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# EU-ACP Economic Partnership Agreements (EPAs) Institutional and Substantive Issues

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# Abbreviations

A4T	Aid for Trade
ACP	African, Caribbean, Pacific
AGOA	African Growth and Opportunity Act
CAP	Common Agricultural Policy
CARICOM	Caribbean Community
Cariforum	Caribbean Forum of African, Caribbean and Pacific States
CEMAC	Communauté Economique et Monétaire de l'Afrique Centrale (Central African Economic and Monetary Community)
CET	Common External Tariff
CIF	Cost, Insurance and Freight
COMESA	Common Market for Eastern and Southern Africa
CTC	Change of Tariff Classification
CU	Custom Union
DG-Trade	Directorate General for Trade
EBA	Everything but Arms
ECDPM	European Centre for Development Policy Management
ECOWAS	Economic Community of West African States
EDF	European Development Fund
EEZ	Exclusive Economic Zone
EIB	European Investment Bank
EPA	European Partnership Agreement
EU/EC	European Union/Community
EUOT	EU Overseas Territory
FOB	Free on Board
FTA	Free Trade Area
GAERC	General Affairs and External Relations Council
GATT	General Agreement on Tariffs and Trade
GSP	Generalized System of Preferences
HS	Harmonised System
IMF	International Monetary Fund
ITC	International Trade Centre
LDC	Least-Developed Countries
MEP	Member of European Parliament
MERCOSUR	El Mercado Común del Sur (The Southern Common Market)
MFN	Most-Favoured Nation
MRL	Minimum Residue Level
NAFTA	North American Free Trade Agreement
NGO	Non-Governmental Organization
NIPs	National Indicative Programmes
OCTs	Overseas countries and territories

ORC	Other Rules of Commerce
PTA	Preferential Trade Agreement
RI	Regional Integration
RIPs	Regional Indicative Programmes
RoO	Rules of Origin
RPTFs	Regional Preparatory Task Forces
RTA	Regional Trade Agreement
SADC	Southern African Development Community
SDT	Special and Differential Treatment
SPS	Sanitary and Phytosanitary Standards
STABEX	Système de Stabilisation des Recettes d'Exportation
SYSMIN	Système de Stabilisation des Recettes d'Exportation de Produits Miniers
TBT	Technical Barriers to Trade
TR	Technical Requirement
TRA	Trade-Related Assistance
TRIPs	Trade-Related Aspects of Intellectual Property Rights
UNCTAD	United Nation Conference on Trade and Development
VA	Value Added
WAEMU	West African Economic and Monetary Union
WTO	World Trade Organization

# Introduction

Since 2002, the EU and ACP countries have been engaged in negotiating Economic Partnership Agreements (EPAs). These negotiations are based on the Cotonou Agreement, which *inter alia* defines the framework and modalities for the coming trade regime between the parties. According to the Cotonou Agreement, the negotiations shall be concluded by 31 December 2007. From this date, the existing non-reciprocal trade relation between the EU and ACP countries is supposed to be replaced with reciprocal trade relations in the form of free trade areas. In other words, in return for retaining preferential access to the EU market, ACP countries have to gradually open their own markets to the EU. However, as this report shows, this deadline will be difficult to meet – at least in some EPA regions.

Following a request by the Danish Parliament, DIIS and the Institute of Food and Resource Economics, Copenhagen University were requested by the Danish Foreign Ministry to conduct a literature review of the issues under negotiation, in order to identify the most important proposals by the Commission, ACP countries and third parties, to highlight the controversies around these proposals and, to describe the literature's assessment of their consequences. Within this mandate, the Institute of Food and Resource Economics was asked to review economic estimates of the impact of different EPA-based market access scenarios. DIIS's Trade and Development Research Unit was asked to review selection of other institutional and substantive issues within the negotiations. A joint report was presented to the Foreign Ministry in November 2007. Subsequently, the Institute of Food and Resource Economics and DIIS are publishing separately their own contributions to this report. The current publication is DIIS's contribution.

Following a Summary, the publication is organised into three sections. Section 1 (Chapters II.1-II.2) discusses the legal and institutional setting of EU-ACP and intra-ACP (regional) relations within which the negotiations are taking place. Section 2 (Chapters II.3-II.6) addresses a range of substantive issues that are addressed in the negotiations, and finally Section 3 (Chapters II.7-II.8) reviews the relation between aid and trade in the EPA negotiations.

The literature described and discussed in this publication dates from September 2007 and earlier. Because of a natural time lag between proposals being made in the negotiations and their discussion in the literature, most developments in the negotiations subsequent to May 2007 are not covered. These include the EU market access offer of May 2007 and its new offer on rules of origin of October 2007.

The views expressed in this report are those of the authors alone.





# SUMMARY

In reviewing all the involved and interested actors' contributions to the discussions concerning the political, legal and institutional context of EPAs, two distinct but interrelated areas of controversy may be identified. Firstly, a rather abstract controversy on the merit of reciprocal trade relation between the EU and ACP countries is identified. Here, while the EU advocates that the new era of trade relation, based on asymmetrical liberalization of trade, is in the ACP countries' own interests, many ACP countries supported by NGOs disagree and argue that ACP countries should continue to enjoy non-reciprocal market access to the EU, or at least be required to liberalize their trade regime over a long transitional time.

As Part I illustrates, almost all economic estimates show that, at least in the short term, many ACP countries will be negatively effected by the EU's demand for reciprocity. On the other hand, as the EU argues, the existing non-reciprocal trade relation between the countries is not WTO compatible and thus has to be changed (Chapter II.1). Faced with this situation, and as required by the Cotonou Agreement, the question becomes if and how the new trade relation can be both WTO compatible and at the same time not place ACP countries in a worse situation than under Cotonou. As Chapter II.1 concludes, these conflicting goals are difficult, if not impossible, to reconcile. It should be noted that according to the Cotonou, if any ACP decides to opt out of the EPA negotiations, the EU is mandated to explore and offer alternative arrangements. However, the alternative offered shall also be WTO compatible. The question whether there are any alternatives to EPAs, as free trade areas, and whether the EU has investigated the question in a satisfactory manner, is widely debated in literature. In this regard, Chapter II.1 argues that the legal primacy of WTO commitments over the trade rules obligations of Cotonou, and the fact that no ACP country has yet opted out of the EPAs negotiations, explains the absence of practical alternatives to EPAs.

A parallel set of abstract discussions concerns the regional dimension of EPAs (Chapter II.2). The regional as opposed to all-ACP aspect of EPAs, as well as the principle that ACP regional integration shall be trade-driven, reflect the strong wishes of the EU. A considerable part of the literature questions the latter assumption, in terms of the argument that developing country trade integration can be successful only if it builds on non-trade forms of economic integration. More concretely, controversy surrounds the viability of some of the six (now perhaps seven) regional configurations that have emerged during the negotiations on the basis of ACP country choices. In some cases this process has led to configurations where members' legal commitments will cut across those they already have under existing regional trade agreements.

Against this clouded background, a second broad area of controversy concerns the substantive issues, other than tariff liberalization, which are addressed in the negotiations across the different

EPA configurations – that is, the non-tariff related content of EPAs regardless of the above-mentioned institutional context. In this regard, there are not only several areas of controversy but also several axes around which it is occurring. Along the first axis (investment, anti-dumping and development assistance), the EU is internally in conflict. The internal conflict has several dimensions: disagreement between EU member states (Chapter II.8 on development assistance to ACP countries), disagreement between EU member states and DG Trade (Chapter II.6 on the absence of a Commission mandate to negotiate dispute settlement mechanisms regarding investment rules) and disagreement between DG Trade and DG Development (Chapter II.8 again, on the trade-development link within EPAs negotiations). Along the second axis, ACP countries are in conflict with each other (Chapter II.6 on their willingness to enter into negotiations with the EU on investment rules). Along the third, on almost all substantive issues, wide differences of opinion exist between the EU and the ACP countries, supported by NGOs and sometimes by academic analysts (Chapter II.3 on Rules of Origin, Chapter II.4 on anti-dumping rules, Chapter II.5 on sanitary and phytosanitary or SPS measures and Chapter II.7 on development benchmarks). The number and complexity of the resulting disagreements explain the apparent lack of progress in the negotiations.

More explicitly, Chapter II.3 describes the controversy on an appropriate EPA Rule of Origin methodology in terms of the EU's intention to generalize the use of a Value Added criterion as its preferred method of calculating the origin of traded goods, as against ACP countries' favouring of a Change of Tariff Classification criterion, which is said to be simpler and less restrictive. At the same time, academic studies differ in their estimation of the likely supply response to a significant change in Rule of Origin methodology.

Chapter II.4, on Trade Defence Mechanisms, especially anti-dumping measures, shows that the EU's current proposal is widely criticized, as it seems to allow only the EU to use such measures against ACP countries' exports. Chapter II.5, on SPS measures, shows that the main focus of debate is shifting from provision of new legal remedies to the EU's introduction of allegedly disproportionate measures towards how to best support the improvement of ACP capacity for conforming to EU as well as other international standards. In this regard, the ACP countries are currently focusing mainly on obtaining enhanced technical assistance for upgrading their public capacity in SPS.

Chapter II.6, on WTO-plus issues, shows that – of the original range of issues raised by the EU at the WTO Singapore Ministerial – only investment rules remains a subject of negotiation in the EPA context, and that even this issue has not been discussed in a detailed manner. However, the discussions that have occurred, illustrate a basic disagreement between the EU and the ACP on the potential merits of such rules for attracting investment and on whether ACP countries have adequate resources either to negotiate the issue in the first place or (if such rules are adopted) to administer them in an effective way.

In order to neutralize any potential losses entailed by entering into an EPA and, more importantly, in order to be able to fully utilize the potential gains that such an agreement may offer, ACP countries have emphasized that trade liberalization shall be linked to promotion of development, and that the development impacts of EPAs shall be measured and monitored. However, as Chapter II.7 illustrates, differences exist between the EU and ACP concerning the main focus of monitoring efforts and what the resulting assessments should be used for. Meanwhile, the ACP itself has yet to reach agreement on which benchmarks to use.

Another aspect of the relation between trade and development is the question of development assistance, which is addressed in Chapter II.8. Here, while requesting additional resources for meeting adjustment costs and building domestic supply capacity, all ACP regions express frustration over the EU's explicit omission of development assistance from the formal negotiations. Controversies here concern the level and scope of support that will be made available alongside EPAs and the mechanisms for its delivery, as well as the process by which assistance is linked to EPA implementation (even if it is not formally linked to the negotiations themselves).



# 1. EPAs, Cotonou and the WTO

## – Legal Dimensions

This section is a review of the discussions on legal issues concerning the EPA negotiations by the negotiating parties, NGOs, academics, and other commentators. The theme of these discussions concerns one major controversy with three parameters. The controversy is on the apparent conflict between establishing WTO compatible EPAs (i.e. reciprocal trade agreement) and offering ACP countries a trade regime which is equivalent to their existing situation (non-reciprocal trade agreement) while respecting their development status and needs (flexibility). Thus the three parameters in this controversy are: flexibility, reciprocity, and the possible combination of these two shaping possible alternatives to the EPAs.

This controversy stems from Cotonou Art. 37.6, which states that ‘In 2004, the Community will assess the situation of the non-LDCs which, after consultations with the Community decide that they are not in a position to enter into economic partnership agreements and will examine all alternative possibilities, in order to provide these countries with a new framework for trade which is equivalent to their existing situation and in conformity with WTO rules’ (emphasis added). Cotonou itself is silent on the modalities for solving the conflict, the criteria that the alternatives have to fulfil, and what ‘examine’ as stated in the Article shall mean.

Art. 37.6 needs to be read in combination with Art. 37.7, which, states that ‘Negotiations of the economic partnership agreements shall aim notably at establishing the timetable for the progressive removal of barriers to trade between the Parties, in accordance with the relevant WTO rules. ... Negotiations shall take account of the level of development and the socio-economic impact of trade measures on ACP countries, and their capacity to adapt and adjust their economies to the liberalisation process. Negotiations will therefore be as flexible as possible in establishing the duration of a sufficient transitional period, the final product coverage, taking into account sensitive sectors, and the degree of asymmetry in terms of timetable for tariff dismantlement, while remaining in conformity with WTO rules then prevailing’ (emphasis added).

In short, these two subparagraphs require EPAs to be:

- WTO compatible;
- Reciprocal;
- Flexible;
- While at the same time preserving the ‘existing situation’ of the ACP countries.

Within the reviewed literature, a disagreement between EU on one side and ACP countries supported by NGOs on the other side is evident, in relation to what these criteria should mean and what determines their fulfilment (see e.g. Borrmann, Grossman et al 2005; Christian Aid 2005). The conflict can be summarized as EU requiring reciprocal EPAs and finalization of negotiations by the end of 2007 in order to comply with the WTO requirements, while the opponents, as the sub-title in a report by Oxfam states, 'request a change of approach, more time, and a transition regime' (Oxfam and TWN Africa 2007: 3). According to the opponents, the EU is 'placing undue pressure on ACP countries to conclude EPA negotiations in 2007. The EC is using the threat of lower market access to force the hands of ACP negotiators, which would represent a breach of the EU's obligations under the Cotonou Agreement' (ibid: 17). More explicitly the following points have been raised:

- The required liberalization of ACP countries' trade regime is contrary to their development policy and will undermine their economies; and
- The EU has not fulfilled its obligation under Cotonou to examine and offer alternative arrangements to the ACP countries.

## WTO CONFORMITY AND RECIPROCITY

EU-ACP trade relations have traditionally been governed by EU granting different forms of non-reciprocal trade schemes resembling or improving upon GSP to the ACP countries. But according to Cotonou, this has to change, which means that EU-ACP trade relations shall be WTO-compatible and thereby lead to reciprocal EPAs (Martenczuk 2000). As Martenczuk states, Cotonou attempts 'to set out objectives and principles that will guide ACP-EC development cooperation well into the 21<sup>st</sup> century. At the same time, it represents a major overhaul of instruments and policies in all fields of ACP-EC development cooperation' (ibid: 462). The main external reason for the replacement of Lomé with Cotonou and EPAs has been the WTO rulings in the so called Banana disputes, where parts of the Lomé Conventions were found to be WTO-incompatible because they favored ACP countries against other developing countries (Meyn 2006). The current trade regime between EU and ACP countries is based on a WTO waiver obtained in 2001, which runs until 31.12.2007. From that date, WTO-compatible EPAs are supposed to enter into force.

According to the EU, 'the aim of the EPAs is to reduce trade barriers between the ACP countries themselves and between the ACP countries and the EU and also to increase cooperation in all areas relevant to trade' (Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung 2007: 1). In other words, ACP countries are supposed to reduce their tariffs in return for market access to the EU. According to the EU, this reciprocity secures compatibility of the EPAs with WTO rules and principles. Legally speaking, this argument is based on GATT Art. XXIV.8.b, which states that 'A free-trade area shall be understood to mean a group of two or more customs territories in which

the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories' (emphasis added). However, according to the EU, reciprocity within EPAs is to be 'asymmetrical, thus taking account of the development status of the ACP countries. The instruments to be used for this are long transition periods and exclusion of sensitive products for the ACP countries' (ibid: 2).

Many NGOs and ACP countries argue that reciprocity in itself is contrary to many ACP countries' developmental goals and policies, and EPAs shall 'have sustainable development as a central objective and include the principle of non-reciprocity' (Oxfam 2005: 2). The argument for this is that ACP countries' trade liberalization would inter alia cause revenue reductions and damage these countries' industries and as such is against the objectives of the Cotonou Agreement, as stated in Cotonou Art. 1 (Christian Aid 2004). Thus as a joint memorandum by UK NGOs calls on the EU to drop 'both its demands for offensive issues and its demand for reciprocity in EPA negotiations' (UK NGOs 2004). Instead, EU must focus on further opening its own market to ACP countries (Oxfam 2006b). Other commentators argue that the potential impact of reciprocity on ACP countries depends on what 'substantially all trade' means, and the 'amount of asymmetry available to ACP countries' (PricewaterhouseCoopers 2007) or, as Stevens and Kennan write, 'ACP countries will have a certain degree of choice because they will not need to liberalise all their trade imports, only 'substantially all'. Moreover the tariff cuts that are made will be introduced over a transitional period which is likely to be at least 12 years and, if the recent Africa Commission recommendation were adopted, could be as long as 20 years' (Stevens and Kennan 2005a: 5).

In short, although commentators may disagree on their recommendations, they agree that reciprocal EPAs impose real problems for many ACP countries, especially African ones. In this connection, some protagonists call for alternatives to EPAs that are both flexible and WTO compatible (UK NGOs 2004; African Union 2007). According to Cotonou, it is the EU's responsibility to examine and offer such alternatives. The EU, on the other hand, claims that reciprocity is part of Cotonou and that there are no alternatives to reciprocal EPAs (see DG-Trade website [http://ec.europa.eu/trade/issues/bilateral/regions/acp/memo010307\\_en.htm](http://ec.europa.eu/trade/issues/bilateral/regions/acp/memo010307_en.htm)). However, in the literature some alternatives have been identified and they will be addressed below. These alternatives are:

- GSP schemes;
- Extension of the current waiver; and/or
- Changing the relevant WTO rules.

Against this background, the central questions that have been debated are: What does Cotonou require? What does WTO require? And whether there are any alternatives to reciprocal EPAs?

## WHAT DO COTONOU AND WTO REQUIRE?

As mentioned, Cotonou Articles 37.6 and 37.7 define the substantial criteria that EPAs have to fulfill. These criteria are:

1. Progressive removal of barriers to trade between the parties;
2. On the EU side, trade liberalization shall aim at improving current market access for the ACP countries;
3. Review of rules of origin;
4. Flexibility in establishing the duration of a transitional period;
5. Flexibility in final product coverage;
6. Flexibility in the degree of symmetry in tariff dismantlement; and
7. WTO conformity.

At the same time, WTO Article XXIV determines the criteria that a Free Trade Agreement shall fulfill in order to be WTO compatible. These are:

1. It must not raise barriers to trade for non-member countries;
2. It shall eliminate trade restrictions with respect to substantially all trade between the parties.

A central question is to what extent these two sets of criteria are complementary and to what extent they are contradictory. According to the WTO case-law, whether a Free Trade Agreement raises barriers to trade for other countries can be determined by economic modeling and may be subject of WTO's Dispute Settlement Mechanism. As the Appellate Body report in Turkey – Textiles (DS34) in Para. 55 states, 'an 'economic' test for assessing whether a specific customs union is compatible with Article XXIV' can be performed. However, since the EPAs have not been negotiated and their exact rules are still unknown, this section will not address this issue, but will focus on flexibility and reciprocal elimination of trade barriers between the member countries. In this regard, reference to GATT 1994 Art. XXIV is essential. Here the keywords are 'substantially all trade' and 'between the parties' (Lockhart and Mitchell 2005).

### Substantially all trade

As 'substantially all trade' has not been defined anywhere in the WTO, the only source of interpretation is the Appellate Body report in Turkey – Textile (DS34). Paragraph 48 of the report states that 'neither the GATT CONTRACTING PARTIES nor the WTO Members have ever reached an



agreement on the interpretation of the term 'substantially' in this provision. It is clear, though, that 'substantially all trade' is not the same as all the trade, and also that 'substantially all trade' is something considerably more than merely some of the trade. ... Thus we agree with the Panel that the terms of sub-paragraph 8(a)(i) offers 'some flexibility' to the constituent members of a customs union when liberalizing their internal trade in accordance with this subparagraph'. It should be stated here that this ruling clarifies Art. XXIV.8.i.a, which covers Custom Unions and not Free Trade Areas which are covered by Art. XXIV.8.b. However, since the terms 'substantially all trade' have a similar function in both subparagraphs and that the relevant difference between Custom Unions and Free Trade Areas in this connection is only on the origin of covered goods, it can be assumed that Appellate Body's interpretation of Art. XXIV.8.a.i can also be applied to Art. XXIV.8.b.

In this connection, EU understands 'substantially all trade' to cover almost 90% of total volume of trade.<sup>1</sup> As an example, the EU-South Africa FTA operates with this threshold (EU gives 95% of South African exports improved access to its markets, while South Africa does so for 86% of EU exports). It should be mentioned here that the remaining 10% can include whole sectors and goods, for example most agricultural products.<sup>2</sup>

### Between the parties

The next issue that has to be addressed is whether the requirement to eliminate trade restrictions in 'trade between the parties', as EU claims, amounts to one for reciprocity and if it does, how flexible a reciprocal EPA is permitted to be. The short answer to the first question is 'yes'. All commentators agree that 'between the parties' in the subparagraph implies reciprocity. This is supported by a contextual reading of this sub-paragraph together with the rest of Art. XXIV.

The answer to the second question about flexibility is less clear, as it is not addressed in the WTO nor in the case-law. Thus as it stands now, it is up to the negotiators to determine what flexibility means. The EPA negotiating parties seem to agree that flexibility refers to two issues. The first

<sup>1</sup> Within the on-going WTO negotiations on Art. XXIV, EU has also argued that 90% of volume of trade corresponds to 'substantially all trade'. In response, the US has claimed that 'substantially all trade' covers all sectors and products, leaving open the possibility of having some limits within them. The difference is that according to the US, all products shall be covered by a free trade agreement, whereas EU would exclude some products from the list. Since the Doha negotiations are not concluded, there is no consensus on this issue,

<sup>2</sup> During the EPA negotiations and in line with recommendations by most commentators, many ACP countries are in the process of defining which product groups should be exempted from reciprocal liberalization. Whether this list can be completed before the end of 2007 and whether it will be accepted by the EU, or become subject of further disagreement, time will show.

relates to the coverage of liberalized products and sectors (as stated above) and the second relates to when liberalization shall take place (the transition time).

Cotonou Art. 37.7. states that negotiations shall establish a 'timetable for the progressive removal of barriers to trade between the parties'. Here, the parties agree that ACP countries should have as long a transition time as possible. Thus the question is how long such a transition time can be. Cotonou makes explicit that the timetable shall be in accordance with the relevant WTO rules. Here the relevant WTO rule is Para. 3 of the Understanding, which defines 10 years as the 'reasonable length of time' except in 'exceptional cases', without specifying what constitutes exceptional cases. Based on this silence, it can be argued that free trade agreements between such unequal parties as in the case of EPAs can be regarded as 'exceptional cases'. This understanding can also be identified as an implicit factor in the EPA negotiations. Here, while ACP countries and NGOs request long transitional periods, EU has not proposed any explicit time-line.

