest against the city authority. The direct cause was the so-called Article 23 Bill, a legislative proposal, which, if turned into law will make illegal treason, secession, sedition or subversion against the central government in the Mainland. The underlying causes, however, appear to include public disquiet over Tung's failure to rescue the Hong Kong economy.<sup>74</sup> It is against this background that the Chinese leadership decided to deliver CEPA as a "gift" to the unpopular Hong Kong government. This was shown in Chinese Premier Wen Jiabao's speech after the signing ceremony, saying that the "real gift [evidenced by CEPA] is the determination of the new Chinese leadership to strengthen the implementation of 'One Country, Two Systems', the principle of 'self-governance of Hong Kong people' and the Basic Law in Hong Kong."<sup>75</sup>

The importance of a politically stable and economically prosperous Hong Kong to China is, of course, not confined to the concern with Hong Kong alone. China's "One Country, Two Systems" policy was devised to apply to all the areas that were not previously within the original sovereignty of the 1949-established PRC - Macao, Hong Kong and Taiwan. As

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<sup>71</sup> Angela Mackay. "A Trade Bridge to the Mainland" *Financial Times* (31 December 2003).

<sup>72</sup> See Pottinger, *supra* note 70.

<sup>73</sup> Antoaneta Bezlova. "'One Country, Two Systems' under Fire" *Asia Times* (17 July 2003) available online: <<http://www.atimes.com>>.

<sup>74</sup> Bryan Walsh. "Will CEPA Make Any Difference" *Time [Asia]* Vol. 162 No.1 (14 July 2003) available online: <<http://www.time.com/time/asia>>.

<sup>75</sup> "Wen Jiabo Xiwang "Anpai" Neng Wei Xianggang Dailai Gengduo Shangji [Wen Jiabao wishes CEPA will bring more business opportunities to Hong Kong]" *Xinhua News Agency* (29 July 2003).

Taiwan is the only region which is not currently unified with the Mainland, the “One Country, Two Systems” scheme must prove workable at least in Hong Kong in order to be acceptable to the Taiwanese. The implication here is that, if Mainland China can “give” CEPA to Hong Kong, it can similarly afford the same to Taiwan, provided that Taiwan agrees to unify with China. In fact, a senior official of China’s Ministry of Commerce extended an offer of a closer economic partnership agreement to Taiwan in November 2003. Taiwan’s Mainland Affairs Council, however, swiftly refused the offer on the ground that such an agreement, a device for “One Country”, was not acceptable to Taiwan.<sup>76</sup>

The long-term goal of the closer economic partnership agreements, as noted by Chinese officials and academics, is to integrate the economies of Hong Kong, Macao and Taiwan and then establish the long proposed “Greater China Economic Circle”.<sup>77</sup> However, as Mainland China has become Taiwan’s largest market,<sup>78</sup> Taiwan’s need to integrate closer with the Mainland market is becoming increasingly urgent. Thus, although China’s discussions with the ASEAN nations, as well as, its recent offer to sign a Hong Kong-like CEPA with Taiwan have been met with “anxiety and skepticism”,<sup>79</sup> a “Greater China Economic Circle” is very likely to come into being. This will be the starting point for China to assert the economic superpower status.

### C. *Economic Security*

It has been argued that having one's own RTAs is a defensive strategy against the proliferation of other RTAs due to the fear of being “left-out”. This, supported by the proposition that European integration spurred the formation of NAFTA. In turn, NAFTA and the EEC contributed to the surge of RTA initiatives in the Asia-Pacific region. According to this view, RTAs are related to the economic security of participating countries, which Mansfield has defined as “the maintenance of given levels of welfare and state power through access to resources, finance and markets.” Mansfield observes that eroding hegemony, global recessions, and strategic interdependence provide strong incentives for countries to establish or enter into RTAs in order to help guarantee that their access to key foreign markets will not be curtailed and their competitiveness abroad will not be undermined.<sup>80</sup>

While China has not expressed fear of being “left-out”, this fear is real considering that all its major trading partners are presently involved in RTAs. China also needs a stable supply of raw materials and commodity components from Southeast Asian countries. China is now the world’s second largest energy consumer after the United States, and has witnessed dramatically increased imports of oil and natural gas. To meet its energy demands, China

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<sup>76</sup> “Dalu Yao Tai Qian CEPA; Tai Luweihui Fandui [CEPA offer to Taiwan by Mainland rejected by Taiwan’s Mainland Affairs Council]” *Phoenix TV News [China]* (13 November 2003) available online: <<http://www.phoenixtv.com/home/news/taiwan/200311/13/146119.html>>.

<sup>77</sup> “Dalu Yu Xianggang Qian CEPA Cu Liangan Jian Xin Jinji Hezuo Jizhi [Mainland-HK CEPA urges the establishment of new mechanism for cross-strait economic cooperation]” *China News Agency* (5 July 2003) available online: <<http://business.sohu.com/85/38/article210753885.shtml>>. See also Pan Hongqi. “CEPA Shi Fen Shenme Yang De Dali? [What kind of big gift is CEPA?]” *Beijing Youth Daily* (30 June 2003).

<sup>78</sup> See Taiwan trade statistics online: <<http://www.trade.gov.tw/stat>>.

<sup>79</sup> U.S., *China’s Growth as a Regional Economic Power: Impacts and Implications: hearing before the U.S.-China Economic and Security Review Commission (USCC)*, 108<sup>th</sup> Cong. (4 December 2003) (statement by Merritt T. Cooke), available online: <<http://www.uscc.gov>>. (hereinafter “USCC hearing on China as Regional Power”).

<sup>80</sup> E.D. Mansfield. “The Proliferation of Preferential Trading Arrangements” [1998] 42 J. Confl. Resolution 523.

therefore has the incentive to engage energy-rich countries, including ASEAN members. The fast growing Chinese economy has also increased China's reliance on ASEAN nations for commodities to support its export economy or status as "world factory",<sup>81</sup> not to mention the fact that ASEAN also represents an increasingly important export market for China.

#### D. *Wooing ASEAN for Regional Security and Influence*

As one commentator notes, "the ASEAN-China agreement is essentially politically motivated."<sup>82</sup> The essence of this statement is, following the fact that China's economic growth has probably outperformed every country in the world for over a decade and China is inescapably heading towards economic superpower status, China has assiduously pursued a strategy to transform its economic clout into political influence by practising "mature", "constructive", and "responsible" great power diplomacy.<sup>83</sup> At this time, China's main goal is to build political trust with its neighbors and other important players in the region, in order to strengthen regional security in favour of itself. The CAFTA proposal, especially the EHP which gives early unilateral concessions to ASEAN states, is likewise directed to allay fears of a "China threat" amongst China's weaker Asian neighbors, who have been suffering the loss of foreign direct investment and have been struggling to compete with China economically over the last decade.<sup>84</sup>

Competing with Japan (and even the United States) for regional leadership and influence is another concern. Thus the CAFTA proposal is widely regarded as a way of pre-empting the dominance of other powers in Asia.<sup>85</sup> Japan has engaged ASEAN since 1973.<sup>86</sup> Yet, largely because of Japan's deep-rooted "Look West" orientation, it has never seriously initiated a comprehensive cooperation programme with ASEAN other than direct investment in the region. Moreover, the Japanese economy's languishing growth in past years has encouraged Asian countries to look elsewhere for an engine of growth. As for the United States, it has been almost entirely occupied with the anti-terrorism campaign since September 11. In China's view, it is now probably the best time for it to rise up and take over a leadership position by stressing economic cooperation in its diplomacy. It is this

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<sup>81</sup> Currently China mainly imports resource- or agriculture-based products (minerals, pulp, wood, vegetable oil and sugar) for ASEAN countries. Growing now is the share of machinery and electrical components for assembly into final goods in China. China in recently has also been proactively in buying national gas and oil fields in Indonesia.

<sup>82</sup> Hadi Soesastro. "Dynamics of Competitive Liberalization in RTA Negotiations: East Asia Perspectives," (Paper presented to the PECC Trade Forum) April 2003, available online: <<http://www.pecc.org>>.

<sup>83</sup> *Supra* note 79 (statement of Bates Gill, Freeman Chair in China Studies, Center for Strategic and International Studies).

