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

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

- WTO Members are subject to several general obligations set out in WTO agreements
- i.e
  - the MFN, NT, principles
  - The market access principle also dictates that members are required to act in accordance with their scheduled commitments on tariffs and not to apply tariffs beyond the bound levels unless these are renegotiated.
  - Members are not generally allowed to impose quantitative restrictions (QRs) on market access for goods.
  - Members are required to ensure that their non-tariff barriers (NTBs) (such as customs formalities) do not constitute unnecessary obstacles to trade.

- Nevertheless, in certain circumstances, **WTO Members may derogate from these obligations, provided that they comply with certain conditions**
- **They include the following**
  - **General exceptions -** Right to take measures, for example, necessary to protect human, animal or plant life or health, which may restrict trade in goods (GATT 1994).
  - **Security exceptions -** Right to take measures to protect essential national security interests, which may restrict trade in goods (GATT 1994).
  - **Exceptions for Regional Trade Agreements (RTAs)** Right to depart from the MFN principle in order to grant preferential treatment to goods (GATT 1994) or service suppliers (GATS) from trading partners within a customs union or a free trade area without extending such treatment to all WTO Members;
  - **Balance-of-payments (BOP)** – Right to take measures to safeguard a Member's external financial position and its BOPs; and,
  - **Waivers -** Temporary waivers granted with the authorization of the other Members, in exceptional circumstances.

EXCEPTIONS	ARTICLES	
General Exceptions	Article XX of the GATT 1994	Article XIV of the GATS
Security Exceptions	Article XXI of the GATT 1994	Article XIV*bis* of the GATS
RTAs	Article XXIV of the GATT 1994; and "Understanding on the Interpretation of Article XXIV of the GATT 1994" Paragraph 2(c) of the Enabling Clause*	Article V of the GATS
BOPs	Articles XII & XVIII:B of the GATT 1994; and, "Understanding of the BOPs Provisions of the GATT 1994"	Article XII of the GATS
Waivers	Article IX:3 of the Marrakesh Agreement Establishing the WTO (WTO Agreement establishing the WTO)	

- Note also that members can also take trade remedies (**trade defence mechanisms**) like anti-dumping, countervailing and safeguard measures

GENERAL EXCEPTIONS

- **GENERAL EXCEPTIONS IN THE GENERAL AGREEMENT ON TARIFFS AND TRADE (GATT) 1994**
- Article XX of the GATT 1994 permits Members to take certain measures, otherwise prohibited by GATT 1994 provisions, subject to stipulated conditions.
- The purpose of Article XX is to ensure that commitments undertaken by the Members under the covered Agreements do not hinder the pursuit of legitimate policy objectives, **such as the protection of human, animal or plant life or health, or the conservation of exhaustible natural resources.**
- In this regard, the Appellate Body Report has stated that the exceptions listed in **Article XX -paragraphs (a) to (j) relate to all of the obligations under the GATT 1994** (including not only the MFN and national treatment principles, but others as well)

- **In general, there are two steps in the application of Article XX exceptions under the sub-paragraphs**
  - **A. Identify whether the policy pursued through the measure falls within the range of policies provided in sub-paragraphs (a) to (j) of** Article XX, for example, designed to protect human, animal or plant life or health (XX(b)), to secure compliance with laws or regulations which are not inconsistent with the provisions of the GATT 1994 (XX(d)), or to conserve exhaustible natural resources (XX(d)) (see also box below).
  - **B. Determine whether the legal elements of the relevant paragraph are met. This examination comprises, for example, the "necessity test" for paragraphs (b) and (d), and the analysis if a measure "relates to" for paragraph (g).**

LEGAL TEXT	*LEGAL ELEMENTS*
Article XX (b): Necessary to protect human, animal or plant life or health	(1) the policy in respect of the measures for which the provision is invoked falls within the range of **policies designed to protect human, animal or plant life or health**; and, (2) the inconsistent measures for which the exception is being invoked is "**necessary**" to fulfil the policy objective.