In conclusion it should also be mentioned that according to Cotonou, EPAs should 'improve current market access for the ACP countries'. In this regard, the European Commission has recently proposed duty free and quota free access to EU markets for ACP countries (except for sugar and rice) upon entry into force of the EPAs ([http://ec.europa.eu/trade/issues/bilateral/regions\\_acp/pr240507\\_en.htm](http://ec.europa.eu/trade/issues/bilateral/regions_acp/pr240507_en.htm)). The only condition attached to the Commission's proposal seems to be conclusion of the negotiations by the end of 2007. It should be mentioned here that although this proposal was endorsed by EU member-states on 14 May 2007, it has been criticized by some EU countries including France, Poland, Ireland, Germany, and Italy for threatening 'the balance achieved in reforming the banana and sugar regimes' (Financial Times: 19 April 2007) and 'weakening the EU's position in a current legal dispute over bananas with Ecuador and Colombia at the [WTO]' (ibid.). This illustrates wider internal conflicts in the EU.

Since the negotiations are not progressing as fast as it was initially intended, many question what will happen if the EPA negotiations are not concluded by the end of 2007, when the WTO waiver expires (see e.g. Bilal and Rampa 2006; Stevens 2007), or if one or several ACP countries decide not to enter an EPA. This issue raises another central discussion: whether there are any alternatives to reciprocal EPAs.

## ALTERNATIVES TO THE EPAs

Cotonou Art. 37.6 states that 'in 2004, the Community will assess the situation of the non-LDC which, after consultations with the Community, decide that they are not in a position to enter into economic partnership agreements and will examine all alternative possibilities, in order to provide these countries with a new framework for trade which is equivalent to their existing situation and in con-

formity with WTO rules' (added emphasis).<sup>3</sup> There is disagreement concerning how this paragraph should be understood. Here two areas of discussions can be identified. The first relates to whether EU has honoured its obligation to examine all alternative possibilities. According to the EU, no ACP country has requested the EU to examine alternatives, and moreover there are no WTO-compatible alternatives, except the standard GSP scheme.<sup>4</sup>

The lack of WTO-compatible alternatives is supported by Meyn (2006), who states that 'Under current WTO condition [reciprocity and non-discrimination between developing countries] it must be ... regarded as doubtful that 'alternatives' exist' (Meyn 2006: 152). On the other hand, NGOs and some ACP countries criticize the Commission for not examining or offering any alternatives to reciprocal EPAs. As a number of NGOs in a letter to the German Presidency of the EU wrote 'there has been no serious consideration of alternative options to Free Trade Agreements, making it difficult for ACP countries to make informed choices as to what their best options would be' (Stop Unfair Trade 2007).

The second area of debate is more substantial and deals with whether any alternatives exist. As stated above, the Commission argues that there are no alternatives to EPAs other than the general GSP scheme. On the other hand, some NGOs have suggested three types of alternatives to the EPAs:

1. Continuation of current situation, with or without a new WTO waiver;
2. Preferential treatment of all ACP countries; and
3. Changing WTO rules in order to incorporate new S&DT aspects into GATT Art. XXIV.

#### Continuation of current situation

The first possible alternative to EPAs, which has been identified by NGOs and some ACP countries, is the continuation of the current situation with a new WTO waiver (Bassilekin 2007).

This suggestion has been raised because it seems that some of the six negotiation groups are not in

<sup>3</sup> It should be mentioned that in 2005, EU and ACP countries agreed to disregard from the 2004 deadline stated in this Article.

<sup>4</sup> Terms such as explore or examine are hard to test (Alavi 2007). For example, in India – Bed Linen on WTO Anti-Dumping Agreement Art. 15 which states that 'Possibilities of constructive remedies provided for by this Agreement shall be explored before applying anti-dumping duties where they would affect the essential interests of developing country Members', the panel wrote: 'Pure passivity is not sufficient, in our view, to satisfy the obligation to "explore" possibilities of constructive remedies, particularly where the possibility of an undertaking has already been broached by the developing country concerned' (WT/DS141/R para. 6.238). Nevertheless, the panel also found that exploring possibilities as stated in the article does not imply any particular outcome.

the position to conclude the negotiations by the end of 2007 (Council of The European Union 2007). However, this option requires a WTO waiver, without which continuation is vulnerable to litigation. Against this, some NGOs argue that the litigation may not come, and even if a case is initiated it may take two years before a ruling is issued (Bilal 2007). Thus EU and ACP countries have sufficient time to continue with the current system. Accordingly, certain NGOs argue that, 'the waiver issue is an excuse for not getting fully to grips with the substantive issues faced under EPAs, with the threat of the loss of existing preferences being used to encourage (some would say force) ACP governments to sign up to EPAs, over which they still have fundamental reservations' (ERO 2007b: 12)

Theoretically a waiver may be requested if the negotiations are not concluded with all or some ACP countries by end of December 2007, which links the issue to the pace of negotiations. According to Cotonou, the pace of the negotiations shall be decided by the ACP countries.

Until recently, EU excluded the possibility of asking for a new waiver. According to the EU, the chance of obtaining a new waiver or extending the existing one is minimal, or if it were possible at all, then its 'political costs' would be too high ([http://ec.europa.eu/trade/issues/bilateral/regions/acp/memo010307\\_en.htm](http://ec.europa.eu/trade/issues/bilateral/regions/acp/memo010307_en.htm)).<sup>5</sup> The fact that the current waiver was only obtained after two years of negotiations in the WTO and was made possible only after it became part of the overall Doha Round of negotiations supports the EU's view that a new and long-term waiver is not a realistic option (Abass 2004). This view is also supported by an ECDPM report, which further points to some Latin American and Asian countries' objections to the existing waiver (Bassilekin 2007).

It should be stated that a new waiver either could be short term to give the negotiations more time to be concluded or long term as an alternative to the EPA. According to some media sources the EU is working on the possibility of extending the negotiations into 2008 and asking for a short-term extension of the current waiver on this basis (Bilaterals.org 2007). This will clearly not satisfy what some of ACP countries and NGOs have in mind, which is a long waiver as an alternative to the EPAs, or at least a two years extension (ECOWAS 2006).

### Preferential treatment of ACP countries

The second alternative identified by commentators, is extending an improved version of EU's GSP scheme, 'GSP+', or the Everything But Arms (EBA) regime to all ACP countries (Stevens 2005; Bilal 2007). This proposal's main aim is to secure ACP countries' current market access status without forcing them to liberalize their trade regimes. Legally speaking, a GSP-based trade agree-

<sup>5</sup> According to GATT Art. XXIV.10 a waiver for free trade agreements can be obtained by a two-thirds majority vote, but the general practice in this regard is consensus decision-making.

ment will move EU-ACP trade relations out of free trade domain of GATT Art. XXIV and into the area covered by the Enabling Clause. According to the Enabling Clause, developed countries may 'accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties'. As the Enabling Clause states, such treatment shall not be reciprocal and must be designed 'to respond positively to the development, financial and trade needs of developing countries' (Enabling Clause para. 3.c).

This provision has been addressed in EC – Tariff Preferences (DS246). According to the Appellate Body report in this case, the Enabling Clause permits differentiation of developing countries by the preference granting country, if identical tariff treatment is available to those developing countries that share a particular development, financial (or) trade need (WT/DS246/ABR.para. 165). This means that either all developing countries should be granted the same treatment or that the EU defines some objective criteria which can be applied to ACP countries. Since it is hard to identify such a criteria, it can be assumed that ACP countries as a group cannot be treated differently by the EU than non-ACP developing countries (Abass 2004). It should be mentioned that so far no one has tested which objective criteria could be used as a basis for differentiation between developing countries. However, it could be argued that some countries, for example land-locked countries or small island economies share such features that could probably justify differentiation. Furthermore, within WTO some countries have been grouped as 'special' in respect of particular characterization or needs, e.g. net-food importing countries. The fact that this common status has been recognized by the WTO may also justify differentiation.

The EU has acknowledged that its GSP scheme can be used by ACP countries, if EPA negotiations fail. In this regard it should be stated that ACP countries consist of three groups, each of which will be affected differently by reciprocal EPAs:

1. The first group is the LDC countries whose trade with EU could be governed by the Everything But Arms (EBA) scheme. According to a report, the Commission informed a MEP attending the Barbados Joint Parliamentary Assembly in November 2006 'if EPAs are not agreed or negotiations are delayed then Least Developed Countries would still have full market access under the Everything But Arms initiative but without the long-term security of EPAs' (ERO 2007b).<sup>6</sup>

Under the EBA regime, LDCs have duty-free and quota-free access to the EU. However, this access is not bound and may be revoked. EBA also suffers from more stringent Rules of Origin than Coto-

<sup>6</sup> According to the Commission, they also 'would lose out on all the regional integration benefits of EPAs' ([http://ec.europa.eu/trade/issues/bilateral/regions/acp/memo010307\\_en.htm](http://ec.europa.eu/trade/issues/bilateral/regions/acp/memo010307_en.htm)). However, these benefits have not been identified.

nou especially for goods from Africa, where there are no current provisions for regional cumulation. Moreover, there are no linkages to development aid under EBA, as there should be in an EPA, and nor under EBA would LDCs have access to any EPA-related commodity protocols.<sup>7</sup> These issues would in practice limit EBA's potential benefits to LDCs. Nonetheless, the main difference for LDCs between EBA and EPAs would arise in a context where one or more LDCs elect EBA, while other countries that were part of a common Regional Trade Agreement sign an EPA. In such cases, because of the improved market access to the region for EU goods as a result of reciprocal EPA, EU goods would be able to more freely enter any that belong to the same Regional Trade Agreement as a signatory of an EPA LDC country. This would mean that LDCs would be de facto parts of reciprocal EPAs whether or not they opt for EBA as an alternative. On the other hand, if no country within a region signed an EPA, then LDC countries would experience less difference in terms of market access to the EU compared to now (Olympio, Bidé et al 2006);

2. Non-LDCs that are not members of WTO. The EU is not obliged to offer these countries WTO-compatible EPAs. Thus, theoretically, they could be granted non-reciprocal access. But in practice, because of WTO's Most Favoured Nation rule, they cannot be treated better than WTO members;

3. Non-LDCs that are members of the WTO. Currently, these countries cannot rely on EBA. As mentioned, the only existing alternative for these countries is EU's GSP scheme, which is available to all developing countries and offers them favorable market access for some categories of goods 'depending on the sensitivity of products and the competitiveness of the DC concerned' (Bilal 2007: 21).

Existing GSP schemes suffer from some important shortcomings. Firstly, (like EBA) they do not provide stable and predictable basis for trade relations, since they can be changed or removed at short or no notice. Secondly, they have to be offered to all developing countries, which neutralize ACP countries' current advantage. Thirdly, they also suffer from stricter Rules of Origin than Cotonou. Fourthly, the GSP margin of preference is lower than that under Cotonou, and would mean 'the EU taxing ACP exports, generating revenue that compares unfavourably with aspects of Union-level aid, and is likely to result in the complete cessation of some ACP exports to the EU with significant adverse economic effects' (ODI 2007b: v). Furthermore, 'a switch from Lomé/Cotonou preferences to the standard GSP regime in 2008, while fully complying with the WTO rules, would

<sup>7</sup> Cotonou Art. 36.4 states that 'the parties reaffirm the importance of the commodity protocols, attached to annex V of this agreement. They agree on the need to review them in the context of the new trading arrangements, in particular as regards their compatibility with WTO rules, with a view to safeguarding the benefits derived therefrom, bearing in mind the special legal status of the Sugar Protocol.' See also Orbie (2007) on the future of the commodity protocols.

arguably put the EU at odds with its [Cotonou] obligations, as it would seriously undermine some of the core objectives of the [Cotonou]' (Bilal 2007: 23).

Some have argued that the improved version of GSP, called GSP+, should be offered as an alternative to the EPAs (Andersen 2006; Development Network of Indigenous Voluntary Associations 2007).<sup>8</sup> A few even argue that the GSP+ scheme is a better option than EPA (Perez 2006).<sup>9</sup> Currently, the GSP+ scheme is offered to those countries that fulfil an extended set of criteria and conditions and the list of recipient countries is not subject of review before 2009. Of course, EU could amend the GSP+ regulation. But although some argue that such an amendment 'can be done at anytime and would simply require the approval of the Council by qualified majority. The decision could be taken with the Commission by the Article 133 Committee' (Bilal 2007: 24), the discussions between EU Member-States on how to proceed with the negotiations suggest that the process of changing the regulation is probably not so simple. Moreover, this option faces similar legal obstacles to those already described if GSP+ is only offered to ACP countries, and 'would probably be challenged under WTO rules, since the ACP states would then be given preferential treatment relative to other developing countries' (Narsey 2003: 37). Thus the GSP+ scheme would have to be offered to all developing countries (or those sharing same economic, development and financial needs), which means that the margin of preferences to the ACP countries compared to other developing countries would be eroded. Nevertheless, as Stevens writes 'The most plausible way to satisfy Cotonou Article 37 (6) – including the requirement for WTO conformity – is to apply the GSP+ to the ACP from the end of 2007, following the precedent established for the Andean and Central American states, and to make special provisions for the handful of products not covered (which could include extending the GSP+ regime in some cases). This would provide a breathing space – which some ACP states may use to complete EPA negotiations' (ODI 2007b: v).

### Changing WTO rules

The third possible option is to change GATT Art. XXIV. The argument is that Article XXIV does not take into account the special needs and status of developing countries (Onguglo and Ito 2003; 2005; South Centre 2005). In other words, the article is not 'designed for trade agreements between

<sup>8</sup> It should be acknowledged that the GSP+ schemes, although providing a better alternative than standard GSP, suffer from similar shortcomings. Thus some have suggested that GSP+ should also be improved on Rules of Origin and the coverage of goods (Perez 2006).

<sup>9</sup> GSP+ differs from standard GSP in several aspects. Most importantly, since GSP+ has been designed to encourage the beneficiary countries to pursue certain policies, e.g. good governance, human rights, it provides better terms of trade (lower tariffs or no tariffs on some products) than the standard GSP scheme does. But, GSP+ benefits are only granted to those countries that apply and fulfil two main criteria: they must be vulnerable and have ratified and implemented 27 international conventions.

countries of very different levels of development, such as the EU and ACP countries' (Christian Aid 2004: 6). In particular, it is argued that some S&DT elements should be included in the Article (Lang 2006). These S&DT elements would relax the reciprocity requirement and introduce longer transition times. To this end, in 2004 and as part of the Doha negotiations on Rules, ACP countries tabled a proposal (WTO document TN/RL/W/155), which suggests that 'With regard to duties, appropriate flexibility shall be provided for developing countries in meeting the 'substantially all the trade' requirement in respect of trade and product coverage, including in terms of the application of favourable methodology and/or lower threshold levels, if to be applied, in the measurement of trade and product coverage of developing country parties to an RTA' (ibid: para. 11.i). The proposal also suggested that the transition time stated in the Understanding, currently 10 years, 'should be determined in such a manner that is consistent with the trade, development and financial situation of developing countries, but in any case not [be] less than 18 years' (ibid: para. 22.ii).

Although some countries, including some developing countries, have criticized the proposal for de facto placing FTAs outside of rule-based system, the EU has officially supported the proposal. However, even if changing the WTO rules may be the best solution to the substantial problem, it cannot be regarded as a solution to the immediate problem that EU and ACP countries are faced with, which is establishing WTO-compatible but non-reciprocal EPAs.

## CONCLUSION

This section showed an embedded conflict in the Cotonou agreement: On one hand EPAs shall be WTO compatible (reciprocal) and on the other hand they have to provide ACP countries with equivalent trade opportunities to those currently available. As illustrated, this conflict has been the main source of disagreement between EU and ACP countries supported by NGOs. It has also been shown that although three types of solutions to this conflict have been identified in the literature, none are likely to solve the problem. The current status cannot continue, there are no objective criteria which can justify differential treatment of ACP countries against other developing countries and it is not likely that the relevant WTO rules can be changed in the near future. Thus the negotiators have to choose one of the two opposing requirements as the basis for EPAs. In this regard, WTO has most likely the upper hand (Cottier and Foltea 2006), and if EPAs are not WTO-compatible, any country may initiate a case against the EU and/or ACP countries before the WTO's Dispute Settlement Body.

In addition, it has been shown that although GATT Art. XXIV does not differentiate between developing and developed countries, it includes some flexibilities that EU and ACP countries may use. These flexibilities permit transition time and asymmetrical liberalization of trade between the parties. The extent of such flexibilities in the EPAs depends on the will and the negotiation power



of the parties. Here the imbalance between EU and ACP countries' resources should be taken into account (Borrmann, Grossman et al 2005: 45).

Nevertheless, even if the EPAs include some flexibility, they may place some ACP countries in a worse situation than now. In this case and according to Cotonou Art. 98, the affected ACP country may initiate a case against the EU before the Council of Ministers (of EU and ACP countries) or the Committee of Ambassadors. However, Art. 98 does not explicitly state how such dispute shall be resolved. Arguably, this is the reason why this provision has not been used yet. It should also be mentioned here that this scenario has not been addressed in the literature.

## 2. EPAs: Regional Integration and Configuration Issues

Since the early 1970s, promotion of regional integration has been a central component of the EU's political and economic agenda in relation to developing countries. Its Generalised System of Preferences (GSP), launched in 1971, embodied relatively generous provisions for 'cumulation', which were seen as encouraging regional integration, it played a strongly supportive role in the creation of Mercosur at the start of the 1990s, and its foreign policy in the Mediterranean area has been built on a series of regional initiatives with the eventual aim of a Euro-Med Free Trade Agreement (EMFTA). The central reason for this policy has of course been the conviction that the European experience of regional economic cooperation (culminating in a single market) can serve as a model on the global stage.

It is therefore little surprise that the EU strove to include a strong regional integration (RI) element in the Cotonou Agreement. Article 2 of the Agreement states that 'particular emphasis should be placed on the regional dimension' in future EU-ACP cooperation arrangements, while Article 35.2 states that 'economic and trade cooperation shall build on RI initiatives of ACP countries, bearing in mind that RI is a key instrument for integration into the world economy'.

The view that RI is a stepping-stone to integration in the global economy is actually the main argument amongst four that the EU has advanced for re-framing its relations with the ACP on a regional basis. The second of these arguments is that the alternative to regional EPAs would be to establish 78 agreements between the EU and each ACP country. This would be impractical. The third argument that has been advanced, is that EPAs combining EU membership with ACP RI will 'lock-in' economic liberalisation (chiefly but not only trade liberalisation), better than agreements between single ACP countries and the EU. This is because regional agreements would create greater loss-of-market-access disincentives to reverse liberalisation than bilateral ones. 'Lock-in' is viewed as critical in attracting foreign investment, on the basis of reducing its risk of exposure to policy change. Finally, it has been argued that RI has clear political advantages, principally that it can contribute to conflict resolution or consolidation of peace.

On this basis, while it is legally consistent with Cotonou for an individual ACP country to negotiate an EPA with the EU, it seems likely that the EU, except in exceptional circumstances, will oppose this.<sup>10</sup>

## EXPERIENCES OF REGIONAL INTEGRATION IN THE ACP GROUP COUNTRIES

Since the 1970s, there has been a steady stream of efforts at regional economic cooperation on the part of countries in the ACP group. As a result, there are more than a dozen agreements of this kind in Sub-Saharan Africa and at least three each amongst the Caribbean and the ACP Pacific countries respectively.<sup>11</sup> On the other hand, there appears to be an inverse relation between the number of agreements entered into and the extent to which additional intra-regional trade has been generated.

In particular, levels of intra-regional trade following the introduction of regional trade agreements, have tended to remain low and stagnant. Amongst current ACP country regional economic associations, CARICOM has the highest level of intra-regional trade (at around 20% of the total imports of member countries, South Centre 2007c) while the Pacific Islands Countries Trade Agreement (PICTA) has the lowest (at 2% of the total imports of member countries, *op. cit.*).

For Africa, Yang and Gupta (2005) comment: 'Regional Trade Agreements (RTAs) may have had a positive, but uneven, effect in intra-regional trade, although over the long run the effect seems to have been small or insignificant'. Intra-regional trade appears to be highest in the West African Economic & Monetary Union (WAEMU) (at 13.3% of the total imports of member countries in 2003, Yang and Gupta 2005) and lowest in the Central African Economic and Monetary Community (CEMAC) (at less than 2% of the total imports of member countries in 2005, Martijn and Tsangarides 2007). Intra-regional shares of total imports of member countries in 2002 were 11.5% for the Economic Community of West African States (ECOWAS) countries (Yang and Gupta *op. cit.*), 6.3% for the Southern African Development Community (SADC) ones (*op. cit.*) and 5.8% for the Common Market of Eastern and Southern Africa (COMESA) ones (*op. cit.*). Of the main African country groupings, only the members of WAEMU, COMESA and SADC registered higher levels of intra-regional trade in 2003 than in 1980.

<sup>10</sup> In September 2006, Cape Verde announced that it was leaving the ECOWAS configuration with a view to negotiating a bilateral EPA. The EU appears to have persuaded it to rejoin.

<sup>11</sup> There is no evidence that Africa is unusual in its large number of regional economic cooperation agreements. As of November 2007, there were 334 RTAs notified to the WTO and a further 141 under review. What is more unusual is the large proportion of RTAs in Africa that have the ambition to become Customs Unions (*cf. Watson and Do 2006*).

Explanations of this in the academic literature and the literature published by the international financial institutions tend to stress two factors. Firstly, levels of commitment to regional trade liberalisation by signatory countries have been generally low. This is mainly ascribed to high levels of fiscal dependence on tariff revenues amongst ACP countries (cf. Khandewal 2004). Low levels of commitment are expressed in failures to fully or in some cases even partially implement agreements as well as in the general absence of mechanisms to pool and redistribute tariff revenues.<sup>12</sup>

Examples of failures to implement agreements are abundant (Hinkle and Newfarmer 2005, Yang and Gupta 2005, Khandewal 2004, Gasiorek and Walters 2004). Where agreements take the form of FTAs, some signatories typically decline to participate, while the tariff reduction schedules of those who do are heavily back-loaded and/or haltingly implemented and numerous exemptions granted. Where, as is increasingly common, they take the form of Customs Unions, it proves difficult to agree on design of a Common External Tariff (CET)<sup>13</sup> and even more difficult to secure its implementation. In the cases of both FTAs and Customs Unions in the ACP, non-tariff barriers continue to abound, for example in the form of non-acceptance of origin certificates and cumbersome and inconsistent customs procedures. Non-convertibility of currencies within ACP FTAs also hinders effective utilisation, even where implementation is on track.