<sup>84</sup> In 1980-2000, China's accumulated net FDI totaled \$209 billion while ASEAN's accumulated net FDI totaled on \$172 billion for the same period. See Phar Kim Beng. "ASEAN and China's Regional Concerns" *Asia Times* (21 January 2003) available online: <<http://www.atimes.com>>. CAFTA can slow this trend by providing multinationals with more incentives to invest or stay in ASEAN while meanwhile continuing to enjoy the benefits of China's huge domestic market.

<sup>85</sup> Chua Lee Hoong. "China-ASEAN Trade Pact – A Landmark Agreement?" *Straits Times* (4 November 2002). See also Phar Kim Beng, *supra* note 84.

<sup>86</sup> *Ibid.*

economic cooperation which is in dire need by nations in the region, even long term U.S. allies Australia and New Zealand.<sup>87</sup>

E. *The Ultimate Goal: Quest for "Peacefully Ascendancy" to Great Power?*

In international relations, "how a country rises often has more drastic consequences for the world than the rise itself."<sup>88</sup> History and international relations scholars, such as Donald Kagan and Joseph Nye, have observed that since the era of the Greek city-states, rising powers have tended to destabilize the established international system as they seek to make the system serve their interest.<sup>89</sup> Conceivably, the incumbent superpower will employ all means it possesses, including resort to military means, to contain, deter, or stop the development of the rising power. Arguably, there has only been one instance in history that an emerging power rose to greatness without such a conflict. That is, when the United States supplanted Britain as the dominant global power in the early twentieth century.<sup>90</sup> Certainly, China appears to be playing this rising power role in the early twenty-first century. Clearly, given all the advantages possessed by the United States in various areas of technology, human and natural resources, population, and especially an efficient and effective legal and political institutional structure, the U.S. is not likely to be "replaced" by any other nation, at least not in the foreseeable future. But it is fairly possible that a rising power like China could grow as strong and great as the United States. This will literally cause the loss of status, on the part of the U.S. as a "single superpower". Furthermore, if a rising power exercises its strength in an aggressive, unilateral, and expansionist way, it will certainly damage the interests of other countries voluntarily or reluctantly engaged with it.

Aware that its growing strength as a potential superpower may cause concerns and even fears amongst other countries, Beijing's leadership has sought to soothe the worries of the international community. The aim is to give history a chance to witness a second peaceful emergence of a great power.<sup>91</sup> In a speech at Harvard during his U.S. visit in December 2003, Chinese Premier Wen Jiabao after describing China's ambitious plan for economic and social development, affirmed to the Americans that his country subscribes to the idea of "*heping jueqi*" (meaning "peaceful ascendancy").<sup>92</sup> To achieve this, he said, China needs "peaceful international development and a stable domestic development."<sup>93</sup> China's worldwide RTA movements, engaging primarily its Asian neighbors at this stage, is thus aimed at expanding its political influence through peaceful economic exchange and cooperation.

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<sup>87</sup> The effect of China's "economic incentive" diplomacy, as I so call it, can be seen in Chinese President Hu Jintao's visit to Australia and New Zealand in October 2003. Local media hailed Hu's friendly gesture and policy declaration focusing on economic cooperation and political dialogue, and contrasted that with U.S. President Bush's almost sole concentration on security and anti-terrorism.

<sup>88</sup> Yoichi Funabashi. "China's Long-Term Strategy: Peaceful Ascendancy" *The Asahi Shimbun* (2 December 2003) available online: <<http://www.asahi.com>>.

<sup>89</sup> See Douglas H. Paal. "The Regional Security Implications of China's Economic Expansion, Military Modernization, and the Rise of Nationalism," in Hung-mao Tien and Tun-jen Cheng eds. *The Security Environment in the Asia-Pacific* (Taiwan: The Institute for National Policy Research, 2000) at 80.

<sup>90</sup> *Ibid.* at 90.

<sup>91</sup> A Japanese Newspaper has noted a researcher at a state-sponsored think tank in Beijing commented that "China aims to grow and advance without upsetting existing orders" and the Chinese "are trying to rise in a way that benefits our neighbors." See Yoichi *supra* note 88.

<sup>92</sup> "Remarks of Chinese Premier Wen Jiabao: Turning Your Eyes to China" *Harvard University News* (10 December 2003) available online: <<http://www.harvard.edu>>.

<sup>93</sup> *Ibid.*

#### IV. THE LEGAL ASPECT: WTO CONSISTENCY OF CHINA'S RTAs AND THE INADEQUACY OF WTO LAW

##### A. *The Need for WTO Compliance*

In theory, any WTO member's regulations and state activities relating to trade shall comply with WTO rules. As mentioned earlier in this article, by accession to the WTO, China has committed itself to abide by all the rules of the multilateral trading system. Violation of which will be considerably detrimental to both its own credibility, as well as, that of the WTO. Thus, China's RTA policy, to the extent that international obligations are involved, would seek to conform with WTO rules, provided there are relevant and meaningful WTO provisions in place.

The framers of the CEPAs and the China-ASEAN FA have, rhetorically, been prudent on the question of WTO compliance. One of the "General Principles" of the two CEPAs is "to be consistent with the rules of the World Trade Organization."<sup>94</sup> In the "Preamble" of the FA, the eleven countries bring their negotiations under the WTO framework by "reaffirming the rights, obligations and undertakings of the respective parties under the [WTO]"<sup>95</sup> In the main text of the FA, substantive WTO obligations are mentioned in eight places, covering a variety of areas including tariff reduction, trade remedy laws and services.

The presumption is, of course, that there must be something in the GATT/WTO that can be "complied with." The GATT/WTO regime is founded on a core principle: non-discrimination, which encompasses a "most-favored-nation" (MFN) rule and a "national treatment" rule.<sup>96</sup> More relevant to RTAs, is the MFN rule which according to the WTO Secretariat, "is so important that it is the first article of the [GATT]" as well as "a priority in the General Agreement on Trade in Services (GATS) and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)."<sup>97</sup> Basically, the MFN clause requires any Member of the WTO to extend unconditionally, "any advantage, favor, privilege or immunity" affecting customs duties, charges, rules and procedures they give to products originating in or destined for any other country.<sup>98</sup>

By definition, regionalism is at odds with the MFN clause. The draftsmen of the GATT and WTO were well aware of this and therefore, created several exceptions for RTAs. Under the current WTO regime, RTAs are subject to three sets of rules. The first is Article XXIV of GATT 1947 which, as clarified in the *Understanding on the Interpretation of Article XXIV* of the GATT 1994, provides for the formation and operation of customs unions and FTAs on trade in goods. The so-called "*Enabling Clause*", formally called the *Decision on Differential and More Favorable Treatment, Reciprocity and Fuller Participation of Developing Countries* passed by the GATT Council in 1979,<sup>99</sup> permits preferential trade arrangements in trade in goods between

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<sup>94</sup> See e.g., China-HK CEPA, Main Text, art. 2 (2).

<sup>95</sup> China-ASEAN FA, *Preamble*.

<sup>96</sup> General Agreement on Tariffs and Trade, 30 October 1947, 58 U.N.T.S. 187 at arts. I and III [hereinafter GATT].

<sup>97</sup> WTO Secretariat. *Understanding the WTO* (Geneva: World Trade Organization, 2003) at 10-11, online: <<http://www.wto.org>>.

<sup>98</sup> GATT, art. I(1).

<sup>99</sup> *The Decision on Differential and More Favorable Treatment, Reciprocity and Fuller Participation of Developing Countries*, (1979), GATT Doc. L/4903 [hereinafter the *Enabling Clause*].



developing country Members. Finally, Article V of GATS, entitled “Economic Integration”, governs the formation of RTAs in the area of trade in services.<sup>100</sup>

Are the above rules effective in terms of judging the WTO-consistency of any RTA? One commentator notes that “RTAs are generally WTO-consistent”, albeit “this is because the requirements of Article XXIV and the Enabling Clause and GATS are very weak and have never been enforced.”<sup>101</sup> This statement reveals the poverty of the WTO rules in containing regionalism, despite the WTO’s view that it is an adversary of the multilateral trading system. The following sections examine the problems associated with the relevant WTO rules concerning regional trade integration, with particular attention paid to China’s RTAs.