Article XX (d): Necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including (...)	**(1) the measure must be one designed to secure compliance with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994; and,** **(2) the measure must be "necessary" to secure such compliance.**
Article XX (g): Relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption	(1) the measure is concerned with the **conservation of exhaustible natural resources**; (2) the measure "**relates to**" the conservation of "exhaustible natural resources"; and, (3) the measure **is made effective in conjunction with restrictions on domestic production or consumption**.

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

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

"smoking constitutes a serious risk to human health and that consequently measures designed to reduce the consumption of cigarettes fall within the scope of Article XX(b)"

SECURING COMPLIANCE WITH LAWS OR REGULATIONS WHICH ARE NOT INCONSISTENT WITH THE PROVISIONS OF THE GATT 1994 - ARTICLE XX(D)

- A measure can be said to be designed ''to secure compliance'' when it is suitable or capable of securing compliance with the relevant laws and regulations, even if the measure cannot be guaranteed to achieve its result with absolute certainty.

CONSERVATION OF EXHAUSTIBLE NATURAL RESOURCES - ARTICLE XX(G)

- In *US - Shrimp*, the Appellate Body held that the text of Article XX(g) **covers not only the conservation of "mineral" or "non-living" natural resources, but also living species**, which are in principle "renewable", and are in certain circumstances indeed susceptible of depletion, exhaustion and extinction, frequently because of human activities

SPECIFIC REQUIREMENTS UNDER ARTICLE XX(B), (D) & (G)

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

- Paragraphs (b) and (d) of Article XX set forth a "**necessity test**": the measures at issue must be necessary either "to protect human, animal or plant life or health" (XX(b)) or to "secure compliance with laws or regulations" (XX(d)).
- the Appellate Body stated that the reach of this word is not limited to what is "indispensable" or "of absolute necessity" or "inevitable".
- The term "necessary" refers to a range of degrees of necessity.
- At one end of this continuum lies "necessary" understood as "indispensable"; at the other end, is "necessary" taken to mean as "**making a contribution to**".
- The contribution must not be "**marginal or insignificant**"

- **The "Necessity Test " under paragraphs (a), (b) and (d) of** Article XX **of the GATT 1994**
  - The "**necessity test**" involves a process of "weighing and balancing" a series of relevant factors, in particular:
    - The contribution made by the measure to the achievement of its objective;
    - the importance of the interests or values at stake;
    - the trade-restrictiveness of the measure.
- In addition, the measure has to be compared with **possible available alternatives**, which may be less trade restrictive while providing an equivalent contribution to the achievement of the objective.

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

- "RELATING TO..."
- The Appellate Body stated that a measure would qualify as "relating to the conservation of natural resources" if the measure exhibited a "substantial relationship" with, and was not merely "incidentally or inadvertently aimed at" the conservation of exhaustible natural resources.

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

- According to the Appellate Body, this is a requirement that the measures concerned impose restrictions, not just in respect of imported products at issue but with respect to domestic products at issue.

- Measures covered by an exception be not administered in a manner that would constitute:
  1. **Arbitrary discrimination between countries where the same conditions prevail;**
  2. **Unjustifiable discrimination between countries where the same conditions prevail; or,**
  3. **A disguised restriction on international trade.**
- The purpose and object of the Chapeau is generally the **prevention of abuse of the exceptions of Article XX**.

"ARBITRARY OR UNJUSTIFIABLE DISCRIMINATION BETWEEN COUNTRIES WHERE THE SAME CONDITIONS PREVAIL"

- In order for a measure to be applied in a manner which would constitute "arbitrary or unjustifiable discrimination between countries where the same conditions prevail", **three elements** must exist.
  - First, the application of the measure must result in discrimination.
  - Second, the discrimination must be arbitrary or unjustifiable in character.
  - Third, this discrimination must occur between countries where the same conditions prevail

Example: Finding on "Arbitrary or Unjustifiable Discrimination" – *US – Shrimp* Case

- The US imposed an import ban on shrimps or shrimp products through Section 609 except for those harvested either under conditions that do not adversely affect sea turtles or in waters subject to the jurisdiction of a nation currently certified
- The Appellate Body found that the measure was "related to" the conservation of exhaustible natural resources, and therefore was covered by Article XX(g)
- However, while examining whether the US measure satisfied the requirements of the Article XX Chapeau, **the Appellate Body Report found that the ban constituted "arbitrary" and "unjustifiable" discrimination**.