It is usually argued that levels of commitment to RI by member countries is closely related to another reason for its failure, namely widespread overlapping membership of agreements, resulting in a dilution of human and technical resources, high administrative costs and inconsistent obligations. As a result, the multiple integration organisations and agendas in each of the main ACP regions and sub-regions are often in conflict with each other. The most glaring example is in Eastern and Southern Africa, in relation to the East African Community, COMESA and SADC. Seven countries are members both of COMESA and SADC.<sup>14</sup> Four COMESA countries and one SADC country are members of the East African Community, which is a Customs Union. COMESA is in the process of adopting a CET and SADC has plans to adopt a CET. Another SADC country (Swaziland) is a member both of COMESA, SADC and of a Customs Union (SACU) within SADC.

<sup>12</sup> Low commitment is also expressed in the member countries' failure to pay assessed contributions to regional economic organisations, or to introduce any instance of supranational authority within them (UNECA 2006).

<sup>13</sup> Problems of CET design include determining the number of tariff bands, determining what levels of tariff to apply to them, and (generally most contentious) determining which tariff lines should be allocated to which band (Khandewal op. cit.).

<sup>14</sup> Some SADC members are also members of the Economic Community of Central African States (ECCAS) or the Indian Ocean Commission (IOC). Some COMESA members are also members of ECCAS, IOC or the Inter-Governmental Authority on Development.

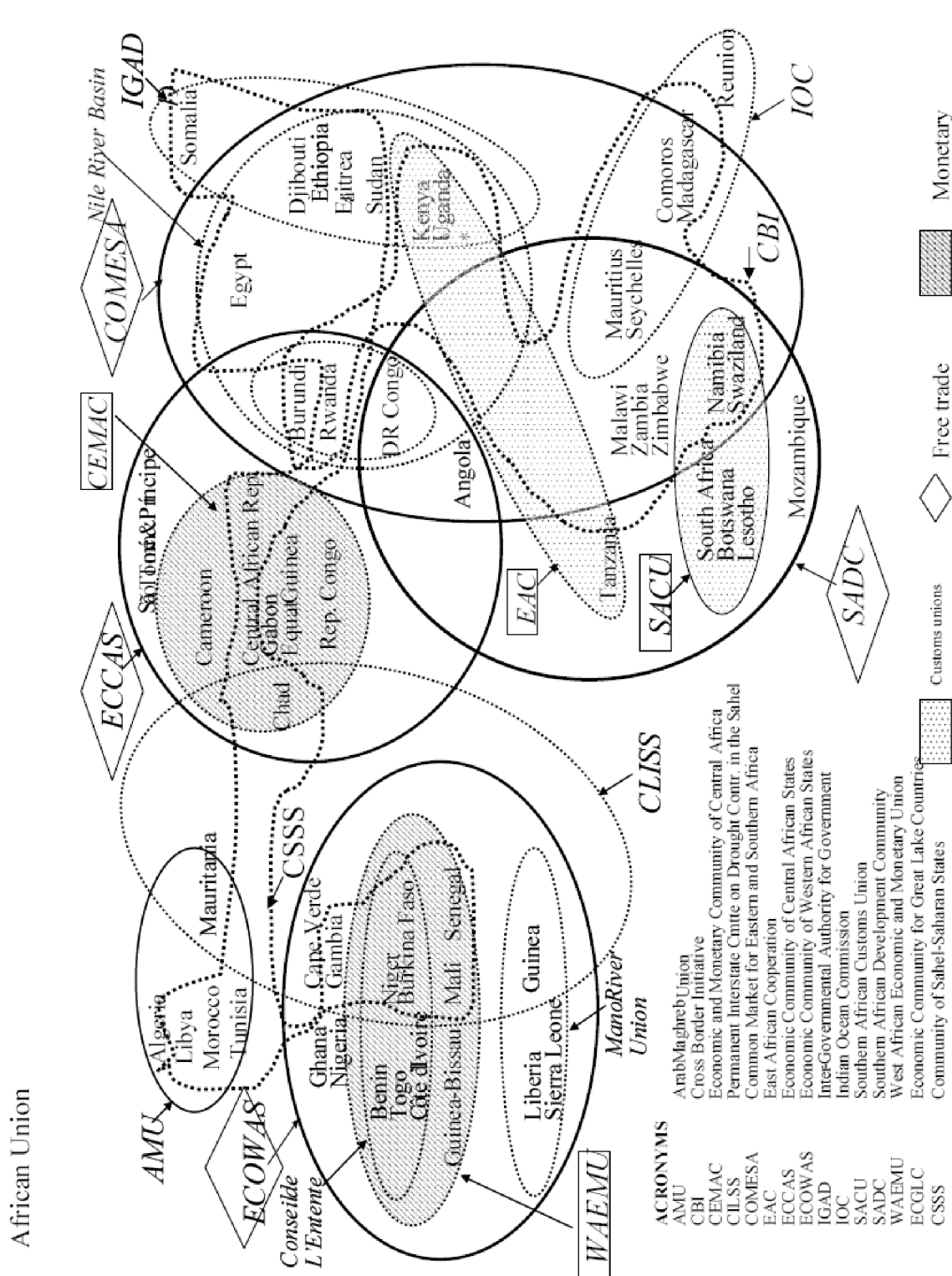


Figure 1: Regional Economic Cooperation Agreements in Africa

This second group of factors is also highlighted by NGOs supporting what they see as the ACP cause. The factors in question are structural, rather than political: low levels of product complementarity and lack of infrastructural integration (cf. Khandewal 2004, Powell 2007, Action Aid 2004).

On product complementarity, Khandewal (2004) measured the similarity between member country export and import baskets for both COMESA and SADC, in order to determine the trade potential of these groupings. On a scale of 0-100 with 0 representing zero complementarity and 100 representing perfect complementarity, South Africa within SADC had a complementarity of 53.0, while other member countries ranged between 10.3 and 23.4. In COMESA, Egypt and Kenya had complementarities of 43.0 and 38.6, respectively, while all other members ranged between 3.2 and 20.0. Khandewal states that these results raise issues not only of low potential, but also of possible polarisation within these groupings. Furthermore, he notes that the potential for polarisation exists in the absence of evidence that Egypt, Kenya and South Africa are internally diverse and dynamic enough to serve as 'growth poles' for their respective groupings.

NGO contributions to this discussion go on to argue that dependence on similar export baskets and low levels of infrastructural integration demonstrate that prioritising regional trade integration over other forms of political cooperation and economic integration in the ACP is mistaken. Rather, ACP regions and sub-regions would more clearly benefit from a combination of improved infrastructural integration, political trust-building and development assistance aimed at economic diversification (Powell 2007, Action Aid op. cit.).

## CRITIQUES OF THE EU REGIONAL INTEGRATION AGENDA IN RELATION TO THE ACP

To a large extent, the EU is alone in postulating that its RI agenda will both accelerate regional economic development in the ACP countries and promote the latter's global economic integration. Academics, economists associated with the international financial institutions, economists working for regional organisations in Africa, and NGOs all see the EU's priorities as misguided.

Gunning (2002), on the basis of a theoretical argument that will be referred to in a moment, concludes that in the ACP, where there are binding constraints on intra-bloc trade deriving from similarities in factor endowments and high transport costs, there is indeed scope for regional initiatives. However, a trade bloc is the wrong instrument for this purpose. Trade blocs may yield indirect benefits, such as improved security or cooperation around common infrastructural projects, but these do not require changes in trade policy. Nor, in the ACP case, will RI lead to the other main trade-related benefit normally associated with blocs (increased negotiating power), since the institutionalisation of ACP regions will be at the expense of the effective disintegration of the ACP

itself.<sup>15</sup> These arguments are echoed in the analyses of EPAs by other economists (e.g., Meyn 2003), the World Bank (e.g., de la Rocha 2003), IMF (e.g., Yang and Gupta 2005) and NGOs (Powell op cit., Action Aid op. cit.), although the NGOs certainly would not subscribe to certain of the central foundations of the main argument advanced by Gunning, nor to some of the other conclusions that accompany it.

The first reason that Gunning and other economists advance for why trade blocs are inappropriate where there are binding constraints on intra-bloc trade, is that in these circumstances there is greater likelihood that they will be associated with trade diversion from the rest of the world, in favour of the most efficient country in the bloc. In this scenario, producers in the most efficient country gain, but consumers throughout the bloc lose due to higher prices, and governments and producers in less efficient countries lose from reductions in tariff revenue and closure of less efficient industries. This outcome is mitigated somewhat where economies of scale rather than constant marginal costs of production are assumed, although welfare losses from reduced competition also need to be taken into account in this revised scenario.

The second reason advanced by economists concerns issues of polarisation and RI. The argument here is that, where a bloc as a whole is 'capital poor' but there are significant differences between member countries in factor endowments before the bloc is formed, then income differences will increase as benefits accrue to the member countries that are relatively similar to the rest of the world in terms of capital endowments (cf. World Bank 2000). Where a North-South dimension is added to the scenario, the South-South polarisation will re-appear in a new form and there will be a decline in South-South integration. The richest Southern country loses access to other Southern country markets to the benefit of the Northern bloc member. This will be partly offset by the richest country being the only Southern country in a position to benefit from Northern market access. But RI, in the sense of South-South trade, will decline.<sup>16</sup>

The basic assumption underlying these economic arguments is that trade blocs promote internal freedom of trade only on the basis of preserving or (more frequently<sup>17</sup>) of increasing barriers to external trade. Since free trade is assumed to be the most welfare-maximising option, and since the

<sup>15</sup> Bilal (2005) argues that this has been a strategic intention of the EU, expressed inter alia in what he depicts as EU efforts to foreshorten and undermine the first (all-ACP) phase of the EPA negotiations.

<sup>16</sup> Results obtained by studies modelling changes in intra-COMESA trade following fully reciprocal EU-ACP liberalisation by Karingi et al (2005) and Mwega (2005) appear to support this conclusion.

<sup>17</sup> It is argued that, in free trade areas, common external tariffs are normally set close to the level of the most industrialised country – which is typically the most protected one. There is certainly evidence for this in relation to African FTAs (cf. Claeys and Sindzingre (2003) on WAEMU).

adjustment costs that free trade implies are probably higher than those associated with joining trade blocs only for the most efficient/rich developing country in the bloc, then Most Favoured Nation (MFN) trade liberalisation is always to be preferred over the creation of blocs (cf. Gasiorok and Winters op. cit., Khandewal op. cit.). A related conclusion is that, if trade blocs are going to be imposed anyway for political reasons, then their negative welfare implications will best be mitigated if their CETs are set as low as is politically possible.

Thus, the many critiques of the EU approach to RI share the perspective that deeper infrastructural and communications integration, upgrading worker skills and cross-sectoral cooperation in areas such as trade facilitation, energy, water resources, environmental management and conflict management are all politically more worthwhile objectives for the ACP regions and sub-regions than forming EPAs. Of course they differ diametrically, in respect of which trade policies are advocated as alternatives to forming EPAs.

## THE QUESTION OF CONFIGURATION

According to the Cotonou Agreement, the make-up of subsequent regional and sub-regional groupings of ACP countries was up to the ACP countries themselves. On the other hand, during the first phase of EPA negotiations it seems that the EU envisaged that EPAs would take shape around specific existing regional economic groupings. This is stated explicitly in 'Orientations on the qualification of ACP Regions for the Negotiation of EPAs' (EC 2001), according to which negotiations should be with existing 'functioning' and 'effective' regional groupings, and that 'regional integration initiatives...which have not been implemented...for which legally binding interim agreements do not exist or are not effectively implemented ... should not be considered' (section 4.1). This led contemporary commentators (including Gunning op. cit.) to state that the EU's aim was to have the four African Customs Unions (WAEMU, CEMAC, SACU and the EAC) as the core of four distinct EPAs in the African region. Gunning also stated that the EU was envisaging that non-members of Customs Unions would evolve slowly towards membership of these groups, with Everything But Arms (EBA) and GSP as interim alternative offers for LDC and non-LDC non-members. The EU's early plans in the Caribbean and Pacific are not discussed in the literature.

Claeys and Sindzingre (2003) state that the idea of centring African EPAs on CUs was dealt a decisive blow by the near-collapse of Cote d'Ivoire, the centre of gravity of WAEMU. Furthermore, there were obvious problems involved in centring a Southern Africa EPA on SACU, since its overwhelmingly dominant member (South Africa) was not a full ACP member and had already concluded a bilateral FTA with the EU in 1999.



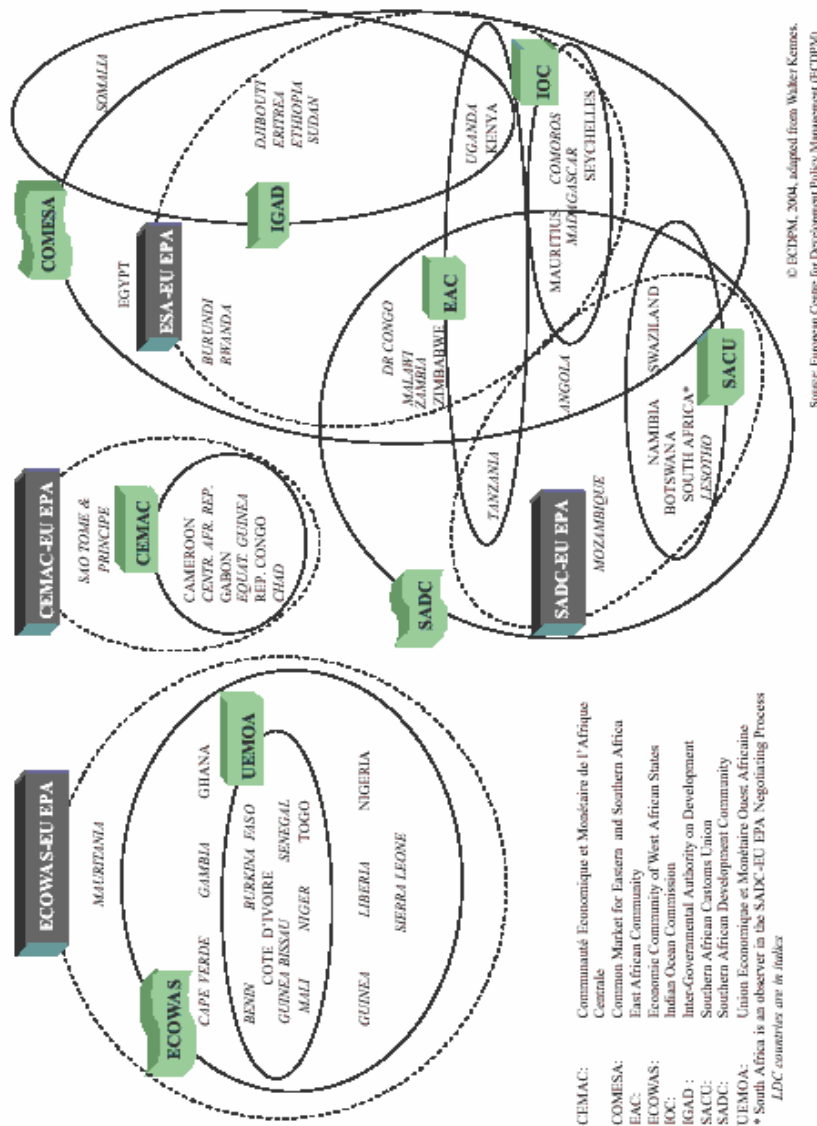


Figure 2 African EPA Configuration, January 2007

The result was indeed the spontaneous emergence of a constellation of African country groupings, only one of which (the Central African group) is co-extensive with a Customs Union.<sup>18</sup> The constellation, which is still shifting (see below), reflects political and historical alignments and rivalries as well as economic interests. As such, it adds a further layer of complexity – some would say confusion – to ACP countries’ already tangled obligations.

<sup>18</sup> Even the CEMAC EPA group is not 100% co-extensive with the CEMAC Customs Union, since it also includes São Tomé & Príncipe, which is not a CEMAC member.

The remainder of this section will focus upon problems associated with the evolving EPA configurations listed in Figure 2. These are identified in the literature as including internally divergent entitlements in relation to Cotonou, internally divergent trade interests, shallow political foundations and failure to resolve the problem of conflicting obligations.

### Internally divergent entitlements in relation to Cotonou

Articles 35.3 and 85.1 of the Cotonou Agreement mandate special and differentiated treatment (SDT) in terms of 'flexibility' and 'asymmetry' to LDCs, small, landlocked and island states. As noted elsewhere in this report, the EU has chosen to interpret flexibility and asymmetry in terms of differential paces and product coverage of trade liberalisation in the ACP countries themselves, rather than in terms of non-reciprocity. Since EPAs include both LDCs and non-LDC members, this implies that, if LDCs seek continued non-reciprocal access by availing of Everything But Arms (or rather, if they are allowed to do so), they will have to maintain tariff barriers in relation to non-LDC members in order to prevent goods from the EU under tariff lines that are still protected from entering their markets. Where they are already members of the same FTA or CU as the non-LDC members of the EPA, this will entail a reversal of the regional trade liberalisation attained under these agreements (Bilal 2005, Hinkle and Newfarmer 2005). If this right is exercised in the context of membership of Customs Unions, it will also entail a probable breach of GATT Article XXIV 8(a)(ii).<sup>19</sup>

So far within the Phase II negotiations, the issue of divergent entitlements has been raised in relation to Mozambique, Angola, and Tanzania with the SADC EPA group. In March 2006, the SADC EPA group proposed that these countries (all LDCs) be freed from the requirement for reciprocity. The EU rejected this as in conflict with WTO rules. It stated instead that it was 'willing to explore all possible options compatible with WTO standards', and indicated that this might include establishing a second SADC EPA group consisting exclusively of LDCs (Kruger 2006, Grant 2006).<sup>20</sup>

### Internally divided trade interests

Divergence in trade interests within the ACP EPA groups goes well beyond those relating to differences in LDC and non-LDC contractual entitlements under Cotonou. They also concern diversity in existing levels of protection and in trade regimes more generally between countries and groups of countries within these configurations.

<sup>19</sup> This states that members of a Customs Union shall apply 'substantially the same duties and other regulations of commerce'.

<sup>20</sup> According to Grant (*op. cit.*), the reason the EU stated for making this proposal (rather than any other WTO-compatible solution within an EPA framework) was that the alternative would have entailed a binding of EBA, which the EU said it was 'not in a position to do'. How seriously the proposal should be taken is another question (see below).

Considering variations in existing levels of protection first, while there is a strong overlap in ACP exports (especially between the exports of African, Caribbean and Pacific countries considered as separate groupings), there is surprisingly little overlap in the products that they currently protect. This will make it extremely difficult to reach agreement on any future CET, or on a common programme of internal tariff liberalisation, or even on lists of sensitive products to exclude from liberalisation commitments. Stevens and Kennan (2005b), analysing similarities and differences in the applied tariffs of members of the different EPA groups, state 'If products where there is an applied tariff of more than 20% are considered candidates for exclusion, there is not a single product that would be on the lists of all members of any (current) EPA group. Where products with applied rates of more than 40% are concerned, no one product for any single member would appear on the list of another member of the same group...'

When it comes to interests concerning membership of common trade arrangements more generally, sharp differences can be found within some EPA groups between sub-groupings defined in terms of historical membership of different regional associations. These differences are probably most intense in the West African EPA grouping, which combines the WAEMU Customs Union and the much looser ECOWAS formation.<sup>21</sup> While all WAEMU members are also members of ECOWAS this has been of little significance, since implementation of ECOWAS trade protocols have been so limited. The essence of the West African EPA group problem is that WAEMU and ECOWAS have a de facto rival relation, revolving around the position of Nigeria (Claeys and Sindzingre 2003). Nigeria, which comprises around 60% of the total West African market and whose GDP easily exceeds that of the whole of WAEMU, is widely regarded as having undermined WAEMU through maintaining the region's most restrictive trade regime and a non-convertible currency on WAEMU's borders. In the context of the West African EPA group, Nigeria will almost certainly insist upon a considerable upward adjustment in the existing WAEMU CET. This will be seen in the WAEMU not only as in conflict with its trade interests, but also as destabilising its anchorage in the Euro and fixed parity (op. cit.). How this is likely to play out remains unclear, particularly as the West African EPA group negotiations appear to have moved more slowly than for any other configuration.

### Shallow political foundations

In the case of the West African EPA group, there is a clear fault line in political foundations underscored by differences in language and external political orientation. However, in ECOWAS there is at least an institution with some authority to develop a regional negotiating mandate. In some other EPA regions, the EU either has no mandated institution to negotiate with, and/or – as in the Caribbean and Pacific – credible negotiating partners such as CARICOM have been by-passed (Bilal

<sup>21</sup> This EPA group also includes Mauritania, which was a member of neither.

2005).<sup>22</sup> Yet, the problem of shallow political foundations is possibly most acute in the eastern and southern Africa. Here there have been ongoing conflicts between the COMESA countries and the COMESA secretariat on the one hand and the SADC countries on the other.

Initially, these countries shared a common platform for negotiating an EPA and the organisations' two secretariats met throughout 2001 and 2002 to discuss its formulation (albeit with provision for differential liberalisation of tariffs). According to Pearson (2007), differences first arose in March 2003 following a meeting of the COMESA secretariat which 'decided' that the eastern and southern African ACP countries should negotiate an EPA as a single group. SADC countries challenged COMESA's authority to take this decision, and some SADC countries started a campaign for a separate configuration (Pearson 2007), which emerged in 2004.<sup>23</sup>

Subsequently conflict has continued within what has become the ESA EPA configuration. Early in 2006, the COMESA secretariat (which, throughout the process has served as the secretariat for the ESA EPA negotiations) sought to appoint a Chief Trade Negotiator who would lead the negotiations in place of the Brussels-based ESA ambassadors. This was opposed by Zimbabwe, whose representative was about to become chair of the Regional Negotiation Forum. The COMESA secretariat subsequently withdrew the proposal (Munyuki, 2006).<sup>24</sup>

### Conflicting obligations revisited

As in the pre-EPA era, the epicentre of conflicting trade agreement-related obligations remains Eastern Africa and Southern Africa, covered by the ESA and SADC EPA groupings. Here the main conflicts of obligations have been as follows:

- Five ESA EPA countries (DR Congo, Malawi, Zambia, Zimbabwe, and Mauritius) are also members of SADC, though not the SADC EPA.
- Two SADC EPA countries (Swaziland, Angola) are members of COMESA, though not the ESA EPA.