### B. *The Substantive WTO Requirements: The Rules and the Problems*

It is necessary to first identify the legal status of China’s accomplished RTAs (the two CEPAs) and the half materialized CAFTA (the FA) under the WTO law. GATT addresses two types of RTAs by drawing a distinction between custom unions (hereafter “CUs”) and FTAs. Additionally, GATT also governs the interim agreement leading to the formation of a CU or FTA. A CU, according to GATT Art. XXIV:8, is essentially an arrangement in which all participating countries adopt common external trade tariffs and eliminate substantially the trade barriers between themselves. China’s RTAs, however, belong to the second category; namely FTAs, the features of which are described as follows.

A Free Trade Agreement/Area (FTA) is a reciprocal arrangement whereby trade barriers between participating nations are abolished. However, each member determines its own external trade barrier against non-FTA members independently. Most commonly, barriers to trade are reduced over time and in most cases, not all trade is completely free of national barriers.<sup>102</sup>

The two CEPAs are apparently FTAs and the CAFTA FA is an interim agreement leading to the formation of a FTA. In China’s notification to the WTO Council for Trade in Goods and Council for Trade in Services regarding the CEPAs, they are described as “[establishing] a free-trade area within the meaning of Article XXIV of the GATT 1994 and [providing] for the liberalization of trade in services within the meaning of Article V of the GATS.”<sup>103</sup> The FA also makes its purpose clear, which is to establish a “China-ASEAN FTA within 10 years”<sup>104</sup>.

With regard to trade in goods, GATT has one general principle and two substantive rules governing RTAs. Paragraph 5 of GATT Article XXIV sets a principle for closer economic

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<sup>100</sup> *Marrakesh Agreement Establishing the World Trade Organization*, 15 April 1994, 1867 U.N.T.S. 3 at Annex 1B, art. V [hereinafter WTO Agreement].

<sup>101</sup> Peter Lloyd. “Implications for the Multilateral Trading System of the New Preferential Trading Arrangements in the Asia Pacific Region,” Paper presented at the PECC Trade Forum) November 2002 available online: <<http://www.pecc.org>>.

<sup>102</sup> Tim Martyn. *A Complete Guide to the Regional Trade Agreements of the Asia-Pacific* written for the APEC, March 2001, available online: <<http://www.apecsec.org>>.

<sup>103</sup> *Closer Economic Partnership Arrangement between China and Hong Kong, China, Notification from the Parties* (submitted on 12 January 2004), WT/REG162/N/1, S/C/N/264, and *Closer Economic Partnership Arrangement between China and Macao, China, Notification from the Parties*, (submitted on 12 January 2004), WT/REG163/N1, S/C/N/265.

<sup>104</sup> FA, art. 2.

integration between WTO Members, stating that “the purpose of a [CU] or of a [FTA] should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories.”<sup>105</sup> The two substantive rules are the “substantially-all-trade” (hereafter, “SAT”) requirement and the “not-on-the-whole-higher” (hereafter, “NWH”) requirement, embodied in GATT Article XXIV:8 and XXIV:5 respectively. In addition, pragmatically recognizing that a CU/FTA cannot come into being overnight, GATT also permits the formation of an interim agreement but states that it “shall include a plan and schedule for the formation of such [CU] or of such [FTA] within a reasonable period of time.”<sup>106</sup>

Simply put, GATT Article XXIV:8 requires that parties to CUs or FTAs eliminate “duties and *other restrictive regulations of commerce*” with respect to “*substantially all the trade*” between their constituent customs territories.<sup>107</sup> Short and simple as it is, this requirement has nonetheless caused major interpretative difficulties, which have even prevented the WTO itself from enforcing this provision. According to the Committee on Regional Trade agreements (hereafter, “the CRTA”), the WTO’s specialized agency for monitoring RTAs, two issues relating to this requirement have hindered the assessment of RTA’s fulfillment of relevant WTO law. These are, the meaning of SAT, and the scope of the list of “other restrictive regulations of commerce” (hereafter, “ORRC”).<sup>108</sup>

As early as 1995, the WTO Secretariat has noted that “differences of opinion among participants in working parties regarding the interpretation of the [SAT] requirement have been a major reason why working parties have not reached a consensus on the GATT consistency of individual agreements.”<sup>109</sup> Since the inception of GATT, there have been two approaches towards the interpretation of the SAT requirement. The first one, characterized as a “quantitative approach”, favors defining SAT as a statistical benchmark, such as, a certain proportion of trade between the parties, to indicate that the coverage of a given RTA fulfills this rule.<sup>110</sup> The problem with this approach is that “a single numerical definition or threshold” cannot suit the various different contexts in which the SAT requirement is used.<sup>111</sup> Worse, it can be easily taken advantage of to exclude sensitive sectors such as agriculture and textiles. The other interpretation, the “qualitative approach”, proposes that no sector (or at least no major sector) is to be excluded from intra-RTA trade liberalization.<sup>112</sup> Ironically, this approach might not automatically result in free trade even if it does include all sectors.<sup>113</sup> As noted by the CRTA, a number of suggestions have been proposed by Members of the WTO in an attempt to bridge or complement the two approaches.<sup>114</sup> However, no agreement has been reached.

The SAT requirement is further complicated by mention of the ORRC in Article XXIV:8. This paragraph states that, apart from the SAT requirement, WTO Members may still “where necessary” exercise their rights to maintain duties or restrictions under GATT

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<sup>105</sup> GATT, art. XXIV:5.

<sup>106</sup> GATT, art. XXIV:5(c).

<sup>107</sup> *Ibid.* at art. XXIV:8 (emphasis added).

<sup>108</sup> WTO, Committee on Regional Trade Agreements. *Synopsis of “Systemic” Issues Related to Regional Trade Agreement* (2 March 2000), WTO Doc. WT/REG/W/37 at para. 52.

<sup>109</sup> See *supra* note 5 at 13.

<sup>110</sup> *Supra* note 106, para. 54(a).

<sup>111</sup> *Ibid.*

<sup>112</sup> *Ibid.* at para. 54(b)..

<sup>113</sup> *Ibid.*

<sup>114</sup> *Ibid.* at para. 55.

Article XI (quantitative restrictions), XII (balance-of-payment exception), XIII (non-discriminative administration of quantitative restrictions), XIV (exceptions to the principle of non-discrimination), XV (exchange arrangements) and XX (general exceptions).<sup>115</sup> Members to RTAs cannot agree on other trade restrictive measures, such as antidumping, safeguard, or countervailing duties which are not mentioned in the list. What other measures should be incorporated into the list is a highly contentious question.<sup>116</sup>

The second substantive rule, the NWH requirement embodied in GATT Article XXIV:5, stipulates that in a FTA or interim agreement leading to a FTA, “the duties and other regulations of commerce” of the parties to the FTA in respect of trade with third parties “shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the [parties] prior to the formation of the [FTA], or interim agreement as the case may be.”<sup>117</sup> It has been generally recognized that Article XXIV:5 therefore governs “external” relations, while Article XXIV:8 deals with mainly the internal trade liberalization of CUs or FTAs. Again, the language used here is short but ambiguous enough to prevent the enforcement of the rule. Apart from highly disputable, undefined terms such as “higher or restrictive”, and “other regulations of commerce” (ORCs), one major problem is, whether, in order to determine if the NWH requirement is met, it is necessary that a country-by-country and product-by-product examination of the effect of increases in tariffs be undertaken. Heated debates have been generated since the GATT’s examination of the legitimacy of the Treaty of Rome which established the EEC. In addition, to date, no agreement as to how Article XXIV:5’s evaluation should be made has been reached among GATT/WTO officials and member-countries.<sup>118</sup> In one WTO case, *Turkey – Restrictions on Imports of Textile and Clothing Products*, a WTO panel indicated that Article XXIV:5(a) requires that the effects of the resulting trade measures and policies of the new regional agreement shall not be more trade restrictive, *overall*, than were the constituent territories’ previous trade policies.<sup>119</sup> In essence, the panel concluded that the terms of this provision “do not address the GATT/WTO compatibility of *specific measures* that may be adopted on the occasion of the formation” of a new RTA.<sup>120</sup> This conclusion, although shared by the Appellate Body, is not the end of the debate, at least in the sense that the WTO’s cases do not constitute legally binding precedents. Another very controversial and unresolved major issue relating to the NWH standard has been RTAs’ rules of origin (ROOs). Since the formation of the EEC, it has been debated in the GATT/WTO that ROOs of RTAs have been designed and administered in a way to create new trade barriers to their trade with third countries. An additional concern is that the absence of GATT guidelines on ROOs for RTAs have left RTA participants free to adopt whatever rules they may deem appropriate.<sup>121</sup>

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<sup>115</sup> GATT art. XXIV: 8(b).