- In its finding of "unjustifiable" discrimination (whether the measure at issue discriminated between those countries that had been certified and, consequently, could export shrimp to the US and those non-certified countries that were subject to the import ban) the Appellate Body found the following omissions:
  1. **The failure of the US to engage in serious negotiations across-the-board** - the US failed to engage in serious negotiations with all the Members exporting shrimp to the US with the objective of concluding bilateral or multilateral agreements for the protection and conservation of sea turtles.
  - Before enforcing the import ban- while the US negotiated with some Members, it did not negotiate with other Members

2. **lack of flexibility of the measure**– the measure did not take into account the different situations which may exist in different exporting countries.

- The measure required "*essentially the same*" regulatory program to exporting Members as that adopted by the US

"A DISGUISED RESTRICTION ON INTERNATIONAL TRADE"

- **Three criteria** have progressively been introduced by GATT/WTO jurisprudence in order to determine whether a measure is a disguised restriction on international trade:
  - **Whether the contested measure is published or not** – In *US – Gasoline*, the Appellate Body considered that concealed or unannounced restriction in international trade does not exhaust the meaning of "disguised restriction"
  - **the consideration of whether the application of a measure also amounts to arbitrary or unjustifiable discrimination**
  - **the examination of "the design, architecture and revealing structure" of the measure at issue**

SECURITY EXCEPTIONS

- A WTO Member is allowed to take any action which it considers **necessary for the protection of its essential security interests** or in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.
- Members are not required to furnish information, the disclosure of which would be contrary to their essential security interests.
- Article XXI of the GATT 1994 ("Security Exceptions") allows Members to take certain measures, otherwise prohibited by the GATT 1994, to protect essential security interests.

- Article XXI has three paragraphs (a), (b), and (c), which provide the following:
  - **Paragraph (a)** refers to the disclosure of information that the WTO Member would consider contrary to its essential security interests.
  - **Paragraph (b)** prescribes the condition under which a Member may take any action it considers "necessary for the protection of its essential security interests" including those relating to:
  - fissionable materials or the materials from which they are derived;
  - the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purposes of supplying a military establishment;
  - taken in time of war or other emergency in international relations.

  - **Paragraph (c)** allows Members to take actions in pursuance of their obligations under the United Nations (UN) Charter for the maintenance of international peace and security. This is a reference to Chapter VII of the UN Charter.

- Article XXI does not contain an obligation for Members to notify measures taken pursuant to the Security Exception.
- For trade in services, the relevant provision is Article XIV*bis* of the GATS. The wording of Article XIVbis of the GATS is almost identical to Article XXI of the GATT 1994 (explained above), which governs the security exceptions for trade in goods, and the concepts do not differ in both instances.
- However, unlike Article XXI of the GATT 1994, under the GATS there is an obligation to notify the measures taken under the security exceptions for trade in services.

REGIONAL INTEGRATION

- WTO Members are allowed, under certain conditions, to **depart from the MFN principle in order to grant preferential treatment** to their trading partners **within a customs union or a free trade area**, without extending such treatment to all WTO Members.
- Article XXIV **of the GATT 1994 and** Article V **of the GATS** allow WTO Members to depart from the MFN rule to grant more favourable treatment to their trading partners within a customs union or a free trade area without extending such treatment to all WTO Members, subject to certain requirements.