<sup>22</sup> According to Bilal (op. cit.), CARICOM was apparently by-passed in favour of the shallower CARIFORUM in order to facilitate the inclusion of the Dominican Republic. ECDPM (2007, 20) states that CARIFORUM is itself reluctant to be defined as a party to the EPA, since it has 'neither the legal nor the policy competence to assume region-wide EPA commitments'. There are also problems related to political foundations in the Pacific region, where three members of the EPA configuration are countries with special legal relations to the US (Federated States of Micronesia, Marshall Islands and Palau).

<sup>23</sup> Bertelsmann-Scott (2007, 187) quotes the COMESA Secretary General Erastus Mwenchu to the effect that South Africa was openly pushing for a distinct SADC EPA.

<sup>24</sup> Kenya issues a separate critical statement. See also [www.bilaterals.org](http://www.bilaterals.org) (2007).

- Tanzania, which was a member of COMESA until 2004 and which has been a member of SADC since its foundation, was until August 2007 both a member of the EAC and of the SADC EPA
- The remaining EAC members (Kenya, Uganda, Rwanda, Burundi) were all also members of COMESA and the ESA EPA until 2007
- Botswana, Namibia, Lesotho, and Swaziland are indirectly party to the EU-South Africa FTA by virtue of common membership of SACU. All are members of the SADC EPA.
- Until February 2007, South Africa was a member of SACU and SADC but not of the SADC EPA group
- Since February 2007, South Africa has been a member of the SADC EPA group while also being a signatory of a bilateral FTA with the EU.

The most immediate of the problems listed above were those concerning the effects of incorporating South Africa in the SADC EPA and the status of Tanzania as a member both of the SADC EPA and the EAC. However, in December 2006 the EU agreed to South Africa's inclusion in the SADC EPA, subject to a 'rigorous system of ... Rules of Origin and the establishment of an autonomous safeguard mechanism' (ECDPM 2007, 11). South Africa's admission was a result of pressure from other SACU members, who believed they would benefit from what amounts to their formal inclusion in the EU-South Africa FTA.<sup>25</sup> South Africa is also likely to be at least temporarily excluded from the free market access to the EU offered to the rest of the EPA and will be expected to address at least some of the EU's 'new trade agenda' (EC, 2007c)

The SADC EPA proposal to include South Africa, as noted above, also included the demand that Mozambique, Angola, and Tanzania be granted non-reciprocal free market access to the EU within the same configuration. Responding by suggesting a second 'SADC LDC' EPA comprising exclusively these three countries, can be read as strong encouragement by the EU for them to join the ESA EPA group. Angola lays on the opposite side of continental Africa to Mozambique and Tanzania, implying an EPA that would have been geographically as well as economically unviable.

In April 2007, the EAC suddenly announced its intention to form an EPA grouping (Kruger 2007). At first it was unclear if Tanzania was party to this decision. Subsequently it has stated that it was. This development implies that Kenya, Uganda, Burundi and Rwanda will have to withdraw from the ESA EPA grouping and Tanzania from the SADC one. Meanwhile, Mozambique and Angola are

<sup>25</sup> According to Meyn (2003), South Africa initially opposed this proposal, as it feared that the EU would use its acceptance as a basis for re-opening the Agreement. Later South Africa relented. The EU of course also undertook an impact assessment, which apparently concluded that the perceived risks of this change in arrangements had been exaggerated (Grant 2006).

faced by what seems to be a choice between joining EPA configurations other than SADC. In the short term, the result is to create a fifth African EPA grouping based (as originally envisaged) on the EAC.

## CONCLUSION

The literature poses two main questions in relation to the regional integration and configuration dimensions of EPAs. One is whether EPAs, whatever their geographical configuration, can create a more effective form of regional economic development in the ACP countries. The second is whether the specific geographical and institutional configurations that have evolved (or, more accurately, are still evolving) in the EU-ACP negotiations, lay the foundation for a more credible or rationalised set of RI arrangements than those that existed prior to 2001.

As has been noted, the consensus of commentary is negative on both points. On the first, academics, the international financial institutions and NGOs all agree that only a different RI approach – or at least a different approach to RI sequencing – is likely to increase rather than diminish RI. At the same time, most academics and the international financial institutions object to the notion that regional trade liberalisation is preferable to MFN liberalisation in any circumstances.

On the second point, although a good deal less has been written on it, the consensus appears to be that the specific geographical and institutional configuration that evolved in Africa up to the end of 2006 was neither more credible, nor pointed in the direction of greater rationalisation, than that it succeeded. Since the beginning of 2007, a higher degree of rationalisation may be emerging, although it will take some time before this is clarified. On the other hand, if effective RI requires a different sequencing from that proposed by the EU, this will make little difference.

### 3. Rules of Origin, the European Union and the Economic Partnership Agreement Negotiations

Rules of Origin (RoO) define the economic as opposed to the geographical origin of products. That is, they define what an importing country considers the amount of value added in a good or service in a given exporting country sufficient for it to be counted as an export from that country. In addition, RoO can restrict the number of countries from which an exporting country may source its non-originating raw materials or components (if permitted to use these), while still having its products defined as originating. Countries (or Customs Unions) normally have two distinct sets of RoO, one applied to Most Favoured Nation (MFN) trade, and one applied to Preferential Trade Agreements (PTAs). Individual preference-granting countries' PTA RoO tend to have a high level of similarity across agreements. This applies to the US (the 'NAFTA model') and to the EU (the 'Pan-Euro model'). Invariably, PTA RoO are more restrictive than MFN ones. Theoretically, the reason for this is to prevent 'trade (and, in some versions of the argument, investment) deflection'. Trade deflection involves transshipment of a good or service via a preference-holding country in order for it to obtain the margin of preference available under the PTA. Under MFN trade there is normally no incentive to misrepresent origin, since all exporting countries face the same tariff.

Transshipment to take advantage of preferences is common, meaning that there is clear case for a country's PTA RoO being stricter than MFN ones. However, PTA RoO may serve purposes other than preventing trade deflection. Principally, they may act as non-tariff instruments of protection or mercantilist trade promotion, or both. They may serve as a protectionist instrument by substituting a tariff barrier by a domestic production requirement that is difficult to meet, thus in effect acting as a tariff on the raw material or component rather than the final product (Kreuger, 1993). They may serve as an instrument of mercantilist trade promotion by allowing only raw materials or components from the importing country itself to count on an equal basis with local ones in conferring origin (see Appendix 1).

For these reasons, debate concerning RoO in PTAs invariably revolves around the issue of levels of restrictiveness. The discussion here will also focus on this issue in relation to trade in goods under the EU's PTA RoO, specifically in the context of the ACP EPA negotiations. But before entering into this discussion, it is necessary to note the different methods of operationalizing RoO.

#### RoO METHODOLOGIES

RoO are administered by Customs Departments rather than trade ministries. As a result, the Kyoto Convention of the World Customs Organisation (1973, revised 1999) is the main international basis

for defining them. The Kyoto Convention recognizes two basic criteria for determining origin (both of which date back in practice long before 1973<sup>26</sup>). The first is the notion of wholly obtained/produced in the exporting country. Rules based on this criterion are typically applied in relation to agricultural goods and minerals. They are also applied typically in relation to fish, although in this case ‘exporting country’ may be defined in terms of territorial waters or the latter plus the country’s ‘exclusive economic zone’ (EEZ) (see Appendix 2).

The second Kyoto criterion is that of ‘substantial transformation’. In other words, although a good or service is not entirely produced in a given country, it can be counted as originating there if it has been substantially transformed in the country in question. Three groups of sub-methods are used to operationalise substantial transformation: Change of Tariff Classification (CTC), Value Added (VA) and Technical Requirement (TR) (See table II.3.1).

<b>Change of Tariff Classification (CTC)</b>	This method refers to the Harmonised System (HS) of tariff classification. The HS system classifies goods at item (8-10 digit), sub-heading (6 digit), heading (4 digit) and chapter (2 digit) level. Correspondingly, a RoO may demand that a local operation is performed on an exported good that results in a change from one to another category. CTC rules are often accompanied by exceptions. These prohibit the use of non-originating raw materials or components in transitions between specific tariff classifications.
<b>Value Added (VA)</b>	This method requires an exported good to embody a minimum local VA, have specified originating parts comprising a specific share of final value, or embody a maximum import content measured in value terms. As will be seen, there is also some variation in the base prices against which VA must be calculated (e.g., ex-works, FOB, CIF, etc). Where VA rules are applied in US and EU PTAs, the level of local VA required usually falls in a range of 25-60%.
<b>Technical Requirement (TR)</b>	A RoO may insist that one or more specified manufacturing operations must take place on the good in the exporting country for it to be classified as originating. A reverse form of this rule can also be found in many PTAs, whereby specific manufacturing operations are identified which are insufficient to confer origin (e.g., labeling, packaging or assembly).

According to WTO data on PTAs for 2002 (cited in Estevadeordal and Suominen 2004, 5), the most widely applied of these rules is CTC (present in 89 of 93 agreements for which there was information). The EU PTA RoO are also predominantly of a CTC kind, although for 20% of tariff lines covered there is no reference to CTC. In the cases of the EU Cotonou and GSP RoO, VA is the sole test in 10-13% of tariff lines (ODI 2006, Cadot et al 2005a).

<sup>26</sup> Estevadeordal and Suominen (2004) state that one of the first PTAs ever signed, the Canada-US FTA, used a version of the ‘substantial transformation’ criterion – ‘production of a new and different article’ from its inception in 1908.



Rules based on CTC and VA are applied mainly to manufactures other than textiles and clothing, while TRs are very common for the latter products. Quite often, goods are expected to conform to more than one method of proving ‘substantial transformation’, although the prevalence of the use of multiple methods does not seem to have been measured in the literature. It should also be noted that, in the case of many North-South PTAs, derogations might be granted to certain (groups of) countries – normally LDCs – in respect of origin requirements for time-limited periods, to accommodate what is agreed to be lack of raw materials or local production. The most famous of these derogations is AGOA’s ‘Third country fabric’ provision for ‘lesser developed beneficiary countries’.

Rules defining origin within overall PTA RoO packages are invariably accompanied by others providing for specific methods by which their impact may be modified. There are three main rules of this kind: De minimis, Roll-up or Absorption, and Cumulation (See table II.3.2).

De minimis	This permits a specified share of the final value or volume of the product (normally between 7% and 15%) to comprise non-originating raw materials or components. Often the components to which the rule applies are specifically identified (for example, zips, buttons and inter-lining for clothing). In the case of the EU’s GSP, De minimis is not applicable to products in HS Chapters 50-63 (‘Textiles and Textile Articles’).
Roll-up or Absorption	This permits intermediate products which are not in themselves originating but which are embodied in an originating product to be counted as wholly originating for the purpose of determining the origin of a final product that incorporates them.
Cumulation	Under cumulation rules, PTA members may source non-originating raw materials or components from specified countries and count them as originating. There are three types of cumulation: <ul style="list-style-type: none"> <li>(i) Bilateral, where only raw materials or components from the preference-granting country can be counted in this way. The EU-Chile PTA provides only for this method;</li> <li>(ii) Diagonal, where raw materials or components deemed to be fully originating from the preference-granting country or from a list of other designated countries to which the same preferences apply can be counted. This method is applied in 58 PTAs (Estevadeordal and Suominen 2004, 6). The EU’s Generalised System of Preferences (GSP) provides for this method, in that beneficiaries can cumulate from fellow members of designated regional groupings in East Asia, Southern Asia and Latin America; and</li> <li>(iii) Full, where all components, even if they are not fully originating, from all countries to which the same preferences apply can be counted. This method is only applied in 8 of 88 PTAs examined (WTO data set for 2002). The Cotonou Agreement with the ACP provided for full cumulation between the 78 signatories, as well as some diagonal cumulation from designated regional groups of developing countries. In Annexes to the Cotonou Agreement added at the time of the EU-South Africa FTA, restrictions are placed on cumulation by ACP countries from South Africa.</li> </ul>

The EU has always seen Cotonou's enhanced cumulation provision not merely as a mitigation of its basic rules for conferring origin, but mainly as a means by which its RoO incorporate a 'development' dimension. Implicitly, development is equated with backward integration. Moreover, even if backward integration is not possible in an individual ACP country because of the absence of opportunities for economies of scale (some ACP countries and territories have populations as small as 2,000 people), it should be possible on an all-ACP basis.

A final aspect of PTA RoO is that they are always accompanied by more or less restrictive administrative conditions. One frequent condition is a prohibition on beneficiary countries providing their exporters with remission of import duties ('duty drawback') on non-originating raw materials or components, where these enter into products benefiting from a margin of preference. Another condition is certification of qualified exporters and/or exports by the customs authorities of the exporting country. In the case of NAFTA, self-certification is permitted. Under Cotonou, exporters require a EUR 1 form verified by local customs authorities for each consignment; frequent exporters may however apply for 'approved' status which, when granted, allows self-certification. AGOA requires a 'customs visa system' to be set up by beneficiary country customs authorities. This entails verification of each consignment by exporting country customs, monthly submission to the US of lists of verified consignments and open access of all exporting firms to roaming US Customs Department 'jump squads'.

## EU PROPOSALS FOR THE REFORM OF ITS PTA RoO IN THE CONTEXT OF THE EPA NEGOTIATIONS

The general background against which discussions of EPA RoO is occurring, is the EU's broader and longer-term process of reforming its RoO. The harmonization element of this process dates back to the early 1990s. Since around 2003, the EU has also unveiled proposals for simplification. In regard to the latter, its most recent step was in 2005, when – following a round of public consultation – a 'Communication' (EC 2005) on the subject was issued. Besides proposing a method for simplifying EU RoO for PTAs with developing countries, this also emphasizes 'efficiency of procedures' and 'enforceability'. The Communication is designed to form the basis for the EU negotiating position on EPA RoO, when this is eventually unveiled.

The Communication states that it is the EU's intention to replace all its existing methods for determining origin with a single but more flexible one. This will be a local VA requirement, set at different levels around a 'standard threshold', according to tariff line. The document mentions that this requirement may still be supplemented by additional tests in the cases of agricultural products, fish / fish products, and textiles and clothing (see Appendix 2). It is planned to calculate local VA in terms of 'net production cost', as opposed to ex-works value (the basis for those tariff lines where VA was

used as a criterion under Cotonou). Two impact assessments are mentioned as having been commissioned. One will model the trade effects of requiring different levels of local VA for textiles and clothing as a product group. The other will model the 'development effects' of different standard VA thresholds. Final proposals will not be drafted until these are complete. The only sector dealt with separately in the Communication is fisheries, where it is stated that all existing requirements on composition of crews will be definitely removed, and that an (unspecified) simplification of vessel ownership requirements will also occur (see Appendix 2).

The Communication repeats past EU assertions that provision for cumulation will secure a link between RoO and development objectives. In addition, cumulation is portrayed as contributing to regional integration between developing countries. Reference is made to extending full cumulation, including through the possible designation of new regional groups.

As far as 'efficiency' and 'enforcement' are concerned, the Communication states that the EU will require registration of all exporters utilizing PTAs. Customs Departments in exporting countries will be required to conduct assessments of the financial records of all such exporters, provide a list of them to the EU and monitor them on a regular basis. Customs Departments will also be required to report regularly to the EU on how such arrangements are working, 'actively cooperate' in any investigations undertaken and assume financial liability in cases of fraud. The 'extension or revision of an existing (preferential) relation' with a beneficiary country will be conditional upon an EU assessment that the Customs Department of this country has the capacity to implement such a system.

The Communication has still not been followed by a Draft Regulation. Initially it was stated that a Draft Regulation would be published in mid-2006; later, March 2007 was given as a date. Correspondingly, the EU has made no concrete proposal on RoO in the EPA negotiations and, to date, has not replied to the few formal and semi-formal proposals tabled by ACP countries. Indeed, indications are that there may not be a proposal from the EU's side, until a broad framework on tariff reductions have been reached for agreements on trade in goods with the different EPA regions.

This impression was reinforced by the fact that as recently as June 2007 the Commission initiated another consultation on revision of PTA Rules of Origin, this time in respect of the level at which the standard VA threshold should be set, as well as on 'how value should be calculated, whether there

should be a list of insufficient operations...and whether the definition of wholly obtained products should remain unchanged' (SJ Berwin's Community Week, 22 June 2007).<sup>27</sup>

### Criticisms of the EU Communication

To date, the EU Communication has attracted rather little discussion, considering the controversial status of RoO. Furthermore, most discussion that has occurred is confined to practical issues rather than questions of principle. The main exception is a Non-Paper<sup>28</sup> by the EPA Pacific Group, where the use of the VA method is criticised on the grounds that, together with the emphasis on cumulation, it assumes the regional presence of significant levels of internationally competitive supply capacity. In the Pacific (and other) EPA region(s), markets do not exist on a scale where local production of specialized inputs could ever be competitive. As the 'VA + cumulation' method biases exporters to buy regionally, their exports to the EU become uncompetitive unless margins of preference are exceptionally high. Even then, exports outside the ACP will remain uncompetitive. Furthermore, 'VA + cumulation' penalises ACP exporters from participation in truly global supply chains, which are credited with creating a variety of efficiency spillovers (Pacific Group 2006).

Some of the practical issues raised also have important implications. Naumann (2005) refers to two general problems with basing RoO on VA methods. Firstly, a disincentive is created to efficiency gains by exporters, since marginal reductions that are attained in local costs may be reflected in local VA shares that are lower overall. Secondly, the magnitude of local VA shares will depend to a considerable extent on currency fluctuations, which are completely beyond the control of local exporters.<sup>29</sup> Naumann goes on to observe that verification of specific levels of local VA will carry considerable firm-level administrative costs, relative for example to verification of foreign content costs (which he proposes as an alternative).

Somewhat surprisingly, no criticisms of the administrative and wider verification costs of the new proposed system appear to have occurred. This is striking given the finding of Cadot et al (2005a) that purely administrative costs associated with Cotonou RoO make up the larger part of the latter's overall costs of compliance. The system now proposed imposes large additional costs on Customs Departments in beneficiary countries, and threatens those countries unable to meet them with withdrawal of preferences. The scale of the potential problem involved is indicated in a document produced for the Pacific Group (KVA Consult 2003) which reports that, of the Customs Depart-

<sup>27</sup> The consultation announced was in the form of a letter to various European Industry Associations inviting their views.

<sup>28</sup> A 'Non-Paper' is a contribution to discussion rather than a formal proposal. There is no obligation on other parties to reply to it.

<sup>29</sup> This point is also made by the Pacific Group Non-Paper (op. cit.).

ments in the Group's 13 member countries, 7 had 'limited' or 'no awareness' of current EU RoO requirements, 4 had not yet adopted the HS system of classification, and 3 were signing EUR 1 forms without any attempts at verification.

### Discussion around appropriate VA thresholds

While the EU has yet to draft proposals on product-specific VA thresholds, claims have been made that it has floated suggestions for thresholds for some specific product groups. Campling (2007), for example, states that a threshold of 40% has been floated for canned tuna (a threshold which he dismisses as unrealistic on the grounds of the exceptionally high international price of whole tuna).

ODI (2006), in a study carried out for the Dutch Development Ministry, takes existing average levels of VA by exporting firms in developing (and all) countries as an alternative point of entry to this discussion. This approach is adopted on the basis of two arguments. Firstly it is claimed that, if the main purpose of a RoO is to prevent trade deflection, then any VA threshold that is higher than the level typically contributed by an exporter will be restrictive. Secondly, it is argued that the change to VA thresholds provides the opportunity for the EU to allow its RoO to reflect the current realities of production on the basis of global value chains, rather than outdated assumptions about vertical integration.

Complementing trade data with UNIDO data on manufacturing VA for exported goods, the study arrives at three main findings. Firstly, the average VA in the manufactured exports of all countries varies greatly between (ISIC) product groups, ranging between processed meats (24%) and ceramics (48%). Secondly, for each single product group there are significant differences between the average VA in the exports of low-income and low-middle-income countries. Taking meat products as an example, average manufacturing VA in low-income countries is 21%, while in low-middle-income countries it is 29%. The differences are much larger for product groups such as clothing and sports equipment. However, there are no significant differences between the average manufacturing VAs of LDCs and those of other low-income countries. Thirdly, in the small minority of tariff lines where Cotonou currently uses (ex-works) VA as a method for determining origin, its thresholds are in a range of 30%-130% higher than the actual average manufacturing VAs achieved by low-income countries.<sup>30</sup>

The study concludes by proposing that the EU sets VA thresholds for each product at the lowest of the three scores (all countries, low-middle income countries and low-income countries) for the

<sup>30</sup> In announcing a second round of consultation on its PTA RoO in June 2007, the Commission stated that '(a) 60% threshold (would be) broadly equivalent to the current rules of origin'.

product groups covered by the survey. In the great majority of cases this would mean a threshold between 20% and 35%.

### Other Counter-Proposals

RoO was originally part of the all-ACP agenda during Phase I of the negotiations, but as with other many other issues, discussion was confined to the realm of generalities. The ACP group proposed 'an improved and simplified system, which contributes both to regional integration and the preservation of preference margins', improved opportunities for cumulation and non-reciprocity in RoO content. While the EU rejected the last of these proposals, it argued that its own evolving proposals would meet the first two. The task of drawing up more specific proposals was referred to 'expert groups'.

During Phase II of the negotiations, more concrete counter-proposals have been made on the ACP side, though mostly in the form of recommendations from expert groups and consultants. Two proposals have been tabled by regional groups, one by the ESA group (to which the EU has yet to reply) and one by the Pacific Group – initially in the form of the Non-Paper already referred to.