<sup>116</sup> In fact, this problem has generated a good number of disputes before the WTO’s Dispute Resolution Body (DSB). See e.g., *Turkey – Restrictions on Imports of Textile and Clothing Products* (1999), WTO Doc. WT/DS34/AB/R; *United States – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea* (2002), WTO Doc. WT/DS202/AB/R; and *Canada – Certain Measures Affecting the Automotive Industry* (2000), WTO Doc. WT/DS139/AB/R, WT/DS142/AB/R.

<sup>117</sup> GATT, art. XXIV: 5(c).

<sup>118</sup> WTO Secretariat, *supra* note 5, at 14-15.

<sup>119</sup> *Turkey – Restrictions on Imports of Textile and Clothing Products* (1999), WTO Doc. WT/DS34/R at paras. 9.120-121 [hereinafter the panel report of *Turkey – Textile*].

<sup>120</sup> *Ibid.* at para. 9.122.

<sup>121</sup> WTO Secretariat, *supra* note 5 at 15.

Moreover, GATS Article V, the equivalent of GATT Article XXIV for services, is modeled closely on GATT Article XXIV. In the GATS, the “substantially-all-trade” ambiguity is only slightly abated, but by no means clarified. Most significantly, a RTA is required to have “substantial sector coverage,”<sup>122</sup> with the term “substantial” understood “in terms of number of sectors, volume of trade affected and modes of supply.”<sup>123</sup> Based on this, the requirement is, to not raise barriers to third countries and evinces a tighter standard. That is, it is applied sector by sector rather than “on the whole”. For a covered sector, “substantially all discrimination” is to be removed.<sup>124</sup> As observed by the CRTA, Article V has also caused many controversies and ambiguities but few have been clarified as a result of such controversy.<sup>125</sup>

### C. *The Notification and WTO Examination Process: Ill-Enforced Requirements*

All RTAs concluded by WTO Members require notification. The confusion and ambiguity caused by the relevant WTO notification rules is by no means less severe than the aforementioned substantive rules. GATT Article XXIV:7 indicates that any Member deciding to enter into a CU or FTA shall promptly notify the WTO Members “as will enable them to make such reports and recommendations to contracting parties”.<sup>126</sup> GATS Article V:7(a) contains a similar requirement. But the major issue is that “the time at which notification of RTAs should be made is neither precisely formulated nor homogeneously expressed in the rules.”<sup>127</sup> Most RTAs, in practice, are already in force long before the WTO is in receipt of notification, despite the requirement in GATT XXIV:7(a) that Members “shall promptly notify”. WTO Members have taken contrasting views with regard to the time of notification. One is that notification and submission of information should take place before entry into force. This will render most RTAs automatically illegal under the WTO law. The other is, that the lack of precision in the text implies a “regulatory forbearance” which reflects the “pragmatism” necessary to address complex negotiations for the formation of an RTA, especially in the context of the political difficulty of notifying agreements before ratification.<sup>128</sup>

Most notified RTAs have been interim agreements.<sup>129</sup> GATT XXIV:5(c) requires that these agreements include “a plan and schedule for the formation of a customs union or of a free trade area within a reasonable time.” However, no definitions to the key terms (“interim agreement”, “plan and schedule” and “reasonable time”) are provided. Such lack of consensus has led to controversy as to whether any particular interim agreement actually qualifies as such. Furthermore, with regard to an interim agreement, Article XXIV provides for the Contracting Parties (now the WTO Members) to make recommendations to the parties to the RTA, if after having studied the plan and schedule included in the interim agreement, they “find that such agreement is not likely to result in the formation of a [CU] or [FTA]” within a reasonable period of time. Accordingly, the parties shall not maintain or

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<sup>122</sup> GATS art. V:1(a).

<sup>123</sup> GATS art. V:1(a), fn. 1.

<sup>124</sup> GATS art. V:1(b).

<sup>125</sup> CRTA, *supra* note 108 at paras. 70-103.

<sup>126</sup> GATT art. XXIV:7(a).

<sup>127</sup> CRTA, *supra* note 108 at para. 12.

<sup>128</sup> *Ibid.* at para.13.

<sup>129</sup> WTO Secretariat, *supra* note 5 at 12.

put into force such an RTA if they are not prepared to modify it in accordance with these recommendations. As noted by John H. Jackson,

The interesting thing about this procedural language is that it does not require advance or later approval of the Contracting Parties of GATT. Instead, it places the initiative with the Contracting Parties to put forward recommendations for changes in the preferential agreement. This means technically, once the agreement has been notified to the GATT, unless the Contracting Parties can somehow arrive at an agreed set of recommendations, the language of GATT permits the preference parties to go ahead. The presumption is thus in favor of the preferential arrangement.<sup>130</sup>

Jackson further notes that, to his knowledge, “the Contracting Parties of GATT have never made an agreed set of recommendations to notifiers of preferential agreements.”<sup>131</sup> As a result, “many such arrangements have been entered into and operated which arguably do not fully comply with the policy goals and the intent and spirit of Article XXIV of GATT.”<sup>132</sup>

Naturally, this kind of situation leads people to question the work of the WTO’s Committee on Regional Trade Agreement (“CRTA”), which was established in February 1999 and charged with the principal duties, in particular to (a) oversee, under a single framework, all RTAs, and (b) consider the systemic implications of the agreements for the multilateral trading system and the relationship between them.<sup>133</sup> There is evidence to suggest that the CRTA has fulfilled its second mission, since it has released a number of valuable reports on this issue and instilled public awareness about the problems surrounding the difficulties imposed on the multilateral trading system by regionalism. However, the CRTA’s performance with regard to its first mission is an openly recognized failure. According to the committee’s 2003 Report to the General Council of WTO, by the end of 2003, the Committee has currently under examination of a total of 147 agreements, of which, “no progress was, however, made on the completion of the examination reports.”<sup>134</sup> In fact, no examination report has been finalized since the WTO’s establishment in 1995. The WTO Director-General, in a number of WTO Annual Reports, has concluded therefore that the CRTA has failed “so far in assessing the consistency of the ... RTAs notified to the WTO, due to various political and legal difficulties, most of which are inherited from the GATT years”<sup>135</sup> and that “since the establishment of the WTO, Members have been unable to reach consensus on the format, let alone the substance, of the reports on any of the examinations entrusted to the CRTA.”<sup>136</sup> As a result, the CRTA has, so far, never approved any RTA as WTO-consistent. Likewise, it has also never officially declared a single RTA to be in violation of GATT/WTO rules.

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<sup>130</sup> John H. Jackson. *The Jurisprudence of GATT and the WTO: Insights on Treaty Law and Economic Relations* (Cambridge: CUP, 2000) at 104.

<sup>131</sup> *Ibid.*

<sup>132</sup> *Ibid.*

<sup>133</sup> For the terms of reference of the CRTA, see WTO, *Decision on the Committee on Regional Trade Agreements of 7 February 1996*, WTO Doc. WT/L/127 available online: WTO website <[www.wto.org](http://www.wto.org)>.

<sup>134</sup> WTO, General Council, *Report (2003) of the Committee on Regional Trade Agreements to the General Council*, WTO Doc. WT/REG/13 (2003).

<sup>135</sup> WTO Secretariat. *WTO Annual Report 2002* (Geneva: WTO, 2002) at 114.

<sup>136</sup> WTO Secretariat. *WTO Annual Report 2003* (Geneva: WTO, 2002) at 111.