BALANCE-OF-PAYMENTS (BOPS) EXCEPTIONS

- Under WTO rules, Members are allowed under certain circumstances and subject to specific conditions, to adopt import restrictions otherwise inconsistent with the WTO rules in order to **safeguard their external financial position and their balance-of-payments (BOPs)**.
- Article XII and Article XVIII:B of the GATT 1994
- **Article XII can be invoked by all Members and Article XVIII:B only by developing country Members**

- **Balance of payments (BoP)** accounts are an accounting record of all monetary transactions between a country and the rest of the world.
- **It registers a countries transactions with all countries in a given year**.
- It is divided in to two broad categories
  - **The current account**
  - **The capital account**
- **The current account records all current payments made by and to the country in connection with international transactions**
- The current account divides these international transactions in to four sub categories
  1. **Trade account:-** which registers all payments made in connection with imports and exports of goods
  2. **Service account**:-registers all payments in connection with imports and exports of service sector activities such as, banking services, insurance, consulting, transportation, tourism , construction etc…
  3. **Income account**:- registers all incomes gong out of and in to a country in connection with Royalties, licensing fees, interest payments etc…
  4. **Unilateral transfers accounts:-**all unilateral transfers from a country and vice versa ex. Remittances, foreign aid expenditures

- Payments made to the country are recorded as credit items, and payments out of the country are recorded as debit items.

❖ **Capital Account:**

- Registers **financial flows** between a country and the rest of the world.
- For example any time an **Ethiopian buys foreign stock, a bond or even a factory in another country, this expenditure is registered as a capital outflow.**
- **Each time a foreigner purchases an Ethiopian financial asset , the expenditure is considered as a capital inflow**
- Capital outflows are registered as negative and capital inflows are registered as positive items in the capital account.

Current Account	
Trade in Goods	
Imports	-1,224,417
exports	772,210
Trade in services	
Net Military transactions	500
Net travel and transportation receipts	3,180
Other services net	72.788
Balance of Goods and services	-375,739
Income receipts	352,866
Income Payments	-367,658
Balance on Income	-14,792
Unilateral Transfers	-54.136
Balance on current account	**-444,667**
Capital Account	
Total US owned assets abroad	-580,952
US official reserve assets	-290
Other US government assets	-944
U.S private assets	-579,718
Foreign owned assets in the US	1,024,218
Foreign official assets	37,619
Other foreign assets	986,599
Balance on Capital Account	**443,266**
Overall Balance (statistical discrepancy)	**-1,401**

BOP= Current Account + Capital Account

- In the above statistics, USA run a balance of payment deficit of 1.4 Billion USD in 2000.
- **A countries current and capital accounts should be mirror images of each other i.e when a country runs current account deficit, it has to have a capital account surplus and vice versa.**
- **The presence of a current account deficit means that a country's total expenditure in a given year ,expenditures in goods and services, on investment in factories and houses and on all other domestic and foreign products are larger than its total income.**
- **In the case of USA this means that in 1999 American residents as a group spent 331.5 billion USD more than they earned**.
- **Residents of a country can spend more in a year if residents of other countries are willing to lend them a portion of their income.**
- The capital account surplus finances the current account deficit.

- If people in other countries are not willing to advance loan, a country will not face deficit and the first country will have no current account surplus.
- **Current account surplus of one country is a result of its willingness to grant loans for one country. Otherwise, the residents of the deficit nation will not purchase goods and services of the surplus country.**
- **The emergence of a large current account imbalance in one country will always be accompanied by a large offsetting imbalance in another country.**
- Ex. For the last 20 years, large American current account deficit have been accompanied by large current account surplus in Japan.
- **The current and capital account must balance i.e the sum has to be zero**
- But there is no assurance that the hundred and thousands of uncoordinated international transactions that private individuals and businesses do will produce the balance.
- This is called **Balance of Payment Imbalance**.

- Balance of payment imbalance takes two forms
  - A. **Balance of payment deficit**: current account deficit is greater than the capital account surplus
  - B. **Balance of payment surplus**: the current account surplus is less than the capital account surplus
- When such imbalance happens countries must undergo **balance of payment adjustment**
- **Balance of payment adjustment refers to policy measures and economic processes that eliminate the imbalance in countries international trade and financial positions.**
- **There are three different ways** used by governments to correct deficit or surplus of their balance of payment

1. **Restriction of international transactions**: this is the simplest method. Ex. Reducing imports through raising tariffs or non tariff trade barriers. This contravenes WTO rules though the GATT allows suspension of trade liberalization measures in the case of large balance of payment deficit.