These counter-proposals refer both to the general methods which should be used to determine origin, as well as making more specific statements on the problematic rules for fish/fish products and clothing (see Appendix 2). The ESA proposal, tabled in early 2006 (Julian 2006), expresses a general preference for retaining 'wholly originating' and CTC, rather than VA, as the main methods used to attribute origin. In relation to the CTC criterion, it is not stated at which level of HS classification change should be required. The Caribbean and Pacific ACP groups appear to have made similar proposals, although draft versions are not available in these cases (ECDPM 2007).

The main emphasis in these proposals seems to be on use of the CTC method. This emphasis is also found in more refined form in a proposal made by Paul Brenton of the World Bank in a presentation to the ACP Secretariat (Brenton 2006). Brenton suggests that tariff classification change at the 6-digit sub-heading would be the most appropriate for EPA rules. The argument for favouring a liberal CTC requirement is that it would support the expansion of labour-intensive industries and the inclusion of African enterprises in global value chains (with the benefits already referred to), while minimising verification costs. The author adds that all ACP exporters should be allowed to choose between this method and a cross-the-board 10% VA requirement. While Brenton (op. cit.) states that this would obviate the need for complex cumulation provisions, the ACP proposals referred to above all continue to call for cumulation.

For fish/fish products, proposals from the ACP Group of Experts (Landell Mills 2005) favour an extension of qualification for 'wholly obtained' status for whole fish to ACP countries' entire EEZs.

For processed fish they favour a rule based again on a change in 6-digit HS classification. Exactly the same proposals on fish are embodied in the Pacific Group Non-Paper, and also appeared in an earlier ESA proposal (for an ESA Regional Fisheries Agreement). Similar proposals have been discussed in the SADC group, although here – prior to South Africa’s admission to the SADC ESA – there was also a strong emphasis on allowing cumulation from South Africa.

On textiles there is a greater variance in proposals. Part of the ESA group proposal was that the AGOA ‘third country fabric’ provision be substituted for Cotonou rules, for all ESA members. This entails a 35% VA threshold. A study for the SADC group (PWC 2007) likewise proposes a ‘liberal’ VA threshold, which could be gradually raised over time. On the other hand, Brenton and Manchin (2002) propose a single CTC (6-digit level) for clothing, as does a study for the Pacific Group by KVA Consult (op. cit. 2003). Brenton and Manchin argue that probable opposition to this proposal in the EU could be allayed by provision for a Safeguard Mechanism.

While there is considerable unevenness in the emphasis and level of detail in proposals by (and for) the ACP countries, some convergence thus seems to be emerging, toward proposing a method where a rule based on CTC (where this is specified at all, at the 6-digit level) as at least an alternative to a VA rule.

## CONCLUSION

PTA RoO are typically of Byzantine complexity. They are also typically restrictive. A growing consensus amongst trade economists suggests a clear link between restrictiveness and under-utilisation, namely: tariff lines with the highest levels of preference margin are normally subject to the most restrictive RoO. Except in the case of whole fish, the main losers seem to be non-LDCs, since these are the main exporters of high preference margin products. Restrictiveness translates into costs of RoO compliance that are very high. Two separate studies of Cotonou’s trade-weighted compliance costs place these in a range between 8.0-8.4% ad valorem.

The main EU defence of its RoO is that their provisions for full cumulation promote development and regional integration. A similar argument is made on behalf of the highly restrictive clothing rule, where this is combined with full cumulation. On the other hand, a case study comparing African clothing exports under Cotonou and AGOA appears to show that, while a combination of a highly restrictive rule and full cumulation hinders trade creation, a neutral RoO promotes both trade creation and export diversification (see Appendix 2).

The problem with the EU’s defence of its RoO approach is that it remains wedded to an outdated model of the global economy, where national and/or regional vertical integration was the rule.

Today production typically occurs in global value chains, where different stages of production are dispersed between countries exhibiting different development characteristics. The global value chain model, originally applying only to light manufactures, now applies to manufacturing in general as well as to some services.

EU RoO proposals for its PTAs, including EPAs, are described in its Communication of 2005. While proposing a methodological change to a VA criterion, they are based on the same assumptions as earlier generations of the RoO. The only empirical study on VA thresholds suggests that any product-level threshold set above 30-35% can be regarded as restrictive. A liberal or neutral VA-based rule would entail the EU having to make deep cuts in its existing VA-based origin requirements, where these are applied. The new rules proposed also appear likely to increase administrative costs of conformity, at least in the short term.

The ACP negotiating groups that have made proposals (as well as some academics) argue that a CTC method would be more development-friendly than a VA requirement. Brenton's remains the only effort to specify which level of change in HS classification such a rule might refer to. While Brenton argues that setting the requirement at this level could dispense with the need for unwieldy and ineffective cumulation provisions, ACP countries appear to wish to retain or extend provisions for cumulation.

While there is general agreement that the EU RoO is unduly restrictive, that this restrictiveness continues to be embodied in new EU proposals, and that a change to a 6-digit CTC rule would be more likely to lead to trade creation, the likely level of supply response to any significant reduction in restrictiveness remains unclear. This is underlined by a recent attempt to model the effects of a 10% reduction in the price of exported goods for SADC EPA region processed fish and clothing exports to the EU (PWC 2007). For processed fish, only Namibia experiences a significant increase in exports (of 10.9%). For clothing, there are increases in exports to the EU for most SADC countries in a range between 50% and 80%. However, given the negligible level of existing clothing exports to the EU, the overall impact is tiny. The authors note: "The dependence on the US market has created a structure of production and export that has become embedded, to the point that... even with more liberal RoO gains will be limited" (op. cit., 48). Supply capacity and low levels of investment remain serious problems constraining responses. Neutral RoO are a necessary condition for them to be overcome, but by no means a sufficient one.



## 4. Trade Defence Provisions in EPAs

Generally speaking, the issue of whether and how EPAs should deal with trade defence mechanisms, such as Anti-Dumping and Safeguards, has not been subject to in-depth analysis or discussion and has been raised only in connection with the EU's Agricultural subsidies. Furthermore, the little discussion that has occurred seem to rest on some misunderstandings on what Anti-Dumping and Safeguard mechanisms are. In order to clarify some of these misunderstandings it should be stated that Anti-Dumping duties are those extra duties that an importing country may impose on specific products, when their exporting producers have dumped them in the country. Thus it is a country's response to actions by private companies. Safeguards on the other hand are those measures a country may apply 'to protect a specific domestic industry from an increase in imports of any product which is causing, or which is threatening to cause, serious injury to the industry' (WTO).

Countries' responses to subsidies provided to other countries' export industries are called Countervailing Measures. The EPA literature seems to confuse Countervailing Measures with Safeguard Measures, when it is argued that ACP countries should be able to apply safeguard actions against 'subsidised' agricultural products from the EU. As an example a note by Oxfam writes that Pacific countries during the EPA negotiations have proposed that 'they can challenge subsidies that cause damage to the Pacific but not vice versa. This could potentially be used to restrict the 'dumping' of subsidised EU agricultural exports' (Oxfam 2006a: 10)

Based on this clarification, discussions on Anti-Dumping and Safeguard Measures within EPAs are reviewed below.

### EPAs AND ANTI-DUMPING MEASURES

The issue of Anti-Dumping in EPAs has not been addressed in any detail in the existing literature. Three reasons can be given for this: 1. Cotonou itself does not refer to the issue; 2. Anti-Dumping policy and remedies are rather technical and cannot be dealt with without considering their embodiment in specific ratified regulations. The final wording of EPAs has not yet been agreed, and the negotiations as such have not completed the more general stage. Thus the status of Anti-Dumping under EPAs is unclear; 3. Traditionally Anti-Dumping duties have not been used by ACP countries (South Centre 2007b), and it is not likely that EPAs will change this. Furthermore, economically speaking, Anti-Dumping is not an advisable action, especially for a small country against a large country, when it is the imposing country that will be harmed (Dunn Jr. and Mutti 2004).

Furthermore, it should be mentioned that there is a general discussion between WTO-law experts on whether Anti-Dumping and Safeguard Measures can be applied at all within a Free Trade Area.

The discussions centre on GATT Art. XXIV.8.b. which reads as ‘A free-trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.’ This subparagraph explicitly lists the exceptions that can be applied in a free trade area: GATT Arts. XI (on certain import and export restrictions in the agricultural sector), XII (on Balance of Payments), XIII (on non-discrimination in application of quotas), XIV (on Balance of Payments), XV (on complying with IMF requirement) and XX (on general exceptions to GATT-rules). Thus ‘the absence of Articles VI [on Anti-Dumping] and XIX [on Safeguard] of the GATT in the exceptions list in Article XXIV:8 has raised the question of whether this provision mandates or allows abolition of trade remedies within customs unions and FTAs’ (Gobbi and Horlick 2006: 111). Gobbi and Horlick argue that, based on the Appellate Body’s Ruling in Turkey – Textiles, which states that ‘we note ... that the terms of subparagraph 8(a)(i) provide that members of a customs union may maintain, where necessary, in their internal trade, certain restrictive regulations of commerce that are otherwise permitted under Articles XI through XV and under Article XX of the GATT 1994’ (WT/DS34/AB/R para. 48), parties in a customs union (as well as in a FTA) can only use the stated exceptions. Thus at least within that portion of trade in a FTA, which can be regarded as ‘substantially all the trade’ between the parties, they are mandated to abolish Safeguard and Anti-Dumping measures (ibid.).<sup>31</sup>

Regardless or unaware of this discussion, some reports suggest that EPAs could nevertheless allow EU to impose Anti-Dumping measures against products from ACP-countries. Against this, the Pacific and the Caribbean countries have called ‘for an EC commitment to not apply Safeguard, Anti-Dumping nor Anti-Subsidy Measures in EC – Cariforum [and Pacific region] trade’ (Julian and Makhan 2006: 6; Oxfam 2006a).

## EPAS AND SAFEGUARD MEASURES

Safeguards have attracted more attention in the literature than Anti-Dumping. The reason for this is that Safeguards are explicitly addressed in Arts. 8-11 of Annex V to Cotonou, and that ACP countries may therefore be able to initiate a dispute or to apply safeguard measures against the EU if their industries are threatened by imports from the EU. However, while the referred Articles allow EU to apply Safeguard Measures, they are silent on whether ACP countries have the same right. Furthermore, although the Articles instruct EU to consult the ACP countries prior to the application of Safeguard Measures (Art. 9.1), they also state that ‘the prior consultations ... shall not

<sup>31</sup> The term ‘substantially all the trade’ is addressed in Chapter 3.

prevent any immediate decisions which the Community, in accordance with Article 8(1), might take where special factors have necessitated such decisions' (Art. 9.3).

This rather one-sided provision for Safeguard Measures under Cotonou has caused NGOs and ACP countries to question the nature of any planned Safeguard regime under EPAs (Stevens and Kennan 2005a; South Centre 2007) and demand that the EU not apply Safeguard Measures in the new regime (Julian and Makhan 2006; Oxfam 2006a).

Regardless of this discussion and even if EPAs do not specify whether ACP countries may apply Safeguard or Anti-Dumping Measures, it could be argued that ACP countries as WTO-members have the right to use WTO's Dispute Settlement Body to initiate a dispute against any other WTO-member's actions and measures, e.g. the EU's Anti-Dumping or Safeguard Measure (Pauwelyn 2004). However, the WTO can only address a dispute which deals with countries' WTO obligations and not those obligations that are solely addressed in a Free Trade Agreement (see e.g. Cottier and Foltea 2006). Thus any potential claim against the EU before the WTO Dispute Settlement Body must deal with the WTO compatibility of such measures and not their EPA compatibility.

## CONCLUSION

As stated above, the limited discussion that can be identified in the literature on the status of Anti-Dumping and Safeguard Measures within EPAs seem to rest on a misunderstanding. Furthermore, the current state of the WTO-law seems to require countries to abolish such measures in their Free Trade Areas. Regardless of this demand, the EPAs may inherit from Cotonou a rather imbalanced Safeguard regime, where only the EU has the right to apply such measures. This has been criticized by NGOs and ACP countries, with some justification.

## 5. Sanitary and Phytosanitary Standards in the EPA Negotiations

Sanitary and Phytosanitary Standards (SPS) have been an increasingly controversial trade policy topic in the last two decades. The central issue in this discussion is the extent to which SPS measures are devised and used in a manner disproportionate to the risks of human, animal and plant disease that they ostensibly address. A turning point in the discussion came with the adoption of the SPS Agreement at the conclusion of the WTO Uruguay Round in 1995. Whereas up to this point, the main theme of discussion was the need to regulate SPS measures, since 1995 it has revolved around the shortcomings of the Agreement firstly in slowing the march of disproportionate measures and secondly in mitigating adverse trade outcomes in developing countries of all SPS measures (whether disproportionate or not). Since the SPS provisions of the Cotonou Agreement (Articles 47 and 48) are based in essence on the WTO SPS Agreement, and since it seems very likely that the SPS provisions of EPAs will also be largely based on it, discussion of SPS measures in relation to EPAs tends to repeat the central themes found in the discussion of SPS in the WTO context.

### RECENT DEVELOPMENT OF SPS MEASURES IN THE EU

Three current areas of discussion concerning EU SPS measures and developing countries can be identified. Firstly, the EPA negotiations have coincided with the adoption and the first stages of implementation of what is widely acknowledged to be a new EU Food (and animal feed) Safety regime. The central elements of this regime are six new regulations covering traceability, food and feed hygiene, special rules for food of animal origin, and controls for verification of compliance with food and feed law.<sup>32</sup> The general direction of the regulations is to move further away from official monitoring of food safety standards in individual establishments towards requiring national systems of control that assure the internalization of acceptable production/process methods and management controls by responsible private operators.

Broadly, more rigour is expected of national systems of control and of establishments involved in the production of food, both in the EU itself and in countries exporting to the EU. For countries to be considered safe sources of food, their national authorities must put in place adequate procedures for monitoring establishments, managing systemic risk and providing accurate and up-to-date

<sup>32</sup> The regulations in question are EC 178/2002 (traceability), 852/2004 (food hygiene), 853/2004 (food of animal origin), 854/2004 (controls for food of animal origin), 882/2004 (controls for verification of compliance with food and feed law) and 183/2005 (feed hygiene). For good overviews, see Graffham (2006) for fruit and vegetables and Reilly (2006) for fish.

information to the EU on their control and risk assessment procedures. For all food-producing establishments, 'Hazard Analysis Critical Control Point' (HACCP) systems<sup>33</sup> must be put in place that have clear procedures for identifying and controlling for risks and hazards and for managing their occurrence – although Guidance Notes to Regulation 882/2004 (2006) state that 'these may be adapted to (particular) situations'. Registration of establishments becomes mandatory exporters of plants and plant products, and requirements for certification by competent authorities prior to export become mandatory for some categories of plant products. All these requirements previously existed in respect of food of animal origin, but are now becoming more general (although by no means generic).

Secondly, the EPA negotiations also coincide with two further EU legislative processes that impact directly on developing country producers. These are the Minimum Residue Level (MRL) Harmonization Programme for pesticides and the Pesticide Approvals Review Programme. The former is aimed at establishing common and mandatory MRLs across the EU for all active ingredients introduced after 1993, while the latter is aimed at reviewing the registration of the 823 active ingredients approved within the EU prior to 1993. Renewal of registration of older ingredients and the establishment of new harmonized MRLs for newer ones is on the basis of applications by chemical manufacturing companies, who must generate and supply data in order to establish safe (levels of) use. Where no data is provided, then the ingredient is automatically considered unsafe at trace level. Commentators (O'Connor & Co 2002, Cerrex 2003, Doherty 2006) have pointed to the probability that, because of the costs involved, companies will (re-)register only those ingredients that are used for major temperate crops and which remain in patent. There is particular concern that key post-harvest fungicides commonly used in developing countries will not be registered, and therefore that products using them will be excluded at EU borders.

A third area of concern raised in relation to EU SPS measures is the proliferation and apparently widespread adoption within the EU of private (mainly process-based) standards for food production, which are used prescriptively to fill the gaps within the legislative framework. These standards tend to be designed by major retail chains or consortia of them<sup>34</sup> and conformity to them becomes a de facto entry requirement to the more remunerative parts of the EU market.

<sup>33</sup> 'The HACCP system is a science based and systematic strategy that identifies specific hazards and measures for their control to ensure food safety. HACCP is a tool to assess hazards and establish control systems that focus on prevention rather than relying mainly on end product testing. HACCP can be applied throughout the food chain from primary production to final consumption...' [www.handwashingforlife.com/us/english/resource\\_center/glossary.htm](http://www.handwashingforlife.com/us/english/resource_center/glossary.htm)

<sup>34</sup> Examples include proprietary standards like the UK supermarket Tesco's 'Nature's Choice', or ones designed by retail consortia such as BRC and EurepGAP.

## SPS AND WTO

The WTO SPS Agreement affirms the right of members to set human, plant, and animal health standards but qualifies this in three ways. Firstly, these standards should be proportionate to their stated health objectives; secondly, they should not discriminate between products except on grounds of differences in the health risks that they pose; and thirdly, while they may be higher than international standards laid down in the Codex Alimentarius and related international standard-setting organizations,<sup>35</sup> departures from international standards shall be notified to WTO and supported by scientific principles and evidence and by a risk analysis. In cases where no scientific evidence is available concerning a risk, then members may impose a new standard on a precautionary basis, until evidence becomes available and/or a risk analysis becomes feasible. The Agreement further mandates efforts to harmonize standards and to establish standards equivalency agreements (Art. 4). In addition, it encourages members to consider applying exclusions of products based upon health grounds to specific regions within exporting countries rather than to an exporting country as a whole (Art. 6).

There are two Special & Differential Treatment (SDT) measures in the Agreement. The first gives developing countries a longer time frame for implementation of the Agreement (now expired), while the second establishes a non-binding requirement for developed countries to provide technical assistance (TA) to developing ones. Requests for TA may be channelled through a WTO SPS Committee, which also provides a forum for ad hoc but non-mandatory consultation on new measures.<sup>36</sup>

Some aspects of the SPS Agreement have been raised in proposals on cross-cutting issues such as SDT. Here, Kenya, India, and Egypt proposed that it should be mandatory for countries notifying new standards to consult over them and to provide TA to facilitate their implementation in developing countries, while the African Group proposed that no new standards affecting developing countries shall be imposed by developed countries, unless the latter make TA for conformity automatically available (Bridges Trade Weekly, 9 (24), 6 July 2005).

<sup>35</sup> The Agreement also refers to the International Office of Epizootics and to the International Plant Protection Convention.

<sup>36</sup> It should be noted that a large number of developing countries have outstanding requests for TA noted by the SPS Committee (Chemnitz and Günther 2006). However, a large majority of SPS aid by-passes the Committee.

Furthermore, the SPS Committee has provided an informal forum throughout the Doha Round for developing countries to raise not only individual standards but issues of general principle. Those raised as a result include:

- Modifying the Agreement to specify the quantity and type of scientific evidence necessary to justify a new measure that exceeds international standards (Doherty 2007)
- Modifying Arts. 4 (on promoting recognition of equivalence between similar standards) and 6 (on facilitating regional as opposed to national exclusions) in the light of what is regarded as their gross underutilization, by providing clear guidelines for when such actions are mandated (Doherty 2007)
- Modifying the provision on precautionary measures in order to specify the steps (short of using the WTO Dispute Settlement Mechanism) that could be taken by members to force the removal of such measures, where they lose market access as a result (Doherty 2007)
- Ensuring that the Codex Alimentarius adopts MRL standards for more pesticides used in developing countries, in order that these can be referred to in WTO consultations/disputes where the EU or other members set standards exceeding these (Bridges Trade Weekly 11 (24) 4 July 2007)
- Clarifying the Agreement so that its provision that ‘members should take reasonable measures ... to ensure that non-governmental entities within their territories comply with the Agreement’ is explicitly extended to cover the private standards of supermarkets (Bridges Trade Weekly 9 (24) 6 July 2005).

In each of the above cases, the response of developed countries has been lukewarm.

## ACP AND NGO PROPOSALS ON SPS AND THE EU’S RESPONSE

Art. 48 of the Cotonou Agreement affirms the parties’ commitment to the WTO SPS Agreement ‘taking account of their respective levels of development’ (but without stating what this might entail). The parties also undertook to reinforce coordination, consultation and information as regards notification and application of proposed measures. However, no specific forum was identified for this purpose. Nor did the parties enter into additional commitments concerning the promotion of equivalence exercises.

All the EU’s other bilateral trade agreements also refer to the WTO SPS Agreement as a basic framework, and none grant SPS ‘preferences’ akin to tariff reductions. However, two of the EU’s

bilateral agreements, trade agreements with Israel and Chile,<sup>37</sup> contain measures that mitigate compliance costs and create greater security against arbitrarily introduced measures for partner country exporters (Rudloff and Simons 2004).

Despite the magnitude of the issues concerned, SPS measures have not been a significant focus of ACP country attention during the EPA negotiations. During the all-ACP first phase of the negotiations the ACP group variously proposed that there should be a moratorium from September 2003 on all new EU SPS measures, that there should be 5-10 year derogations for ACP countries on compliance with all new EU SPS measures, and that a programme should be adopted to allow the conclusion of more national equivalency agreements. The EU rejected the first two of these proposals as unrealistic and as in conflict with its consumer protection obligations and stated in relation to the third that it could only begin to negotiate equivalency agreements, where the conditions for them had been demonstrated to exist. At the same time, the EU signaled its willingness to establish a consultation forum with the ACP on new SPS measures, but professed itself otherwise unwilling to go beyond its obligations under the WTO SPS Agreement (op. cit., 22). In the regional phase of the negotiations the ACP countries have seemingly dropped the first two proposals and have focused on capacity building issues.

In this regard, Doherty (2006), following Cerrex (2003), argues that conformity with the evolving EU food safety regime entails major capacity building for ACP countries, both in their public and their private sectors. In ACP countries' public sectors, the critical capacity necessary is that of enforcing standards according to the basic philosophy of the new EU regulations. Doherty (2007) claims that this entails capacity to understand modern food law and regulation, to practice coordinated food control management, to put into the field a well-trained and effective inspectorate, to have a reasonably full range of accredited laboratory services, and to have a functioning platform for exchange of information and consultation with the private sector. Doherty puts the initial investment cost of this at €2+ million per country, assuming that there are also regional level facilities available for each EPA configuration. Initial investment costs for the latter are put at €5 million. No estimates are given of recurrent costs. A close reading of the Guidance Notes (op. cit.) suggests that, in practice, it is unlikely that countries exporting food of non-animal origin will require such extensive capacity building, at least in the medium term.