#### D. *So, is there the Need to Comply with WTO Rules?*

Theoretically, the answer is yes. After all, if a country is a Member of the WTO, the obligation to comply with the rules of the multilateral trading system is mandatory. However, a more useful answer is probably “no”, because of the reasons implied in the above analysis. To summarize, firstly, the WTO rules on the introduction of RTAs are troublesomely ambiguous and cannot be followed in an operational way. It is the inadequacy of the WTO rules that is principally to blame, as opposed to Members’ non-compliance (if any). Secondly, the nature of the WTO as a consensus-based institution prevents it from strengthening the enforcement of the existing rules. Roughly starting with the examination of the EEC, which was given up in early GATT days due to a clash of political interests, and was never picked up again. Although the reason behind the failure of enforcement is the divergent interpretations of WTO rules by Members, the real implication seems to be that almost no RTA can ever be declared unlawful under the current WTO regime and that the process of CRTA examination can, in practice, be ignored.

Experience shows that, to comply literally with GATT/WTO rules governing RTAs, Members, involved in RTAs, need only to notify the agreements to the WTO in a timely fashion either before or after their taking effect. Until the WTO substantially revises its rules governing regional economic integration, there is no imminent need for RTA members to worry about compliance with the substantive WTO requirements. In this sense, since China has already notified the WTO of its RTAs, it can be assumed that those RTAs are to be deemed compatible by the WTO unless the WTO can render adverse reports and recommendations.<sup>137</sup>

### V. A REALIST VIEW

#### A. *National and Regional Security as A Legitimate Goal in International Trade Relations*

In the absence of multilateral control through WTO rules, nations are free to pursue many goals in conducting regional integration through RTAs. The primary purpose of regional economic integration, according to a World Bank report, “is often political, and the economic consequences, good or bad, are side effects of the political payoff.”<sup>138</sup> Political benefits such as peace and security are, quite rightly, of paramount concern in the minds of the framers of many RTAs. This is based on the rationale that regions that are economically highly integrated tend to have less internal conflict. For example, the preamble to the 1951

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<sup>137</sup> There is a counter-argument saying that the legal status of RTAs in the WTO can be considered as remaining unclear, and thus WTO Members are preserved with the rights under dispute settlement procedures with regard to RTAs in any event. See WTO, Secretariat, *Compendium of Issues Related to Regional Trade Agreements*, WTO Doc. TN/RL/W/8/Rev.1(2002) at para. 24. This argument, however, does not go against the prima facie compatibility of an RTA. Furthermore, even though a RTA is challenged before the DSB for non-compliance with the WTO framework, the DSB, based on above analysis, does not possess the legal tools to examine the legal standings of RTAs vis-à-vis WTO rules. In *Turkey-Textile*, the panel observed that “it is arguable” that panels do not have jurisdiction to assess the overall compatibility of a customs union with the requirements of art. XXIV of GATT. In the end, the panel assumed *arguendo* that the arrangement between Turkey and the EC is compatible with the requirements of GATT art. XXIV:8(a) and 5(a). The Appellate did not address this issue. See *ibid.* at para. 27.

<sup>138</sup> World Bank. *Trade Blocs* (Oxford: OUP for the World Bank, 2000) at 11.

treaty establishing the European Coal and Steel Community states its aims, “to create, by establishing an economic community, the basis for broader and deeper community among peoples long divided by bloody conflicts.”<sup>139</sup> The founding fathers of the European Community (EC) even considered that economic integration would make war “materially impossible”.<sup>140</sup>

That trade fosters global peace is a long-established liberal conviction.<sup>141</sup> Theorists like Montesquieu and Kant and practitioners like Woodrow Wilson asserted that economic relations between states pacify political interaction. The literature of modern economics and international relations discloses that states fight for two reasons, and both are related to cost contests. Cost contests involve two elements. The first is that there is zero-sum competition for an “excludable good”. Secondly, states choose a settlement method, but the choice of method is typically, non-zero-sum. Liberal conviction is based on these two elements. Firstly, states fighting each other must have incentives to compete, which is often competition over an excludable good. States differ over such goods which each cannot possess simultaneously. Secondly, there is uncertainty as to the private information about strategic variables (capabilities, resolve, and so on) possessed by each state. If states could credibly share private information, efficient *ex ante* bargains could be identified. Uncertainty provides weak or unresolved states an opportunity to conceal weaknesses even as competition creates an incentive to bluff. Only by imposing costly contests, by military or similar measures, can states distinguish resolute opponents from those seeking to bluff. Furthermore, uncertainty also causes states to be unable to realize or overlook the likely consequences of their contests.<sup>142</sup>

Interdependence functions to promote peace in the sense that it helps remove incentives for states to engage in conflict. In addition, it serves to reduce the uncertainty states face when bargaining in the shadow of costly contests. The argument put forward by a group of international relations scholars is that “interdependence makes it easier to substitute nonviolent contest for militarized disputes in signaling resolve,” because “states that possess a range of methods of conflict resolution have less need to resort to the most destructive (and costly) techniques,” while “states without linkages must choose between a very limited set of options, including – more often – war.”<sup>143</sup> Specifically, based on empirical studies and quantitative analysis, the argument concludes:

Trade and direct investment increase cross-border economic contact and raise a state’s stake in maintaining linkages. Monetary coordination and interdependence demand that states strike deals. Though such interactions, states create a broad set of mutually beneficial economic linkages. While these linkages may deter very modest clashes, their main impact is as a substitute method for resolving conflict. Political shocks that threaten to damage or destroy economic linkages generate information, reducing uncertainty when leaders bargain. Threats from interdependent states carry more weight than threats from autarchic states precisely because markets inform observers as to the veracity of political “cheap talk.” Multiple channels of economic

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<sup>139</sup> *Ibid.* at 12.

<sup>140</sup> *Ibid.* at 13.

<sup>141</sup> Erik Gartzke *et al.* “Investing in the Peace: Economic Interdependence and International Conflict” [2001] 55 *International Organization* 391 at 394.

<sup>142</sup> *Ibid.* at 397-399.

<sup>143</sup> *Ibid.* at 400.

interactions help states to credibly communicate, increasing the “vocabulary” available to states in attempting to assess relative resolve.<sup>144</sup>

Despite many other concerns such as supporting Hong Kong and pursuing the “Greater China Economic Circle” (which is roughly a Chinese domestic matter), the major consideration behind China’s RTA approach lies in engaging its Asian neighbors for the sake of creating a peaceful and friendly regional environment for its economic development. China’s goal, however, not only coincides with that of its neighbors but serves a supreme interest in the region, which is peaceful existence and enhanced security.

Given East Asia’s warring colonized history, diverse culture, extremely fragmented ideological groupings, long existing borders disputes, and deeply rooted mistrusts in regional politics, it is an area where conflicts can be easily generated. Countries in East Asia, especially China and Korea, traditionally have a lingering mistrust of Japan because of its history of aggression. Recently, China’s rise as a regional and global power has brought fears to its neighbors, both economically and strategically. The conventional “China threat” theory has been in place for decades. Indeed, ASEAN was originally formed for the purpose of containing China when it was practising communism. However, the perception of a threat from the “dragon” (China) has persisted in contemporary intra-Asian regional politics. One major dispute between China and its southern neighbors is that they have all laid claim to the Spratly islands and the Paracel islands (called *nansha* and *xiasha* islands, respectively, by the Chinese) in South China Sea, which are of strategic and, potentially, economic importance. Since the 1970s, China had been involved in battles with Vietnam and has exchanged fire with the Philippines and Malaysia over the islands.<sup>145</sup> Given the PRC’s growing military might and uncompromised history in safeguarding its claimed territory, there is reason for China’s smaller and weaker neighbors to fear that the giant dragon may seek to resolve these disputes by force. This fear, in turn, can lead to political distrust, arms races, and eventually regional instability. Worse, China and its Asia neighbors would not be able share the benefits of each others’ fast growing economies.

RTAs, if managed well, are certainly capable of promoting peace and common security. A World Bank publication describes the role of RTAs in this regard,

[T]rade relations, including [RTAs] and, especially, deeper arrangement, might assist political relations between member countries by developing means for avoidance and management of intramural conflict. The negotiations between leaders of neighboring countries that are required to form and operate an [RTA] tend to generate trust between them. This helps them identify with each other, understand each others’ problems, and interpret each others’ actions. Trade talks allow political and economic elites to form coalitions from subsequent collaboration and consensual action.<sup>146</sup>

China’s recent RTA movement is based on this rationale that RTAs can be used as an instrument to strengthen friendship with its neighbors and enhance regional security, thus

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<sup>144</sup> *Ibid.* at 418.