2. **Changing the Exchange Rate**:- Ex. **Currency devaluation** which makes locally produced goods cheap and increases exports. (this reduces foreign price of domestic goods and raises domestic price of foreign products)

- Conversely a country with surplus can revalue its currency.
- Though this is less disruptive than trade restrictions, frequent exchange rate changes heighten uncertainty and depress international trade and investment.

3. **Changing Domestic Economic Activity**: this method requires governments to use **macro economic policies to influence domestic economic conditions.**

- **Macro Economic Policy**: refers to efforts made by the government to influence **aggregate economic activity** in the national economy such as the rate of economic growth, the rate of inflation, the level of unemployment etc..
- **Governments basically use two policy instruments to implement its macro economic policy.** There are **Fiscal Policy and Monetary Policy**

- **Fiscal policy** refers to the tax and spending measures that governments adopt.
- An **expansionary fiscal policy** such as tax cut and additional spending can raise the rate of growth and reduce unemployment.
- **Restrictive fiscal policy** : such as a reduced government expenditures or tax increase will most often reduce economic growth and increase unemployment.
- **Monetary policy:** which is conducted by a countries central banks concerns money supply and interest rates.
- **An expansionary monetary policy**:- reduces interest rates and increases money supply and thus boosts economic growth and reduces unemployment.
- **Restrictive Monetary policy**:- increases interest rates and reduce money supply in the market and in effect slows down economic growth, increases unemployment and inflation.
- If the country suffers from balance of payment deficit, the government must tighten fiscal and monetary policies (increase in interest, reduction of gov't expenditure, tax increase etc…).

- So by slowing down economic activity, restrictive macroeconomic policies will reduce the country's demand for imports, increase the amount of goods available for export and attract foreign capital in to the country.
- If the country suffers from balance of payment surplus, the government may expand fiscal and monetary policies. i.e interest rates must fall and the government must spend more or tax less and there by boost economic growth.
- More rapid growth raises the demand for imports, reduces exports and encourages domestic capital flow abroad.
- Though this mode of adjusting balance of payment has little effect on international economy, it may have substantial impact on the domestic economy.
- Countries with balance of payment deficits will have to accept higher unemployment as they adjust.
- And countries with balance of payment surplus will be forced to accept higher inflation as they adjust.

- Adjusting the imbalance in deficit countries is cumbersome and relatively easier in the surplus nations as surplus does not erode a country's foreign exchange reserves.
- **Since the surplus in on country is a necessary counterpart of the deficit in another country, and adjustment in one will rectify the other.**
- But a political conflict as to who should shoulder the cost of adjustment arises when ever the imbalance happens.
- The adjustment mechanisms has been different in the international monetary system over the past 100 years.
- **In gold standard era of the 19th and early 20th century, adjustment could occur through changes in domestic economic activities as exchange rates were fixed under the gold standard.**
- **In the Bretton woods system adjustment was done by a combination of changes in domestic economic activities and changes in exchange rates.**
- **In the contemporary monetary system, advanced industrialized countries basically rely on exchange rate changes and only in rare circumstances they alter domestic economic activities.**

WAIVERS

- A waiver is normally used when there are no other provisions which would allow a Member to derogate from a WTO principle or a specific provision.
- While there is no need to negotiate before adopting a general exception under Article XX of the GATT 1994 or Article XIV of the GATS, waivers shall be granted by three fourths of the Members, through a decision of the Ministerial Conference
- Consequently, in contrast to such exceptions, a waiver may be viewed as a "negotiated right".
- Waivers are temporary so, when they are granted, a definite time-period is set for termination.
- Moreover, if granted for more than a one-year period, a waiver must be reviewed annually to establish if the exceptional circumstances warranting its grant still exist