<sup>37</sup> The agreement with Israel has a provision mandating (rather than simply permitting) consultation in the event of the introduction of new measures, and also allows some product exceptions from certification requirements under the EU's food hygiene regulations, based on risk analyses. The agreement with Chile goes further by mandating specific procedures to be followed in its consultation forum and by setting out relatively precise and helpful guidelines of the requirements to be followed in establishing equivalence both of standards and of accreditation procedures for certification and testing.



A more serious issue is that of the capacity of ACP private sectors to meet the requirement for a move toward HACCP systems. The only empirical estimates available for HACCP adoption on a sector-wide basis concern examples where this was accompanied by a wider upgrading of hygiene standards. The best known is Cato and Santos's (2000) study of the costs of adoption of a HACCP+ system for operators in the Bangladesh shrimp sector, following a EU import ban in the late 1990s. This corresponded to \$18.4 in initial investment costs and \$2.4 million annually in operational costs.

### Trade assistance and capacity building

Across the regions, a common focus on enhanced TA has emerged, in some cases accompanied by a call for the European Commission's DG Development to participate in the formal discussions. The SADC and ECOWAS EPA groups appear to have adopted regional capacity building shopping lists, or are in the process of doing so (op. cit., ECDPM 2007). The EU has indicated that it 'will adopt a flexible and understanding attitude to the SDT measures required in relation to the capacity building needs of the ACP countries' with two provisos. Firstly the ACP countries must accept that 'the principle of SPS measures (consumer protection) is not eroded' and secondly, the EU will finance capacity building only from the 10<sup>th</sup> EDF or existing programmes. There are currently two such programmes available on an all-ACP basis, Strengthening Fisheries Products' Health Conditions and the Pesticide Initiative Programme.<sup>38</sup> The Pesticide Initiative Programme is of interest, since it is aimed at assisting ACP producers conform to the new EU pesticide regime (see above), mainly by adapting production techniques – although one component of the programme concerns adaptation of the EU's own regulations.<sup>39</sup> There are also several bilateral and multilateral programmes aimed at specific ACP countries, or groups of them, together with non-ACP ones.

### Harmonization

The issues of harmonization and equivalence have been raised in different forms in the ESA and SADC groups. The SADC EPA group has proposed that the EU secure full harmonization of its member states' SPS measures (rather than tolerating EU+ standards in some), while the ESA EPA group has proposed that the EU's SPS requirements be systematically harmonized (in effect, in many cases reduced) to the standards adopted by the Codex and its sister standard-setting organizations. The EU has not formally responded to either of these proposals (Chemnitz and Günther 2006).

<sup>38</sup> These programmes date from 2002, when €42 million and €29 million, respectively, were committed to them.

<sup>39</sup> A much larger EU programme, the Pan Africa Programme for the Control of Epizootics addresses animal disease issues in Central Africa. In addition to this, ACP countries have access to multilateral facilities such as the World Bank Standards and Trade Development Facility. Kenya has been a major beneficiary of this programme, but most ACP countries have received minimal or no assistance through it (Chemnitz and Günther 2006).

The only NGO forum to have actively addressed SPS issues in relation to EPAs is the consortium of ESA country NGOs following the negotiations in this region. This consortium has issued a call for the EU to respond during the EPA negotiations to some of the proposals listed above as having been raised by developing countries in the WTO SPS Committee during the Doha Round. In addition they raise the issue of EU+ standards in some member states and propose the simplification of EU traceability requirements for livestock (without specifying the mechanisms involved) (ECDPM 2007).

## ACADEMIC AND CONSULTANT COMMENTARY

Independent commentaries on the integration of SPS measures into the EPA negotiations coincide in focusing mainly on securing enhanced access to TA and on the detailed formalization of a EU-ACP consultation mechanism that the EU appears to have conceded. On TA, Chemnitz and Günther (2006) and Doherty (2007) both call for more detailed and reasoned specification by ACP countries of their TA needs. Doherty supplements this with a call for the ACP countries to also make full use of the TA provisions unveiled in Regulation 882/2004. Doherty further calls for a re-orientation of ACP demands for automaticity of TA away from their existing reference to all new EU SPS measures and towards those SPS measures, where the EU invokes the precautionary principle. On the consultation mechanism, Chemnitz and Günther call for procedures allowing for mandatory consideration of 'least harmful' (to developing country exports) conformity mechanisms of new SPS measures, as well as for an improved and more binding early notification procedure linked to (an unspecified) improved strengthening of ACP capacity.

Somewhat surprisingly, neither these nor other academic commentaries make specific proposals in respect of mitigating the implications for ACP countries of the new EU pesticide regime, and nor do they explicitly call for simply carrying over the SPS provisions of the EU-Chile FTA to the EPAs.

## CONCLUSIONS

EU food safety regulations are moving in the direction of requiring enhanced national systems of control and adoption of HACCP-type systems for managing food safety risk, although over the short-medium term these requirements are likely to be applied with considerable flexibility. At the same time, a new EU pesticide control regime is emerging, which is likely to make illegal the application of a large number of chemicals commonly used in the tropics.

The WTO SPS Agreement forms the basis for SPS provisions in all the EU's bilateral trade arrangements, although the Agreement has been criticised by developing countries as inadequate in a number of areas. While no EU bilateral agreement provides 'concessions' on SPS similar to tariff

reductions, those with Israel and especially Chile contain provisions that mitigate some of the problems arising from lack of clarity in the WTO Agreement.

Little has been written on ACP capacity building requirements in relation to the new EU food safety regime, and the estimates that are available of the costs of upgrading national authorities to EU standards may be inflated. They may be no more than €100 million for the ACP as a whole, and it should be possible to cover them within existing or programmed EU assistance. However, costs for enhancing the conformity of ACP country private sectors are several times higher, and it is unlikely that they can be met without an expansion of envisaged assistance.

Within the EPA negotiations, the ACP countries are currently focusing mainly on obtaining enhanced TA for upgrading their public capacity in SPS, having dropped more radical demands such as a moratorium on new SPS measures. Recently, they have also focused more on the issue of harmonizing EU standards internally, as well as externally, in relation to those of international standard-setting organizations. It is unlikely that the EU will consider the latter proposal seriously.

There is clearly some way to go before the ACP countries formulate systematic (needs assessment-based) lists of capacity building measures that they need assistance for in order to meet the requirements of the emerging EU regime. The ACP countries would certainly be seriously handicapped if the negotiations concluded before they could put forward these lists. Another immediate and realistic priority would be to gain agreement on regarding the SPS chapter of the EU-Chile FTA as a floor for SPS provisions within all EPAs, that could then be improved on by the ACP countries on a region-by-region basis. This leaves untouched the question of how to deal with the new EU pesticide control regime, where the best option may lay in joining forces in the Codex and in WTO with the countries most active on this question, such as Argentina. The route here implies more active engagement in the Codex followed possibly by use of the WTO dispute procedure.

## 6. WTO+ Issues in the EPA Negotiations

WTO+ issues refer to two types of matters. Firstly, those issues that are not addressed in the WTO, most importantly the four Singapore issues raised by the EU in 1996 in the first WTO Ministerial in Singapore – hence the name. These issues are Trade Facilitation, Government Procurement, Competition and Investment. Second, those issues that are covered by the WTO, but which negotiating parties in regional trade agreements decide to address in deeper or broader terms, such as TRIPs.

In this section the focus will be on the first group of WTO+ issues and more precisely on investment rules, since the debate on the WTO+ issues within the EPA negotiations and the literature dealing with it has mainly dealt with investment. This situation should be seen as a consequence of three underlying conditions: Firstly, in general, because of resistance from developing countries during international trade negotiations, the WTO+ issues have lost their importance. As known, during the Doha Round, the EU has been advocating the inclusion of these issues in the WTO. The mandate of the negotiations on these issues is expressed in paras 20-27 of the Doha Declaration and states that negotiations ‘will take place after the Fifth Session of the Ministerial Conference on the basis of a decision to be taken, by explicit consensus, at that Session on modalities of negotiations’. But during the Fifth Session in Cancún, many developing countries objected to starting negotiations on three of the four Singapore issues and the required explicit consensus was only achieved on Trade Facilitation, which is now part of the Doha negotiations.

Second, developing countries have also objected to the inclusion of these issues in the EPA negotiations. Part of their argument is that the WTO does not require regional trade agreements to include these issues. Third, since the EPAs negotiations are not as advanced as they are supposed to be, the EU’s original emphasis on inclusion of these issues in the EPAs negotiations has also diminished. This softening of approach can be seen by comparing the statement of Pascal Lamy, previous EU Trade Commissioner, in 2004, which claimed that ‘investment, public (government) procurement and competition are areas which we [the EU] are always addressing in our bilateral free trade agreements’ ([www.bilaterals.org/article.php?id\\_article=610](http://www.bilaterals.org/article.php?id_article=610)) with the Deputy Director-General of Trade, Mr. Falkenberg’s statement in 2006, which only emphasized investment rules as a necessary component of any EPA ([www.bilaterals.org/article.php?id\\_article=5206](http://www.bilaterals.org/article.php?id_article=5206)).

Meanwhile, the few references that can be identified in the literature point to a general disagreement between EU on one side and ACP countries and NGOs on the other. The substance of the debate can be summarized as the EU insisting that investment rules are necessary for establishing the ‘development-friendly’ EPAs, mainly in the sense that they will attract foreign direct investment (FDI) to the ACP countries ([www.bilaterals.org/article.php?id\\_article=5206](http://www.bilaterals.org/article.php?id_article=5206)). Against this argument, other sources argue that business-friendly investment rules are not necessarily followed by actual FDI. As

an example, a report by a group of NGOs states that ‘although Africa has joined the rush to sign bilateral investment treaties, levels of FDI there have generally declined. Angola has proved more attractive in per capita terms than Egypt and Nigeria, indicating that there are pull factors other than a predictable and transparent environment’ (Christian Aid 2006: 10).

Furthermore, it is argued that not only some ACP countries’ lack the necessary resources to engage in serious negotiations on this issue, but also if investment rules are included in EPAs, administering them requires a great deal of resources that many ACP countries are not able to provide (SOMO 2006). According to this line of arguments, the lack of resources explains why those African countries that actually have established investment-friendly regimes cannot attract FDI. In this regard it is argued that FDI follows growth and countries’ economic fundamentals (Te Velde and Bilal 2005). Thus it is argued that the EU must assist ACP countries with capacity building, promote domestic investment, and permit ACP countries to regulate their investment policies according to their needs (see e.g. SEATINI 2006).

It should also be noted that there is some internal debate between the Commission and member states (Szepesi 2004); and amongst ACP countries (Te Velde and Fahnbulleh 2006) on investment rules. The internal EU debate concerns the mandate of the Commission to negotiate investment rules. As it has been noticed, ‘The investment-related provisions of free trade agreements concluded by the European Union are generally not as comprehensive as those of traditional BIT [Bilateral Investment Treaties]. One reason for this is that EU Member States have so far resisted to hand competency in negotiating some of the most substantial BIT provisions entirely to the European Commission. ... In fact, the EU agreements refer directly to bilateral relations with Member States where certain provisions are concerned’ (Szepesi 2004: 2).

The internal ACP debate concerns whether EPAs should include investment rules in the first place, and if so of what type. As an example, while the SADC region resists any investment rules, the Caribbean region favors such rules.

It should be stated that generally speaking there are three types of Investment Agreements:

- a. Investment liberalization provisions;
- b. Investment protection provisions; and
- c. Dispute settlement provisions (Ortino and Sheppard 2006).

One of the main problems in analyzing the impact of investment rules in EPAs is that it is not clear which type of investment rules the EPAs will include. This issue has also been raised by some commentators who state that ‘A Cotonou Investment Agreement must explicitly identify its objectives:

to increase long-term foreign direct investment into the ACP countries for activities that promote the sustainable development goals of the host country, consistent with the [Cotonou]’ (von Moltke 2003: 1).

## CONCLUSION

Although it is agreed that investment, and especially FDI, will promote ACP countries’ development, there is no agreement on what determines FDI flows and on what form an investment policy should take. On one side EU argues that rule-based investment regimes encourage FDI, and on the other NGOs argue that ACP countries’ growth potentials and economic fundamentals determine investment flows. Faced with this lack of agreement, as well as different evaluations of the trade-offs that may be gained by conceding to the EU in this area, different ACP countries and negotiating regions have adopted different approaches to the question of investment within the EPAs negotiations. However, the overall EPAs negotiations are not so advanced as to permit countries to engage in more substantial discussions on investment – not to mention other WTO+ issues. Furthermore, the limited competence of the Commission also hinders a more comprehensive treatment of investment policy in the negotiations. These factors have led to a de-emphasis on investment rules’ priority in the EPAs negotiations.

## 7. Development Benchmarks and Monitoring and Review Mechanisms

The formulation of ‘development benchmarks’, and monitoring or review of the EPA process against them, was first proposed at the fourth meeting of the Joint ACP-EU Parliamentary Assembly in Cape Town in March 2002. A Declaration agreed at this meeting outlines ‘the main objectives which should inform the conduct and outcome of the negotiations; the principles which should inform the negotiations; the major issues which will need to be addressed within the process of negotiations and the approach which should be adopted (in the) process...’ (ACP-EU 2002). The document goes on to specify 26 benchmarks in relation to objectives<sup>40</sup>, principles<sup>41</sup> and issues to be addressed<sup>42</sup> and seven benchmarks in relation to approach<sup>43</sup>. But the wide range, large number and highly general nature of these benchmarks have contributed to the fact that they have left little mark on the negotiations to date. So too has the vague manner in which the Parliamentary Assembly proposed to follow up on the initiative. The Declaration refers to the Joint Parliamentary Assembly ‘seek(ing) to establish appropriate mechanisms’ in the context of ‘initiatives of the European Parliament to establish a worldwide WTO Parliamentary Assembly’.<sup>44</sup>

<sup>40</sup> Benchmarks listed in relation to objectives include ‘promotion of sustainable forms of development’, ‘contribution to structural transformation’, ‘integration into the global economy’, ‘increased levels of local value-added’ and ‘reduction of gender gaps’.

<sup>41</sup> Benchmarks listed in relation to principles include ‘that no ACP country is left worse off in terms of (market access)’, ‘full respect for the rights of LDCs to non-reciprocal trade preferences’ and special attention to ‘small island and single-commodity-dependent economies’.

<sup>42</sup> Benchmarks listed in relation to ‘issues to be addressed’ include ‘substantive improvement in market access’, investment-friendly Rules of Origin, consultation over and minimisation of costs of compliance in relation to SPS measures, ‘comprehensively addressing supply-side constraints’ – including in gender-sensitive ways, ‘enhanc(ing) human and institutional capacity’, ‘mak(ing) provision for the extension of assistance (for) fiscal adjustment, and ‘taking fully into account the impact of the internal process of reform of the Common Agricultural Policy on ACP countries’.

<sup>43</sup> Benchmarks listed in relation to ‘approaches’ include recognising differences in negotiating capacity, structuring the negotiations so that ‘the collective expertise of the ACP Group (can) be brought to bear on major issues of concern’, ‘bring(ing) all concerned stakeholders into trade policy debates’, and ‘commitment to open and transparent... negotiations’.

<sup>44</sup> The last meeting of the ‘WTO Parliamentary Assembly’ appears to have taken place alongside the WTO Ministerial in Cancún in September 2003.

## EU INTERPRETATIONS OF BENCHMARKING, MONITORING AND REVIEW

Since 2002, while many references to EPA monitoring and review mechanisms can be found in official documents and pronouncements of the EU, few references to development benchmarks can be traced. An exception is a resolution of the European Parliament of March 2005, on the Development Impact of EPAs (P6\_TA(2006)0113, 2005/2/62(INI)), which called for implementation of a new monitoring mechanism 'with the full involvement of parliamentarians and civil society, to ensure political scrutiny and accountability against development objectives or established benchmarks throughout the negotiating process'. This resolution, which was non-binding and not implemented, was succeeded by decisions of the European Council in November 2005 and April 2006, which repeated 'the need to establish and implement an improved monitoring mechanism toward development obligations in the EPA process', but which referred to the timeframe for monitoring commencing only with the 'start of the implementation of the EPA' (Conclusion 8384/06 at [http://www.europa-eu-un.org/articles/en/article\\_5902\\_en.htm](http://www.europa-eu-un.org/articles/en/article_5902_en.htm)). The same decision of April 2006 refers to monitoring during the period of the negotiations as being covered by the Review Process laid down under Article 37.4 of the Cotonou Agreement (see below).<sup>45</sup> The main considerations laid down in this Article do not concern development as such, but rather determination of the overall progress of the negotiations.

In a parallel initiative, dating from the beginning of 2005, a new EPA provision, described both as a 'review mechanism' and a 'monitoring mechanism' and aimed at checking 'at regular intervals whether or not EU development assistance to the ACP was delivering the right results', was proposed by the EU Trade Commissioner Peter Mandelson. Mandelson (2005) explicitly counter-posed this provision to attempts to apply development benchmarks: 'this is not about making the progress of our talks conditional on any specific quantitative and inevitably artificial benchmarks... It is about... getting the most out of our existing development assistance.' It should be noted that, from the EU viewpoint, formulating the purpose of a monitoring mechanism in terms of disbursement of development assistance, takes the idea of such a mechanism outside of the negotiations themselves and into the area of competence of the Regional Preparatory Task Forces (RPTFs) – which the EU see as independent of Regional Negotiating Fora.

In short, therefore, the proposal to introduce ongoing development benchmarking of EPAs has, on the EU side, been displaced by an emphasis on the immediate priority of reviewing or monitoring

<sup>45</sup> This paragraph of the Article reads: 'The parties will regularly review the progress of the preparations and negotiations and will in 2006 carry out a final and comprehensive review...to ensure that no further time is needed for preparations or negotiations'.



negotiation timetables and the disbursement of development assistance. In the latter case, this involves a displacement out of the negotiating arena altogether.

## NGO APPROACHES TO DEVELOPMENT BENCHMARKING AND MONITORING

NGO work on EPA development benchmarks also dates from early 2005, surfacing initially in the publication of a joint paper by ICTSD and APRODEV (2005). This paper proposed a framework, loosely based upon the benchmarks listed by the Joint Parliamentary Assembly in 2002, for monitoring 'the conducted outcome of the negotiations'. The framework consisted in a restatement of the goals of EPAs as formulated by the Assembly and a list of specific issues that it was proposed to monitor in relation to these goals. These are 'market access and fair trade', the ACP 'policy space' and 'resources for development'. Under 'market access and fair trade', the benchmarks listed include solving differences on asymmetrical liberalisation, dealing with preference erosion, improving EU Rules of Origin, providing support for improved capacity in relation to technical barriers to trade and sanitary and phytosanitary standards, and implementing the EU Commodity Action Plan of 2004.<sup>46</sup> Under 'policy space', the main benchmarks relate to 'prioritising regional integration over global integration' and permitting a wide range of government interventions in relation to supply-side constraints. Benchmarks concerning 'resources for development' include the level, sequencing and administration of EU development assistance in respect of adjustment costs and overcoming supply-side constraints. An unelaborated 'mutual accountability' mechanism is proposed as the vehicle for monitoring the negotiations in the EPA regions, a process which it is stated should occur between two and four times a year. It is also acknowledged that the benchmarks identified needed to be provided with more concrete indicators.

The release of the ICTSD-APRODEV document was followed by commissioning of work on more detailed development benchmarks in relation to the different EPA regional configurations, as well as by additional conceptual work by ECDPM and the German DIE. It was also followed by a series of workshops with stakeholders in some of the EPA regions

<sup>46</sup> Under this Plan, the EU pledged actions supporting commodity-dependent developing countries in elaborating strategies covering critical parts of the commodities chain; supporting regional initiatives for commodity development; increasing access to finance and commodity risk insurance schemes; supporting diversification; helping integrate commodities-dependent countries in the international trading system; and enhancing sustainable corporate practices and investments in such countries. The main features of the Plan were increased targeted support to cotton sectors and simplification of access to the EU's main commodity-related finance mechanism, FLEX (see *Bridges Trade Weekly* Vol. 8 (6), 19 February 2004).

Amongst the ICTSD-APRODEV studies on specific regional configurations, that on the Caribbean configuration (Byron and Lewis, 2007) and Bilal et al's (2007) work for ECDPM add new benchmarks (some of them accompanied by indicators) concerning recognition of ACP countries' level of development in market liberalisation schedules, actions to 'strengthen the trade and investment environment of the ACP' in line with ACP countries' own national development strategies, and ensuring the coherence of any concluded agreement with existing programmes of economic reform in the ACP, and participation of civil society organisations in the monitoring process itself. Finally (and somewhat superfluously) it is proposed that 'successful performance in the negotiations' by the ACP is also given the status of a benchmark.

As can be seen, the NGO approach to development benchmarks continues the approach of the Joint Parliamentary Assembly in deriving these benchmarks from a combination of the text of the Cotonou Agreement and the negotiation goals of the ACP countries. In a few cases, additional goals have been proposed. Monitoring their implementation therefore largely corresponds to checking whether the EU, and to a lesser extent the ACP countries themselves, have reached agreement on these points. Since the text of the Cotonou Agreement and the negotiation goals of the ACP are known in advance, the purpose of the benchmarks is essentially to galvanise external moral pressure on the negotiation process.

## ACP GOVERNMENT APPROACHES TO DEVELOPMENT BENCHMARKING AND REVIEW

In the WTO Doha Round, where (groups of) ACP governments used the term 'development benchmarks' it was in the sense described above, i.e., as a list of negotiating objectives.<sup>47</sup> However, since 2005 in relation to the EPA negotiations, some ACP governments have been using the term also to refer to the attainment of economic outcomes relating to the over-arching objectives of the Cotonou Agreement, rather than to specific negotiation goals. This is the sense in which reference to benchmarks appear in the Draft regional EPA Agreement proposed by the ACP members of the ESA EPA configuration in August 2006 (ESA ACP countries, 2005). Furthermore, this Draft seeks to contractualise a relationship between attainment of these benchmarks and implementation of

<sup>47</sup> This was certainly the sense in which it was used by the African Union in elaboration of the so-called 'Arusha Development Benchmarks' for the Hong Kong Ministerial in December 2005, for example.

trade liberalisation.<sup>48</sup> Article 19 of this Draft proposes five-yearly reviews of the Agreement by an 'ESA-EU EPA Council'.