<sup>145</sup> Jianming, Shen. “China’s Sovereign over the South China Sea Islands: A Historical Perspective” [2002] 1 Chinese JIL 94 at 100-101.

<sup>146</sup> Maurice Schiff & Alan Winters. *Regional Integration and Development* (Oxford: co-publication of the World bank and Oxford University Press, 2003) at 192.



-serving its long-term central task of economic growth and development of *zonghe guoli* (national strength). Observers widely hold the view that “there’s more than trade at stake.”<sup>147</sup> The geopolitical dimensions of China’s economic diplomacy imply that “for Beijing, cementing closer economic ties with neighboring East Asia states is also about establishing regional influence and leadership at the expense of the U.S. and other major economic powers,” and that “China ... hopes to form at some point a counter power comparable to the U.S. and Europe by unifying Asian countries.”<sup>148</sup> However, there is no reason to presume that China is the “wolf” taking advantage of innocent Little Red Riding Hood. Perhaps, more significant is that these economic-diplomatic measures put forward by China will also “lock in” China’s role as a promoter of regional stability. In the East Asia context, China’s RTA approach is closely accompanied by a host of other efforts to provide increased support for and participation in regional security mechanisms. In November 2002, China co-signed the *Declaration on the Conduct of Parties in the South China Sea* with ASEAN, which reaffirms China’s respect for and commitment to freedom of navigation in and overflight above the South China Sea “provided for by the universally recognized principles of international law”,<sup>149</sup> and which reiterates the principle that parties should “resolve their territorial and jurisdictional disputes by peaceful means, without resorting to the threat or use of force ... In accordance with universally recognized principles of international law.”<sup>150</sup> Furthermore, on 8 October 2003, in response to ASEAN’s decade-long plea, China, becoming the first country outside ASEAN to do so, acceded to the *Treaty of Amity and Cooperation in Southeast Asia*, a dispute settlement procedure established by ASEAN in 1976. This legal treaty commits China to use peaceful means to resolve territorial disputes.<sup>151</sup> In addition, China is obliged to not “participate in any activity which shall constitute a threat to the political and economical stability, sovereignty, or territorial integrity” of other signatory states.<sup>152</sup> This series of strategic moves, according to an American observer, is underlined by the intent to “ease ASEAN fears that China has territorial designs on the South China Sea claims of littoral ASEAN members.”<sup>153</sup> But more significantly, they contribute to the creation of an environment of peaceful co-existence between China and Southeast Asia with an almost determinative effect given the fact that China is in a good position to destroy unilaterally stability in this area. Evidently, China’s past behaviour, very different from the current approach and based on restrained unilateral acts and insistence on bilateral (rather than multilateral) talks, has caused grave concern among ASEAN members. China’s new move has certainly been embraced by its smaller neighbors. Notably, after China’s accession to the Treaty of Amity, ASEAN’s spokesman interpreted the ASEAN understanding of China’s motivation as follows,

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<sup>147</sup> Michael Vatikiotis & Murray Hiebert. “Free Trade Agreement: China’s Tight Embrace” *Fast East Economic Review* (17 July 2003).

<sup>148</sup> *Ibid.*

<sup>149</sup> *Declaration on the Conduct of Parties in the South China Sea*, between the Governments of the Member States of ASEAN and the Government of the People’s Republic of China, 4 November 2002, Phnom Penh, Cambodia, art. 3. Available online: ASEAN website <[www.aseansec.org](http://www.aseansec.org)>.

<sup>150</sup> *Ibid.* at art. 4.

<sup>151</sup> *Treaty of Amity and Cooperation in Southeast Asia*, signed on 24 February 1976 and amended in 1987 and 1998, respectively, art. 2 (hereinafter TAC). Available online: ASEAN website <[www.aseansec.org](http://www.aseansec.org)>.

<sup>152</sup> *Ibid.* at art. 10.

<sup>153</sup> USCC Hearing on China as Regional Power, *supra* note 79 (statement of John J. Tkacik, Jr., research fellow in China Policy, the Heritage Foundation).

China needs a favorable environment in the region to continue its economic development, which is not inconsistent with ASEAN's strategic needs...China wants to be seen as a responsible member of the international community, a country that is prepared to follow the rules accepted by the international community...[On the part of ASEAN,] there is no other way to deal with China but to engage it in regional process. China is important as a neighbor politically, in terms of security and is also important as an emerging economic power.<sup>154</sup>

B. *Regional Integration and Multilateral Liberalization: the Moral Obligation to Ensure RTAs as Building Blocks*

Regional integration through free trade agreements has been shadowed by heated debates featuring regionalism versus multilateralism. At the core of the debates are the costs and benefits of regionalism. The classic model for analyzing the economic effects of regional trade arrangements is still Jacob Viner's scholarship on the concepts of trade diversion and trade creation.<sup>155</sup> Viner explains how RTAs (including FTAs and CUs) have opposite effects on welfare or income. Trade creation takes place when, as a result of the removal of tariffs on intra-area trade, domestic production of a good is displaced by imports from another member of the RTA, whose comparative advantage enables it to produce the goods at a lower cost. On the other hand, the preferential tariff rate established by a RTA might cause trade diversion, defined as a shift of production away from a lower-cost producer outside the RTA to a higher-cost source of supply within it.<sup>156</sup> Viner concludes that, apparently, the formation of a RTA will lead to improvement in economic efficiency and welfare if trade creation exceeds trade diversion. An opposite effect, harmful to economic efficiency and welfare, will be generated if trade diversion exceeds trade creation.<sup>157</sup>

Viner's main contribution was to show that the formation of a RTA is not necessarily welfare-improving, or, using the more enthusiastic words of the eminent economist Jagdish Bhagwati, "to destroy the common fallacy that a preferential move toward (total) free trade was necessarily welfare improving and thus to demonstrate that all preferential paths to (total) free trade were not monotonic in welfare."<sup>158</sup> Following Viner, an enormous amount of literature on the benefits and costs of RTAs was generated. The modern version of the debates focuses on whether RTAs serve as a "stumbling block" or "building block" to multilateral trade liberalization. Bhagwati asserts that RTAs are by definition discriminatory and thereby trade diverting. While maintaining that trade diversion is likely to occur when a RTA is formed, he also argues that a RTA is inherently unhealthy even for its members because they are led by the RTA rules to engage in wasteful, discriminatory trade practices rather than trade induced by healthy market preferences.<sup>159</sup> Both Bhagwati and Anne O. Krueger, another prominent opponent of RTAs, cite RTA rules of origin ("ROOs") as a

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<sup>154</sup> Isaqani de Castro. "China snuggles up to Southeast Asia" *Asia Times* (7 October 2003) available online: <<http://www.atimes.com>>.

<sup>155</sup> Jacob Viner. *The Customs Union Issue* (Carnegie Endowment for International Peace 1950).

<sup>156</sup> Grimwade, *supra* note 2, at 237-38.

<sup>157</sup> *Ibid.*

<sup>158</sup> Jagdish Bhagwati. *The World Trading System at Risk* (Hemel Hempstead, Herts:Harvester Wheatsheaf: 1991), at 59.