The EU's response to this proposal was twofold. First, it rejected the proposal as incompatible with GATT Article XXIV on Free Trade Agreements, on the grounds that it would make liberalisation of 'substantially all trade' conditional on non-trade considerations. Such a provision, according to the EU, would leave any EPA agreement open to abuse 'particularly by parties aiming to disguise... partial liberalisation under the heading of a FTA' (Caliari 2007). Secondly – and opening for the first time for the incorporation of a Review Clause in a concluded EPA – it stated that, should such clauses be included, they should be 'limited in scope and mainly aimed at accelerating or extending liberalisation' (op. cit.).

Some commentators state that fear that the EU would demand the insertion of such a Clause, should a 'contractualising' Review Clause proposal be made by ACP countries, has limited wider support for the ESA perspective amongst the ACP countries (Bridges Trade Weekly, 10 (40), 29 Nov. 2006).

## CONCLUSIONS

Table II.7.1 summarises proposals made to date concerning EPA development benchmarks and the monitoring of their attainment. There are at least six versions of this proposal. In most cases, the proposals are sketchy on how monitoring is to be carried out and silent on how it is to be followed up on. On the latter point, the ESA ACP group's proposal – aiming to contractualise the relation between attainment of benchmarks and (scheduling of) liberalisation commitments – is an exception, although as argued by the EU it is probably WTO incompatible. Throughout the discussion, interest in the topic from the side of the European Commission has been close to zero. On the other side of the negotiations, interest seems greater amongst NGOs than amongst a majority of ACP countries. This is evidenced in the absence of reference to either Development Benchmarks or to a Monitoring Mechanism in the part of the Mid-Term Review text that has been released for publication.

<sup>48</sup> At a workshop on Development Benchmarks organised by a number of NGOs in Nairobi in April 2007, the Ethiopian Minister of Trade, Ahmed Hashim, proposed that amongst the concrete indicators which should be referred to were diversification of ACP exports, increases in export value added, and an increase in export revenue double the level of increase in GDP (CUTS, ECDPM and FES, 2007).

Table II.7.1: Proposals on Development Benchmarks and Monitoring Mechanisms

Proposed by	EU Parliament and EU-ACP Parliamentary Assembly	EU Council	European Commission, DGs Trade and Development	ICTSD and APRODEV	ECDPM and DIE	ESA ACP countries
Benchmarks derived from	Cotonou Agreement	Cotonou Agreement	EDF Log Frame	Cotonou Agreement	Cotonou Agreement	ACP National Development programmes
Subject of Benchmarks	Outcome of negotiations	'EPA process'	Effectiveness of EDF	Process and outcome of negotiations	Process and outcome of negotiations	Economic trends in ACP countries
Monitoring Authority	Not stated	Not stated	DGs Trade and Development and RPTFs	'Mutual accountability' at Regional and all-ACP level	At Regional level, several options sketched	Regional ACP-EU EPA Councils
Time Frame	Concurrent with negotiations	EPA implementation period	Concurrent with negotiations	Concurrent with negotiations	Concurrent with negotiations and during implementation period	At 5-year intervals during implementation

## 8. The Trade-Aid Relation in the EU-ACP EPA Negotiations

Official declarations on objectives and negotiation guidelines for EPAs demonstrate fundamental agreement over the need to address supply-side constraints and support structural transformation of ACP economies through the transfer of aid from the EU. However, little progress has been made in the negotiations on how to integrate aid with the agreements in practise. This chapter is a review of the literature on the subject. First, it provides the background by giving a brief overview of aid policies and flows in the EU-ACP relationship, discussing the closely-linked Aid for Trade (A4T) initiative, and the perceived development implications faced by ACP countries from the implementation of EPAs. Secondly, it focuses on the central controversies in the negotiations related to aid from the perspective of three stakeholders: The European Commission , the ACP countries, and NGOs.

### DEVELOPMENT ASSISTANCE FROM EU TO ACP COUNTRIES

EU countries gave a total of \$55.7bn (€44.8bn) in Overseas Development Assistance (ODA) in 2005, which amounted to 52.2% of global ODA from Development Assistance Committee (DAC) members. About 51% or €22.4bn of EU ODA went to ACP countries. €7.5bn of the total was distributed by the European Commission . Of this, €2.5bn was channelled through the European Development Fund (EDF).<sup>49</sup>

The EDF finances EC cooperation with the ACP countries and the 20 overseas countries and territories (OCTs), as well as European Investment Bank (EIB) programmes in ACP countries. It is an inter-governmental fund financed by voluntary contributions from EU member states that are separate from the financial contributions made into the EU budget as a whole. The general EU budget also provides some funding to ACP countries – about 6% of total European Commission aid to ACP in 2005 – and member states provide aid to ACP countries through their bilateral programmes.

The European Commission is tasked with the management of the EDF resources on behalf of the EU member states. Traditionally, EDF has consisted of financial allocation cycles of five years. Between 1959 and 2000, each five year EDF allocation ran from the date of signing of the corresponding ACP-EU convention, thus:

<sup>49</sup> Data from OECD (2007a) and EC (2006a).

- First EDF: 1959-1964
- Second EDF: 1964-1970 (Yaoundé I Convention)
- Third EDF: 1970-1975 (Yaoundé II Convention)
- Fourth EDF: 1975-1980 (Lomé I Convention)
- Fifth EDF: 1980-1985 (Lomé II Convention)
- Sixth EDF: 1985-1990 (Lomé III Convention)
- Seventh EDF: 1990-1995 (Lomé IV Convention)
- Eighth EDF: 1995-2000 (Lomé IV Convention and the revised Lomé IV)

With the Cotonou agreement, however, it is no longer the date of signing but the date of ratification by EU member states and two thirds of ACP countries, which constitute the legal entry into force of EDF. Although signed in 2000, the Cotonou agreement was not ratified until 2002. Consequently, the 9<sup>th</sup> (and current) EDF runs from 2002 to the end of 2007.

The number of instruments for disbursement of EDF funds increased steadily during the Lomé years. Under Lomé IV bis (8<sup>th</sup> EDF), funds were made available through ten instruments (up from only two under Lomé I (4<sup>th</sup> EDF)) that could be grouped in three main categories:

- Programmable aid: Resources allocated on a geographical basis to an ACP country or region (through national or regional indicative programmes – NIPs and RIPs);
- Non-programmable aid: Resources allocated not on a geographical basis, but for specific purposes such as emergency aid, STABEX<sup>50</sup> and SYSMIN<sup>51</sup>, or for structural adjustment support;

<sup>50</sup> STABEX was introduced under Lomé I to compensate ACP countries' shortfalls in export earnings due to fluctuations in the world price or domestic supply of agricultural commodities with non-conditional support. From 1975 to 2000, €5.1 billion was granted to ACP countries. Under Lomé IV (7<sup>th</sup> EDF), STABEX disbursement rose to 16% of all EDF aid; in 1989 it constituted 41% of all EDF payments. Initially, STABEX support was to be extended as loans to be reimbursed into a revolving fund. However, sharply falling commodity prices led to the collapse of repayment rates, and in response the European Commission converted existing loans into grants in 1990. At the same time, the European Commission found itself committed to disburse three times more than had been reserved for this purpose, resulting in only 40 and 60% of eligible transfers being covered in 1990-1992 and 1993, respectively. STABEX payments dropped sharply under Lomé IVbis to 6% overall and to only 1.4% in 1999. With the Cotonou Agreement, STABEX was replaced with the more modest and less flexible scheme, FLEX, which constitutes 1% of commitments for the 9<sup>th</sup> EDF. However, some funds previously allocated to STABEX have found their way into the commodity assistance segment of structural adjustment support.

<sup>51</sup> SYSMIN was established with Lomé II to address adverse effects of instability of export earnings in the mining sector for ACP countries. SYSMIN payments never reached STABEX proportions. It peaked under the Lomé IV with 4% of all commitments being made to SYSMIN. This dropped to 1% under Lomé IVbis.

- **Loan finance:** Resources administered by the European Investment Bank (EIB) in support of enterprise development.

According to the European Commission (EC 1997), the efficiency and impact of the EDF were limited by the difficulty of ensuring consistency between different instruments applied in related areas but according to different logics, programming methods and procedures. The European Commission therefore suggested simplifying and reducing the number of instruments to curb ‘the impression (...) of complexity, inflexibility and lack of transparency (ibid: 27)’. The Cotonou Agreement then replaced these instruments with two broad instruments: a ‘financial envelope’ for long-term development cooperation activities providing the grant element of NIPs and RIPs and an investment facility of loan/equity capital managed by the European Investment Bank (EIB). The distinction between ‘programmable aid’ and ‘non-programmable aid’ was abandoned. Instruments for specific purposes like STABEX and SYSMIN disappeared while support for specific purposes remained, but as part of the ‘financial envelope’ for long-term development and under much more stringent eligibility criteria.

The Cotonou Agreement (9<sup>th</sup> EDF) also meant a shift to so-called ‘rolling programming’: a system of flexible and regular review mechanisms. As such, the 9<sup>th</sup> EDF represents the final abandonment of ‘entitlement’ aid (i.e. fixed allocations regardless of performance) of the Lomé Conventions and a shift to allocation according to ‘needs’ and ‘performances’. In other words, the Cotonou Agreement confirmed the trend towards increased conditionality, in relation to the quality of aid utilisation as well as policy performance, and expanding the discretionary powers of the European Commission, which had been emerging over the course of successive Lomé Conventions (Silva and Grynberg 2006). In practice, it meant that more money could be channelled to ‘good performers’ and the share allocated to ‘bad performers’ reduced.

It is difficult to provide a comprehensive picture of EDF disbursements trends by sector, as definitions have changed numerous times over the years. However, major shifts in sector deployment of EDF aid in ACP countries are traceable. Under the earlier Lomé Conventions, agriculture and rural development was the major focal sector accounting for the largest proportion of aid. The second most important sector for EDF aid was transportation infrastructure. Since Lomé III, however, the sector focus of EDF aid has shifted. While transportation infrastructure remains an important sector for EDF aid, support to agriculture and rural development have decreased dramatically, with first commodity assistance support and subsequently budgetary support coming to play a leading role (Goodison 2006). Consequently, under the 9<sup>th</sup> EDF, only 7% of total NIP spending was committed to rural development and 1% to agricultural development, while almost 31% was committed to structural adjustment support (commodity assistance programmes and budgetary support) (see below).

Over time, the focus of EDF aid has been broadened and progressively extended to meet a growing range of development policy priorities. This has had two implications. First, EDF funds have been spread more and more thinly. This has become more pronounced with the financing of a growing number of 'vertical' programmes outside the traditional NIP/RIP framework, such as debt relief (HIPC), the Global Fund for HIV/AIDS, Malaria and TB, the African Security Facility, the Water Facility, and the Energy Facility. Furthermore, the expansion of activities has occurred against the backdrop of a decline in the real value of EDF allocations since 1990. Secondly, the dislocation between the European Commission's development policy priorities at any given moment and actual EDF programmes being implemented has increased with the expansion of mandates for EDF aid.

Throughout its existence, the EDF has been plagued by a considerable time lag between the nominal allocation of funds and their disbursement (see table II.8.1). There seems to be two overall reasons for this:

- **Increased policy dialogue:** intensification of policy dialogue prior to aid commitments and in negotiating conditionalities of disbursed aid creates bottlenecks. For instance, the introduction of policy conditionalities to the quickest disbursement instrument, the now defunct STABEX, resulted in a dramatic slowing down of the aid disbursement procedures, with STABEX funds allocated in the 1990s still lying unutilised today.
- **Cumbersome administrative procedures:** the European Commission's record on aid delivery was recently referred to as 'positively embarrassing' by a major newspaper (FT, March 27, 2007). Maxwell (2006) comments that 'the European Commission has been regarded by most member states as delivering aid which is below the quality of their own programmes and often at higher cost'. Oxfam (2004) ranked six major donors and found that the European Commission scored far worse than the other donors in terms of delivering aid on time. More than 20% of the Commission's aid was said to arrive more than a year late, compared to only 3% for the other donors (US, UK, Germany, Japan and the World Bank). The European Commission also scored second-worst for 'committing to the long term' and 'fitting in with the government budget cycle'. Save the Children (2006) concludes that, despite recent tangible progress, the European Commission consistently showed the biggest gap (of six donors investigated) between pledges and disbursements between 2002 and 2004. The report also cites the European Commission's own figures showing that 40% of delays are due to its own administrative processes, compared to 25% caused by administrative problems in the recipient countries. Additionally, aid from the European Commission is notoriously vulnerable to fraud. A 2006 report from the EU's anti-fraud watchdog OLAF shows that 21% of fraud investigations in 2005 related to the European Commission aid programmes, although aid only accounts for about 7% of the budget (OLAF 2006).



The European Commission argues that its performance has improved since a reform program began in 2000, and OECD (2007b) supports this. However, the same OECD report cautions against complacency: the European Commission's development partners 'frequently commented on the continuing need to devolve authority to the field and further simplify procedures and accelerate programme implementation' while 'the internal reform process was frequently presented [by the European Commission] as completed'.

EDF	Initial Allocation		Commitments		Payments	
	Million (€)	Real Values*	Million (€)	%**	Million (€)	%**
4 <sup>th</sup> EDF (Lomé I)	3 390	2 696	3 053	90.1	3 053	90.1
5 <sup>th</sup> EDF (Lomé II)	5 227	2 586	4 207	80.5	4 207	80.5
6 <sup>th</sup> EDF (Lomé III)	8 400	3 264	8 589	102.3	7 334	87.3
7 <sup>th</sup> EDF (Lomé IV)	12 000	3 514	11 735	97.8	10 084	84.0
8 <sup>th</sup> EDF (Lomé IV bis)	14 625	3 464	13 224	90.4	8 385	57.3
9 <sup>th</sup> EDF (Cotonou)	15 200	3 131	9 215	60.6	2 599	17.1

\* Base year: 1975  
\*\* % refers to Initial Allocation  
Source: Goodison (2006), EC (2007a)

In nominal terms, EDF allocations have grown consistently from €3.4 billion to €15.2 billion or 348% from the 4<sup>th</sup> (Lomé I) to the 9<sup>th</sup> EDF (Cotonou). However, the real increase (adjusted for inflation) over the same period show an overall 16% rise but an 11.4% decline from the 7<sup>th</sup> to 9<sup>th</sup> EDF (see table II.8.1). The nominal amount of aid actually spent under each EDF has increased more or less steadily. However, the funds actually spent relative to funds allocated during each EDF financial cycle have fallen significantly (see table II.8.2). Whereas the real EDF allocations increased from the 4<sup>th</sup> to the 9<sup>th</sup> EDF, ACP per capita allocations dropped sharply from about €8.5 to about €4 during the same period.

	Total funds allocated	Total disbursements within financing cycle to which the funds were allocated	Percentage of total allocation disbursed in the financing cycle to which it was allocated (%)
4 <sup>th</sup> EDF (1975-79)	3 390	1 455	43
5 <sup>th</sup> EDF (1980-84)	5 227	2 041	39
6 <sup>th</sup> EDF (1985-89)	8 400	3 342	40
7 <sup>th</sup> EDF (1990-94)	12 000	4 418	37
8 <sup>th</sup> EDF (1995-1999)	14 625	2 922	20
9 <sup>th</sup> EDF (2000-2006)	15 200	4 239	28

Source: Silva and Grynberg (2006)

The €15.2bn available for 9<sup>th</sup> EDF is divided into funds for the ‘financial envelope’ for long-term development (€11.3bn), the investment facility (€2.2bn) and resources from EIB’s own funds (€1.7bn). Of the funds for long-term development, €10bn is allocated to national indicative programmes, while the remaining €1.3bn is allocated to regional co-operation and development (including pan-ACP programmes). Table II.8.3.6 shows the allocation of funds of the 9<sup>th</sup> EDF NIPs. In addition to the aforementioned focus on structural adjustment and transport, the data shows that only limited resources are allocated to business, trade and private sector development. Indeed only 0.7% of NIP funding was reserved for this purpose. A partial reason for this is that the European Commission has tended to favour to fund such programmes through regional instruments.

Sector	Percentage of Total Funds Allocated*
Structural Adjustment	30.7%
Transport	21.4%
Governance	7.9%
Rural Development	7.0%
Water	6.7%
Education	6.3%
Minerals	5.0%
Health	4.3%
Civil Society	2.9%
Social Provisions	1.3%
Agriculture	1.1%
Food Aid	1.0%
Business	0.6%
Environment	0.5%
Trade	0.1%
Undifferentiated	3.1%

\*Allocations made to specific programmes totaling €6.24bn

Source: Silva and Grynberg (2006)

In December 2005, the EU agreed to commit €22.68bn for the 10<sup>th</sup> EDF. Of this, €21.97bn is allocated to the ACP countries, €286m to the OCT and €430m to the European Commission as support expenditure for programming and implementation of the EDF. The amount for the ACP countries is divided to €17.77bn to the national and regional indicative programmes, €2.7bn to intra-ACP and intra-regional cooperation and €1.5bn to Investment Facilities.

An increased share of the budget is devoted to regional programmes, thereby emphasising the importance of regional economic integration as the basic framework for national and local development. An innovation in the 10<sup>th</sup> EDF is the creation of 'incentive amounts'. Countries can earn these extra resources by improving governance, for which an agenda will be agreed between the EC and individual ACP countries.

The 10<sup>th</sup> EDF is planned to run from 2008 to 2013. Yet, as of June 2007, only four EU countries and eight ACP countries have ratified the internal agreement on the 10<sup>th</sup> EDF. For the 10<sup>th</sup> EDF to start on 1 January 2008, the ratification process should be completed by November 2007. The European Commission refers to the situation as 'clearly worrying' (EC 2007a: 3) and Goodison (2007) argues that the 10<sup>th</sup> is unlikely to be ratified on time, suggesting a scenario in which the 10<sup>th</sup> EDF will run from 2010 to 2015. Ratified on time or not, the negotiation and implementation process coincides with that of the EPAs (projected to start in 2008). The European Commission has stated that it will take into account the needs of ACP countries arising from EPAs in the programming of the 10<sup>th</sup> EDF. The two processes are, thus, strongly linked, although formally independent from each other.

## FROM TRADE-RELATED AID TO AID FOR TRADE

After the Uruguay Round, developing countries in general and African countries in particular requested help to strengthen their capacity to formulate trade policy, participate in trade negotiations, and implement trade agreements. In response, WTO, UNCTAD and ITC established the Joint Integrated Technical Assistance Programme (JITAP) aimed at addressing such issues. Likewise, at the first WTO Ministerial Conference in 1996, the special challenges LDCs faced from trade liberalisation were recognised, and an initiative for strengthening LDCs trade capacities, the Integrated Framework for Trade-related Technical Assistance to LDCs (IF), was established the following year. It was supported by six multilateral institutions (IMF, ITC, UNCTAD, UNDP, the World Bank and WTO). The two initiatives constitute the start of a process that has culminated with what is now known as A4T. Their approach to the relationship between aid and trade is, however, much narrower than the approach envisioned with A4T. The following focuses on the development of the European Commission's approach to the trade-aid relationship from TRA to A4T.

## TRADE-RELATED ASSISTANCE (TRA)

In response to the challenges of the WTO Doha Development Agenda and EPA negotiations with ACP countries, the European Commission developed a strategy for Trade-related assistance (TRA) in 2002 (EC 2002, 2003). Originally, it was defined as a 'very broad' concept, which 'could incorporate most development activities' and four categories of TRA were identified (see Appendix 3).

However, the European Commission's definition of TRA has become narrower over time. In a 2007 document, the European Commission writes: 'since the early 2000s, support to trade has been understood as comprising two areas of action: trade policy and regulation and trade development' (EC 2007b: 2). The resulting narrow definition of TRA now corresponds to the definitions used by OECD, WTO and the above-mentioned multilateral initiatives. In this form, TRA is primarily aimed at supporting recipient countries' capacity to implement trade liberalisation.

### Aid for Trade

The narrowing of the European Commission TRA definition has occurred simultaneously with the emergence of a debate on Aid for Trade (A4T). This debate originally took place under the auspices of the World Trade Organisation (WTO) as a part of the Doha Round negotiations and culminated at the Hong Kong Ministerial conference in December 2005 with a decision to mandate a Task Force to provide recommendations on how to operationalise A4T.

The Task Force (WTO 2006) defined what could be funded under A4T as 'activities ... identified as trade-related development priorities in the recipient country's national development strategies'. Building on the OECD/WTO database on past TRA, it provided a list of what it considered would qualify. The database covers the two categories which make up TRA, but the Task Force added another three. So the Task Force's suggestion for an A4T definition comprises five categories:

1. Trade policy and regulation
2. Trade development
3. Trade-related infrastructure
4. Creation of productive capacity
5. Trade-related adjustment

These categories are not unlike the categories which constituted the European Commission's first definition of TRA. Indeed, it has been argued that much of the current thinking on A4T originates from the European Commission's original contribution to the debate on TRA (ODI 2007a). Yet, the European Commission refers to the additional categories as 'new' and A4T as a 'broader dimension', beyond TRA (EC 2007b).

There is not yet a generally agreed upon definition of what the broader dimension entails. While there seems to be an emerging consensus that A4T at least includes the first three categories suggested by the WTO Task force, there is less agreement on whether support to supply-side constraints should remain confined to addressing trading costs or should be expanded to cover creation of productive and competitive capacity. There is even less agreement on the inclusion of adjustment costs in the framework. OECD (2006) argues that some of the activities related to adjustment costs, such as export diversification and fiscal reform, are included in the first three categories, whereas other adjustment-related activities, such as social safety nets, balance-of-payments support, compensation for preference erosion, and loss of tariff revenue, are not.