<sup>159</sup> Jagdish Bhagwati. "Multilateralism and Regionalism in the Post-Uruguay Round Rea: What Role for the US?" in O. Memedovic ed. *Multilateralism and Regionalism in the Post-Uruguay Round Era: What Role for the Eu* (Kluwer: 1999) at 34.

negative product of RTAs. They claim, for example, that the ROOs in one RTA, more than likely would not coincide with the ROOs in many of other RTAs. Eventually, the incongruity of these different regulations governing the same subject matter could create a customs administration nightmare and lead to a “spaghetti-bowl” phenomenon.<sup>160</sup>

The many exponents of RTAs question the assumptions of Bhagwati and his fellows in this academic battle. Economist Robert Z. Lawrence argues that the theory traditionally applied to RTAs (by Bhagwati, Krueger, and others) is too narrow to be applied to recent RTAs such as NAFTA, which involve far more economic integration than the elimination of tariffs and thereby have led to a reduction in barriers on services trade, investment, and other areas.<sup>161</sup> He concludes that these dynamic welfare enhancing characteristics of RTAs are likely to outweigh any trade diversionary effect.<sup>162</sup> But even for RTAs in general, both traditional tariff-reduction RTAs and modern more comprehensive RTAs, Lawrence Summers suggests that they are generally favorable tools for trade liberalization because of the following propositions. Firstly, under the existing structure of trade, plausible regional RTAs are likely to have trade creating effects that exceed their trade diverting effects. Secondly, even trade diverting RTAs are likely to increase welfare. Thirdly, RTAs have other beneficial effects in addition to their impact on trade. Finally, reasonable RTAs are as likely to promote global liberalization as to slow it down.<sup>163</sup>

Obviously, the literature on the costs and benefits of RTAs does not offer conclusive answers on whether, in general, trade creation will exceed trade diversion or *vice versa*. It is, however, important to note that there is no major dispute as to the final goal: multilateral trade liberalization. The controversy is all about whether RTAs set up forces that encourage or discourage the evolution toward globally freer trade. In his highly regarded writing of 1996, economist C. Fred Bergsten praises the multilateral approach as follows,

The global approach is fundamentally superior because it maximizes the number of foreign markets involved and avoids the economic distortions (and political risks) of discrimination among trading partners. Indeed, the succession of GATT “rounds” throughout the postwar period has made a major contribution to the freeing of global trade.<sup>164</sup>

Bergsten nevertheless argues that RTAs, in lieu of multilateral trade negotiations, are the next best things. In contrast to the many deficiencies of the multilateral approach, the regional approach turns out to be less time-consuming and less complicated in reaching meaningful results. Moreover, RTAs often serve the priority national security concerns of countries involved.<sup>165</sup> Hence, a less controversial position, or perhaps even a common point, agreed by both sides of the debate is that “the economic impact of regional arrangements depends on their particular architecture, including how far they go in reducing trade barriers

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<sup>160</sup> *Ibid.* at 36.

<sup>161</sup> U.S. Congressional Research Service, William H. Cooper. *Free Trade Agreements: Impact on U.S. Trade and Implications for U.S. Trade Policy* (Washington D.C.: The Library of Congress, 2002) at 12.

<sup>162</sup> *Ibid.*

<sup>163</sup> Lawrence H. Summers. “Regionalism and the World Trading System,” in Jadish Bhagwati ed. *Trading Blocs: Alternative Approaches to Analyzing Preferential Trade Agreements* (Boston: MIT, 1999) at 562.

<sup>164</sup> Institute for International Economics, C. Fred Bergsten. “Competitive Liberalization and Global Free Trade: A Vision for the Early 21<sup>st</sup> Century” Working Paper No. 96-15 available online: < <http://www.iie.com> >.

<sup>165</sup> *Ibid.*

and how many sectors they cover.”<sup>166</sup> Bhagwati recognizes that Viner’s model can lead to the conclusion that “preferential moves can indeed be welfare improving. It just depends on the parameters.”<sup>167</sup> A World Bank special report on trade regionalism concludes, “Whether or not trade diversion dominates trade creation depends on the specific circumstances.”<sup>168</sup>

The supreme principle is that a RTA should be designed, with appropriate policy choices, to supplement multilateral trade liberalization. This principle is not inconsistent with the aforesaid position that national and regional security is a legitimate goal to pursue in regional economic integration. There is no inherent conflict between pursuing security in a RTA and setting up the RTA to be friendly to global-scale trade liberalization which we value.<sup>169</sup> When we admit that regionalism is only “second-best”, it is important to keep in mind that its general structure should not be inconsistent with a policy that eventually meets the needs for “first-best.” There is, however, a balance to be struck. On one hand, the international trade regime should make itself ready to embrace the seemingly unstoppable trend of regionalism. On the other hand, an international trade policy should be formulated to encourage RTAs to achieve trade creation and avoid trade diversion, both for the sake of members and to minimize harm to third-countries. The bottom line is, RTAs should not be used for protectionist purposes.

Leading trade powers, such as the United States, EU, and China, have the responsibility to ensure that their regionalist policies, which are actively pursued by all of them, serve as “building blocks” for multilateral trade liberalization. The arguments of both the proponents and opponents of RTAs all should be credited to the extent that they have pointed out the positive and negative aspects of RTAs in the world trading system. The technique is easy to express but probably difficult to implement. Using a Chinese idiom, it is to *yangchang biduan*, maximizing favorable factors and minimizing unfavorable ones.

The United States has been a leader of free trade since World War II. Yet, till 2001, the U.S. had only two FTAs (the U.S.-Israel FTA and NAFTA) and neither was initiated by itself. In the following years, however, the U.S. has been proactively involved in bilateral trade talks, having signed FTAs with Jordan, Singapore, Chile, Australia, and a number of Central and South America countries. However, as one commentator notes, “most of these [FTA] deals ... are unlikely to have a major impact on the gigantic U.S. economy, given the amount of additional trade at stake: Singapore, for example, is a city-state of more than 4 million whose dynamic economy is already largely open.”<sup>170</sup> Obviously, the U.S. is implementing a strategy which can be characterized as “competitive liberalization”. This term was (allegedly) coined by Bergsten in his 1996 article which argues, in essence, that RTAs will trigger a wave of liberalization towards global free trade as nations compete to open their market to one another by joining RTAs due to the fear of being left-out”.<sup>171</sup> It is

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<sup>166</sup> WTO Secretariat. *World Trade Report 2003* (Geneva: WTO, 2003) at 62.

<sup>167</sup> Bhagwati, *supra* note 158 at 59. However, Bhagwati qualifies this recognition by two further points relevant to GATT art. XXIV. First, for a RTA to be welfare improving, it is not necessary that regional trade liberalization be 100 percent. A less amount of reduction in trade barriers can also lead to welfare improving. Second, with the progressive cut of tariff (eventually towards zero) in a RTA, the gain from trade creation is less, while the probability of loss from trade diversion was increased. See *ibid.* at 60.

<sup>168</sup> *Trade Blocs*, *supra* note 138 at 61.

<sup>169</sup> Bergsten argues that “regional and global liberalization initiatives have mutually reinforcing throughout the past three decades or more” and that “the fears of some observers that regionalism would derail globalism have been demonstrably overcome.” See Bergsten, *supra* note 164.

<sup>170</sup> Paul Blustein. “U.S., Singapore Near Pact on Trade: Talks Are First of Many Bush Administration Plans to Purse for Bilateral Deals” *Washington Post* (20 November 2002).

<sup>171</sup> *Ibid.* See also Bergsten, *supra* note 164.

no secret that Washington's aim in regionalism is to induce other major players in world trade, including the EU, Japan and the coalition of a large number of developing countries, to compete within the broader, multilateral agenda of the WTO, momentarily the Doha Round. The U.S. is also riding a bicycle; at the same time, it does not cease to press the other trading powers to act in multilateral talks. At the beginning of January 2004, United States Trade Representative (USTR) Robert Zoellick wrote to the trade ministers of the other 146 WTO Members, in which he indicated that "the U.S. does not want 2004 to be a lost year for the Doha Development Agenda" and suggested ways to advance the negotiations in 2004.<sup>172</sup> With his "common sense" proposal, Zoellick traveled all over the world one month later and embarked on a global push to make strong progress in 2004 on multilateral trade negotiations.<sup>173</sup> The trip, which earned the support of many countries, including China, on a variety of sensitive issues which had collapsed during the WTO Cancun Ministerial Conference in 2003, will hopefully bring a restart of the Doha Round negotiations.<sup>174</sup>

The above example does not necessarily suggest that the U.S. is sincerely devoted to multilateralism. As a matter of fact, the U.S. has been criticized for its overuse of aggressive unilateralism for many years. The implications for China, however, are that trading powers, while pursuing regionalism to cure the deficiencies of multilateralism, should not lose sight on the multilateral approach towards global free trade. China became the world's fourth largest trading nation in 2002 and its third largest importer in 2003.<sup>175</sup> Like the U.S., EU and other lead trading powers, China also plays an important role in shaping international trade policy. In addition, China's traditional role as a leader of Third World suggests that its behaviour will likely have an impact on the trade policy orientation of other developing countries. As a rising power which appears willing to shoulder a larger global responsibility, China should take a pragmatic RTA approach which balances its national objective with multilateral trade liberalization. The proposed China-ASEAN Free Trade Agreement (CAFTA) should be designed in a fashion that helps this balance. Such a balance is very likely to be achieved if the RTA framework is constructed with the following considerations in mind.

1. *A sound international trade policy has two faces.*

First, it should be pragmatic enough to accommodate the security needs of trading nations, as long as those needs do not go against positive international law. In the East Asian context, in particular with respect to China and its neighbors, economic interdependence through integration has become essential for each individual country's security needs as well as for regional stability. There is no inherent conflict between these two goals. As noted by the World Bank report referred to earlier, even though RTAs can arise for essentially political reasons, there are strong returns to ensuring that they are set up with economic efficiency in mind. Only efficient, economically sustainable RTAs can help solve political problems, while a wasteful or divisive RTA could only produce opposite effects in the long run.<sup>176</sup> In the case

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<sup>172</sup> United States Trade Representative, Press Release. "Zoellick Embarks on Global Push to Make Strong Progress in 2004 on the Doha Trade Negotiations" (8 February 2004) available online: <<http://www.ustr.gov>>.

<sup>173</sup> *Ibid.*

<sup>174</sup> *Ibid.* See also, United States Trade Representative, Press Release. "Transcript of Ambassador Robert B. Zoellick, U.S. Trade Representative Press Conference" (12 February 2004) available online: <<http://www.ustr.gov>>.

<sup>175</sup> See WTO, News Release, 2004 Press/373, "World Trade 2003, Prospects for 2004" (4 April 2004).

<sup>176</sup> See Schiff & Winters, *supra* note 146 at 264.

of China's RTAs with its neighbors, various authoritative studies show that the economic returns are strong and obvious. The ASEAN-China Experts' Group's report on the feasibility of CAFTA suggests that "an ASEAN-China FTA will increase ASEAN's export to China by 48 percent and China's exports to ASEAN by 55.1 percent. The FTA increases ASEAN's GDP by 0.9 percent or by US\$ 5.4 billion while China's real GDP expands by 0.3 percent or by US\$ 2.2 billion in absolute terms."<sup>177</sup> The larger welfare-improving effect of China's RTAs was also confirmed by a policy study of the United Nations Conference on Trade and Development, which uses the gravity model and the computable general equilibrium (CGE) model, two basic models in economics, to assess the empirical effects of RTAs.<sup>178</sup> According to the study, for example, the simulation results of both models suggest the proposed Japan-Korea FTAs have negative coefficients in all the experiments conducted except for agriculture. However, expanding this arrangement to include China has resulted in a positive estimated coefficient on trade integration between these economies, strongly significant in both manufacturing and overall merchandise. Therefore, this suggests that "a bloc centred on China might be beneficial".<sup>179</sup> Further expanding the arrangement to include ASEAN also results in highly significant increases in positive efficiencies.<sup>180</sup> These results provide economic legitimacy for China and its neighbours' RTA initiatives in the region, even if these initiatives are themselves politically driven.

2. *The moral, but not legal, obligation to pursue multilateral liberalization in regional initiatives.*

As discussed above, multilateral liberalization is in the long-term interest of trading nations. However, because the process of pursuing multilateralism is too long and arduous, and the associated benefits might even be remote, and if in certain areas the collective action mechanism for global liberalization could not be established (to avoid the free-rider problem), countries should be allowed to pursue the "second best" approach which improves the economic welfare of the parties involved. After all, the world trading system does not require trading nations to be deontological; they are merely obligated to comply with the positive legal rules in the system. Apart from this long-term, yet probably remote interest, countries can pursue the benefits of liberalized trade on a smaller scale as long as the detrimental effects are limited and not obvious. This can be characterized as trading nations' "mid-term" interest.<sup>181</sup> In case trade diversion outweighs trade creation, the economies can still go ahead with a RTA as long as it enhances the mid-term economic welfare of their countries. Theory and practice suggest that RTAs combining only small economies are likely to be trade diverting.<sup>182</sup> However, especially for developing countries which have desperate needs to achieve development, RTAs should be assessed on the basis

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<sup>177</sup> The ASEAN-China FTA Report, *supra* note 7 at 31.

<sup>178</sup> UNCTAD. *Assessing Regional Trade Arrangements in the Asia-Pacific*, Policy Issues in International Trade and Commodities, Study Series No. 15, U.N. Doc. UNCTAD/ITCD/TAB/16, U.N. Sales No. E.01.II.D.21 (2001).

<sup>179</sup> *Ibid.* at 18.

<sup>180</sup> *Ibid.*

<sup>181</sup> In the analytical framework of this article, the long-term interest, referring to the eventual goal of global trade liberalization, is certainly the goal without major dispute. The mid-term interest is worth pursuing because the benefits are obvious and damage to other members of the international trade community are non-obvious, limited, and not a result of international legal obligations. The short-term interest refers to those benefits which can be achieved at the expense of massive environmental damage, human rights violations, or direct violations of the positive rules of international trade law.

<sup>182</sup> Schiff & Winters, *supra* note 146 at 263.

of national objectives and criteria, not according to whether they satisfy the relevant WTO articles or the purposes of the multilateral trading system. In the rare case where there is a conflict, meeting the purpose (not necessarily positive laws) of long-term multilateral liberalization is probably only an abstract, moral obligations while meeting the objectives of economic development would become a more urgent need.

3. *Promoting rules convergence as a way of promoting multilateral liberalization.*

The well-known imprecision and ambiguity of GATT Article XXIV in particular and GATS Article V, as well as, the inability of WTO Members to reach consensus on the interpretation of these articles, has led to deadlock where there is no universally accepted understanding of all the important provisions in the articles. The effect is that members are, in practice, left with a broad discretion to unilaterally adopt their own interpretations of the disputed provisions. While this situation is clearly undesirable, the decisive movement toward its reform is not likely to be achieved in the near future, given the complexity of extracting sufficient political will from WTO Members. For individual WTO Members, who are willing to ensure that the RTAs they are involved in are consistent with the spirit of the multilateral trading system, one of the best things they can do is to promote rule-convergence and to minimize “spaghetti bowl” problems through harmonization and adoption of common rules. This is especially so, in highly divergent but crucial areas such as rules of origin, customs valuation, trade facilitation, and investment. Where there are relevant WTO provisions in place, the RTAs should follow those rules as closely as possible. In other areas where WTO rules are in absence, international standards or “best practices” should be developed and adopted. China and its RTA partners are now in the best position to contribute to the convergence approach because most of the RTAs involving them are still at the negotiating stage.

## VI. CONCLUDING REMARKS

China’s recent RTA initiatives, contributing significantly to the proliferation of regional trade arrangements, should be viewed in a broad context encompassing the country’s and its neighbours’ economic, political and security concerns. Like other RTAs, this could run at odds with the goal of the multilateral trading system, although it is equally likely to supplement the process of multilateral trade liberalization. The ideal way is to use multilateral trading rules, embodied in the WTO regime, to control the direction of regionalism and minimize the adversary effects of multilateralism. The existing WTO rules, including mainly GATT Article XXIV and GATS Article V, are evidently weak, ambiguous and almost completely unenforced. Legally, it could be argued that WTO Members should be free to pursue a particular goal through trading behavior in the absence of positive WTO rules which prohibit it. Taking a realist view, the point of this article is that China’s RTA approach is just another example of how the international trade system should be pragmatic enough to accommodate the vital security needs of trading nations, in the absence of prohibitive WTO rules. This is especially crucial in the East Asian context given its history and geopolitical layout, for example, China’s complex political and military role in the region. An alternative route in East-Asia, without even politically driven regional integration could be much less effective for promoting regional prosperity and stability. However, trading nations, especially leading trade powers like China, have a moral obligation to ensure that their RTAs serve as “building blocs” for multilateral trade liberalization through promoting rule convergence.

Yet, I would not suggest putting this moral obligation above national objectives as there are no international legal obligations to compel this.