Stiglitz and Charlton (2006) identify four (non-exclusive) rationales for A4T. First, a political motivation to use aid to 'buy' progress in trade negotiations. Second, A4T can be seen as a tool for compensating preference-dependent countries, net-food importers, and others adversely affected by the implementation of trade agreements. Third, if used as a mechanism of redistribution adjusting for unbalanced outcomes from trade, aid can ensure fairness in trade agreements. Fourth, by targeting aid on supply-side constraints in developing countries, it can enable them to take advantage of the market access offers in trade agreements.

All four rationales rest on the perception that trade liberalisation (accompanied by trade measures) alone is not enough to ensure the 'development dimension' of trade agreements; aid is needed. As such, A4T is a move away from the optimistic view of trade liberalisation dominating among policy makers in the Uruguay Round and the early Doha Round of the WTO negotiations: that trade liberalisation would provide significant benefits for all developing countries and have no negative effects. As the Doha Round proceeded, it became increasingly clear that this view was overly-optimistic. In July 2002, (WTO 2002: 1-2), the LDCs suggested that:

'supply side constraints in developing countries and their need to retain the flexibility of being able to adopt pro-development policies and options should be addressed. This can be done in several ways, including: (i) exemptions from obligations for developing, particularly least-developed countries, if those obligations would constrain or prevent developing countries from adopting policies or measures required for their economic and social development, and (ii) obligations on the part of developed countries to assist developing countries to build their supply-side capacity to foster national production capacity as well as export supply capacity.'

This was followed by a growing acceptance by international organizations and donors that trade liberalisation would not benefit all countries, and that the effects might be negative for some (ODI 2007a). In 2005, a group of experts examined what developing countries could gain from the Doha

Round, and concluded that A4T was an essential part of a package to rescue the Round and ensure that developing countries gained (Zedillo 2005). This was followed by the WTO Task Force report a year or so later. The European Commission is currently in the process of developing an EU A4T strategy due in the autumn 2007. The process was initiated by a formal decision on 16 October 2006 by the General Affairs and External Relations Council (GAERC), endorsing the recommendations of the WTO A4T Task Force. At the meeting, the Council explicitly recognised that increased and more effective A4T is needed to support ACP countries to use trade as a tool for development and take full advantage of EPAs (GAERC 2006). The negotiations on EPA-related aid are therefore closely intertwined with the debate on A4T.

## THE DEVELOPMENT DIMENSION OF EPAS

In the EPA negotiations, the notion that trade liberalisation cannot stand alone has been explicit throughout the process. All parties envisage EPAs as Free Trade Agreements (FTAs) but at the same time stress the necessity for EPAs to be more than standard Free Trade Agreements. They should have a 'development dimension' in order to meet the development challenges and fulfil the official objectives. The most important development implications are:

- **Loss of import revenues:** fiscal reforms are needed to offset the loss of import revenue from tariff reductions. Such income constitutes a considerable part of many ACP countries' total income. Tax collection/administration systems need to be strengthened.
- **Supply-side constraints:** removal of protective trade barriers will expose domestic industries to global competition and could cause the loss of jobs. Adjustment measures for loss of competitiveness, restructuring of domestic industries, and creation of productive capacity need to be addressed. Other aspects of supply-side constraints include trade-related infrastructure, which should be strengthened.
- **Institutional weaknesses:** to address issues such as compliance with food and safety standards and harmonisation of custom procedures, institutional reform and development is needed.

Although officially agreeing on the general principles and on the development challenges of EPAs, the negotiating approaches on the practical integration of the development dimension of the agreements by the two parties have diverged significantly. ICTSD and APRODEV (2005) argue that the European Commission's negotiating position until 2004 in practice contradicted the official objectives and guidelines. In January 2005, Trade Commissioner Peter Mandelson implicitly acknowledged this:

'[EPAs] should become what they really are: trade and development tools. They are not classical hard-nosed, free trade agreements ... Therefore, the EPA process will be

broader than pure trade arrangements and cover issues linked to development policy and support ... I intend this to be a new start for the EPAs – to give the negotiations a new impetus – and to ensure that from now on, until the final implementation of what we will negotiate by 2008, development concerns have pride of place.<sup>52</sup>

The 'turn-around' followed harsh criticism of the European Commission's negotiation strategy levelled by ACP countries, member states (the UK in particular, see UK Government 2005) and NGOs (e.g. ERO 2005; Christian Aid 2004) and culminated with the aforementioned GAERC decision prompting the EC to develop an A4T strategy with particular focus on ACP countries. However, ACP officials have frequently noted that while flexibility sometimes emerges in ministerial level encounters with Commissioner Mandelson, this often does not materialise at the technical level from European Commission officials.

Overall, fundamental disagreements between the parties on substantive practical issues remain, which is reflected in declaration-type agreements on generalities. The chapter continues by discussing these disagreements and the broader controversies they have spawned.

## CONTROVERSIES

The controversies in the negotiations are related to the level and scope of support made available by the EU for ACP countries, the mechanisms for delivery and the process to link aid with the EPA negotiations and implementation. In the following sections, the three areas of controversy will be discussed from the perspective of three actors: the European Commission, the ACP countries, and NGOs and academic observers.<sup>53</sup>

Generally, the European Commission has adopted a defensive agenda on the aid aspect, maintaining that it is not mandated to discuss aid in the EPA negotiations. The European Commission position is complicated by two aspects that have led to difficulties in defining and identifying a coherent European Commission strategy on the trade-aid relation. First, the EPA negotiations are conducted by DG Trade, whereas aid issues are the responsibility of DG Development. Second, disagreement between EU member countries on EPAs is evident. A number of countries are pursuing offensive trade interests vis-à-vis ACP countries, while others maintain that they have no such interests. Also, some new member countries are concerned with the prospect of ACP countries gaining advantages

<sup>52</sup> 'Economic Partnership Agreements: putting a rigorous priority on Development', Speech by Peter Mandelson to the Civil Society Dialogue Group, Brussels, 20 January 2005.

<sup>53</sup> Where nothing else is noted, the sections draw on various issues of Trade Negotiations Insights published jointly by ECDPM and ICTSD.

to their disadvantage, both in relation to increased market access and aid. NGOs and academic observers have an offensive agenda on the aid aspect of the EPA negotiations, typically calling for additional and 'better' EPA-specific aid. The ACP countries are a heterogeneous group of countries with respect to geography and their development stage and needs. They have, however, been largely in agreement on the aid aspect of the EPA negotiations and are generally closer to the NGO line in the negotiations than to the European Commission's.

## LEVEL AND SCOPE OF SUPPORT

### The European Commission perspective

Overall, the European Commission maintains that the €22.6bn pledged to the 10<sup>th</sup> EDF will significantly cover all EPA-related aid from the European Commission, without jeopardising support to other issues. Also, the European Commission urges ACP countries and others to consider the benefits from EPAs when discussing aid needs. More specifically, the European Commission approach to the level and scope of support is two-fold. First, it focuses on the volumes of TRA which will become available, strongly emphasising a €2bn pledge made in 2005. Second, it focuses on the European Commission contribution to the emerging A4T framework.

From 2001-2005, the European Commission provided TRA amounting to a total of €4.3bn. This equals €867 million a year on average. Of this ACP countries received €1.6bn or €323.8 million a year on average (see table II.8.4). TRA provided under trade policy and regulation heading amounted to €1.5bn from 2001-2005 (34% of total and €297 million a year on average). The most important programmes in this category were trade facilitation and regional trade agreements. The most important trade facilitation programmes are in the Mediterranean and Western Balkans regions, whereas support for regional trade agreements is the dominating TRA intervention in the ACP group. The trade development category accounted for €2.6bn in the same period (66% of total and €570 million a year on average). Trade promotion and market development programmes within this category are particularly important in ACP countries (EC 2006a).

	2001	2002	2003	2004	2005	Total
	Million €	Million €	Million €	Million €	Million €	Million €
ACP	557.5	166.5	318.6	283.4	293.9	1 619.9
Others	268.3	521.8	566.6	665.4	694.1	2716.2
Total	825.5	688.3	885.2	948.8	988	4 336.1

Source (EC 2006a)



In July 2005 at the G8 meeting in Gleneagles, the EC promised, in the words of the President for the Commission, José Manuel Barroso, 'a significant boost for aid for trade, aimed at helping developing countries help themselves' by pledging €1bn in TRA a year by 2010, of which a 'significant' part would be reserved for the ACP countries. The pledge by the European Commission was followed by pledges from the member states to likewise provide €1bn a year collectively by 2010 made at the WTO Hong Kong Ministerial in December 2005. As shown above, the European Commission came close to fulfilling the pledge in 2005 by providing TRA of €988m. As the European Commission itself acknowledges (EC 2007a:4), the bulk of additional TRA funds will have to come from the member countries, which gave around €300m a year on average between 2001-2005.

The €1bn TRA from the European Commission is to be allocated through the 10<sup>th</sup> EDF. It seems most likely that the EU will opt for a decentralised process, where the European Commission delegations and the National/Regional Authorising Officers in ACP countries (and subregional organisations) decide on what they want to use TRA funds for. Countries and regions that agree to EPAs and/or regional integration are likely to receive (increased) development support from the European Commission, as the bulk of TRA is used for this purpose in ACP countries.

Although fully supporting the A4T agenda identified by the WTO task force, the European Commission has made no substantive pledge of support to the new A4T categories, i.e. trade-related infrastructure, productive capacities and trade-related adjustment. The European Commission is, however, already providing support to such areas. For instance, support for trade-related infrastructure averaged €1.29bn a year from 2001-2004. In the same period, member countries' support averaged €1.48bn a year for the same purpose (EC 2007b). Likewise, the European Commission provides support to sugar and banana producing ACP countries to meet adjustment costs related to changes in preferential trade arrangements with the EU. For sugar, this is planned to average €190m a year from 2007 to 2013; for bananas the European Commission provided €252m from 1999 to the end of 2005. Thus A4T is not new to the European Commission in terms of scope for support; it is the underlying perception that trade liberalisation will not provide significant benefits for all developing countries and may have negative effects for some, which the European Commission is finding difficult to reconcile with its negotiating position.

## THE ACP PERSPECTIVE

ACP governments have persistently requested additional non-EDF aid targeted specifically at EPA-related needs. In particular, their requests have focussed on adjustment costs and loss of tariff revenues. They argue that since the implementation of EPAs is only one among many priorities of the 10<sup>th</sup> EDF, the current level of promised funds will not suffice. For ACP countries with LDC

status, the prospect of additional aid related to the signing of EPAs is one of ‘the carrots’ keeping them in the negotiations and away from opting for Everything But Arms access.

Another factor keeping the ACP countries at the table, is their high dependence on aid to make ‘ends meet’ in their annual budgets. As the deadline approaches and the European Commission remain steadfast that there will be no funding over and above what is already offered, the ‘development carrot’ will crumble.

ACP countries have repeatedly expressed their disappointment over the narrow approach that the European Commission has adopted on the development dimension in maintaining that asymmetric trade and investment rules are the key means to development. Borrmann and Busse (2007) argue that few ACP countries are in a position to benefit from trade liberalisation, as this requires a strong institutional setting. This the ACP countries, particularly the African ones, generally lack. In this, the authors reflect the position of the ACP countries, which emphasise the aid aspect of the EPA negotiations over trade aspects.

#### The NGO perspective

Overall, the NGO perspective is well represented by a joint statement from more than 30 NGOs, calling for EU and ACP leaders ‘to reject a 10<sup>th</sup> EDF that reduces the required allocations’ by, inter alia, ‘incorporating funding for adjustment related to the Economic Partnership Agreements (EPAs), despite promises that additional funding for ‘Aid for Trade’ would be made available for this purpose’ (Concord Cotonou Working Group 2006). The arguments underpinning the statement are discussed below.

Oxfam (2006) calls the EU pledges of additional EPA-related aid ‘a mirage’. It argues that the 10<sup>th</sup> EDF represents no additional EPA-related funds. The European Commission will, thus, cover EPA-related adjustments costs from its existing aid portfolio only diverting money away from other headings such as health, education, and rural development. The claim is based on the conclusions of Clarke and Grynberg (2006) regarding allocations for the 10<sup>th</sup> EDF. They argue that EPA-related adjustment needs will be significant and additional to the current needs of ACP countries, and that the €22.6bn only represent some €1.4bn in additional funds (relative to a ‘business-as-usual’ scenario), which is far from the €9.2bn they estimate that ACP countries will need to cover EPA-related adjustment costs.

ERO (2007a) argues that since the 9<sup>th</sup> EDF runs from 2002-2008 and the 10<sup>th</sup> EDF officially will run from 2008-2013, but is more likely to run from 2010-2015, using the old basis for determining the start date, means de facto that one EDF has been ‘lost’. In other words, the period from 2000-2015 will be covered by only two EDFs rather than the usual three. This has real implications for the

annual level of funding made available to EDF activities: the annual nominal aid allocation will fall by some 37% from 2000 to 2015 (from €3.7bn to €2.4bn).

It is a common misunderstanding among NGOs and other observers that the EU €2bn pledge is made to A4T and not TRA (this is somewhat understandable, since the European Commission itself frequently makes the same mistake). The difference is not merely semantic. It means that support for the most important development implications as identified above are not covered by EU pledges, as they are beyond the TRA framework. On the one hand, this leaves all EPA-related support outside the TRA framework to the discretion of the European Commission and the individual EU member countries. On the other hand, it assures that the EC and member countries cannot opt for the temptation to simply reclassify some of their ongoing programmes, which could be defined as A4T, but not TRA, to meet their pledges.

The misunderstanding leads some NGOs and observers to conclude that the €2bn pledge represents reallocated money (e.g. Napoletano et al 2007, Kinnock 2006, South Centre 2007a), thereby missing the point: the European Commission is not trying to meet a pledge by reallocating funds, it made a pledge it already fulfilled. Furthermore, the pledge was made to support aid programs essentially aimed at facilitating smooth implementation of trade liberalisation and not, for instance, at mitigating adjustment costs or creating productive capacity.

Another central point widely emphasised by NGOs is related to additionality. Of the €2bn, only about €700m is additional, namely the funds that EU member states have pledged. Consequently, additionality is at the discretion of member states. Where and how this money will be spent is, thus, not for the European Commission to decide.

## MECHANISMS FOR DELIVERY

### The European Commission perspective

The European Commission insists that the proper mechanism for EPA-related support is the 10<sup>th</sup> EDF and that not only have sufficient funds been made available, but the effective delivery of such funds has also been assured through a successful reform of the EDF disbursements procedures and methods. Yet, the GEARC conclusions on 16 October 2006 state that ‘the preferred delivery mechanisms for this support [A4T] will be nationally and regionally owned financing mechanisms’ (GAERC 2006:6). While this seems to indicate that the delivery mechanisms will be the NIPs and RIPs already used for EDF disbursements and/or existing regional funds such as the COMESA fund for the ESA region, the word ‘preferred’ may signal a willingness to consider alternatives. However, given the European Commission’s current focus on the 10<sup>th</sup> EDF, alternative mechanisms will most likely have to rely on bilateral funds from EU member states, i.e. a ‘substantial’ part of

about €700m a year and/or other donors. The growing European Commission discretionary power through increased aid conditionalities may be an important underlying rationale for its continued focus on the EDF and rejection of alternatives.

### The ACP perspective

As an alternative to the 10<sup>th</sup> EDF for EPA-related aid, the ACP countries are calling for a so-called Financing Facility, as envisaged in Declaration XV of the revised Cotonou Agreement. The Financing Facility should, at the national and regional level, address EPA-related adjustment costs and supply-side constraints of ACP countries. Funding should come from the 10<sup>th</sup> EDF, the EU member states and other donors and should be primarily additional to already pledged funds. The rationale for establishing a Financing Facility for EPAs is related to the need for effective and predictable aid. EPA-related aid will be time-sensitive by nature, since it aims at mitigating adjustment costs and building capacity to compensate for lost revenue and gain from increased market access. Thus, it must be disbursed in a quick, effective, and timely manner. As discussed above, the European Commission has a doubtful history as an aid donor. Combined with the fact that the EDF has had little previous experience with support to business, trade and the private sector, which are to represent a vital part of EPA-related aid, the appropriateness of the 10<sup>th</sup> EDF as the main mechanism for EPA-related support is questioned. Also, EPAs will be implemented over more than a decade, but the 10<sup>th</sup> EDF is planned to run for a five-year period only and funds for a presumed 11<sup>th</sup> EDF is a distant prospect, given that actual availability and programmed use of funds from the 10<sup>th</sup> EDF is not certain at this stage. Thus, the predictability of EDF funds is limited.

Although an integrated part of the ACP position in the negotiations, the Financing Facility seems to be ruled out by the European Commission. The alternative hinted at by the European Commission does not constitute a Financing Facility as envisioned by ACP countries, as long as the European Commission maintains that its EPA-related support will be channelled through EDF support mechanisms.

### The NGO perspective

As shown above, NGOs are generally very critical of the European Commission's ability to deliver affective aid through the EDF. The NGO literature is, however, silent on alternatives.

## THE LINKING PROCESS

### The European Commission perspective

The European Commission has refused to formally link the issue of aid to the EPA negotiations, arguing that:

- The EPA negotiations as foreseen in the Cotonou Agreement are about trade and trade-related issues, not aid.
- Aid is already covered by the Cotonou Agreement through the EDF.
- The European Commission is not mandated by the EU member countries to include aid as part of the EPA negotiations.
- The European Commission does not want to be perceived as buying the ACP countries into EPAs with aid.

In a leaked letter<sup>54</sup> from the head of DG Development and the Deputy Head of DG Trade to the Fijian trade minister, the European Commission writes: 'In your draft EPA submission, detailed development co-operation details form an integral part of the text...as you know, this is not acceptable to us.' In the same letter, the European Commission officials call for aid and EPAs to be 'mutually reinforcing' but kept separate. In other words, the European Commission seems adamant that the real crux of development cooperation is and remains within the Cotonou Agreement, and not within the EPA negotiations. Essentially, the European Commission's approach to the trade-aid relationship is limited to the programming process of the 10<sup>th</sup> EDF, which, as mentioned above, will take into account the needs of ACP countries arising from EPAs. Thus, aid is officially distinct from trade issues, and although Regional Preparatory Task Forces comprising officials and experts from both the ACP countries and the EU have been set up to interlink the two processes, how the 10<sup>th</sup> EDF will address the needs arising from EPAs is not a part of the formal negotiations.

To the European Commission, aid and trade liberalisation policies go hand-in-hand; the one will not work without the other. The policy context should be right with trade liberalisation being implemented or at least planned and 'locked in' before restructuring programmes are designed and implemented, since only if the right policy context exists will aid be effective. Thus, to the European Commission the sequencing of aid and trade liberalisation should be simultaneous.

### The ACP perspective

The ACP countries have requested binding commitments in the legal texts of EPAs for EPA-related aid to ensure predictability of the available resources. Independent of the debate on additionality, the ACP countries request legal certainty that aid will be available, when needed to ensure that legally binding EPA-related trade reforms will be matched by equally binding aid commitments. Some EPA groupings, like the Eastern and Southern Africa (ESA) EPA group, have prepared a development matrix identifying development objectives which they would like to include in their EPA to bind the European Commission to their implementation. Likewise, a review clause to allow ACP countries to

<sup>54</sup> Seen by the Financial Times and cited on 28 November 2006.

halt or backtrack trade liberalisation, if EU promises on aid are not met after a 10-year period, has been proposed. Several ACP countries have stressed the need to insert a rendezvous clause in the EPAs to ensure that EPA-related aid continues after the 2020 expiry of the Cotonou Agreement. They stress that the EPAs should be trade and development agreements, in which the ACP give binding commitments on market access and, possibly, trade-related rules in exchange for binding commitments from the EU for development support.

The European Commission is not against well-defined review clauses *per se* and recognises the significance of discussing aid commitments. However, it argues that review clauses 'should be limited in their scope and mainly aimed at accelerating or extending liberalisation' and trade reforms should not be linked to 'undefined development targets'.<sup>55</sup> Also, the European Commission argues that such a clause would constitute micro-management of trade, and thus violate WTO-rules. Further, as mentioned, the European Commission does not want to be perceived as buying ACP countries into EPAs with aid. Curiously, on 2 August 2007, the Pacific ACP countries in a joint letter to the European Commission expressed their 'disappointment and annoyance' with the European Commission's attempt to link the signing of an EPA to the programming of the 10<sup>th</sup> EDF and threatened to stop the negotiations. They claim to have been told by the European Commission that of the €76m aid planned for the Pacific ACP countries in the 10<sup>th</sup> EDF, 48% would be 'reprogrammed', if an EPA was not signed. European Commission officials argue that the aid would be diverted from programmes to support regional integration to other programmes within the region and maintain that 'at no time have the EU used development aid as a bargaining chip'.<sup>56</sup> However, ACP countries are generally wary of EDF 'reprogramming', since the use of 'unprogrammed' funds is not guaranteed.

Another important aspect to ACP countries is the sequencing of aid and trade reforms. Essentially, the ACP countries argue that aid should be made available and programmes implemented before trade reforms are introduced, so that ACP countries are prepared to meet the development implications from EPAs and take advantage of market access to the EU. In other words, aid should be disbursed and development objectives achieved, before ACP countries are to implement trade reforms. To assure a proper sequencing between meeting development objectives and trade reforms, ACP countries request a monitoring system as an integral part of EPAs.

### The NGO perspective

As mentioned, the Cotonou Agreement marked the end of 'entitlement aid' and a move toward more aid conditionality. This has spurred intense criticism from NGOs arguing that European

<sup>55</sup> Financial Times, 28 November 2006

<sup>56</sup> Financial Times, 2 August 2007

Commission aid is being increasingly bound to foreign policy objectives. Much of the criticism has been targeted at an European Commission Communication on governance (EC 2006b). According to NGO criticism, the communication aims at strengthening the conditionality of the commission's aid programmes by making disbursements partly dependent on government improvements in the receiving country. In addition to widely agreed criteria on political rights, rule of law, corruption, and government effectiveness, the communication added cooperation in the fight against terrorism and illegal immigration and regional economic integration (Open Europe 2007). According to NGOs and recipient countries, this resembles 'old-style aid with strings attached'. In a joint statement, ten EU-based NGOs accuse the European Commission of having 'imposed its own definition of governance, the tools to monitor it [the governance profile and indicators] and the financing mechanisms [a €3bn incentive tranche]' thereby aligning aid policy with other policies, such as trade (Concord 2006).

Goodison (2007) argues that the discretionary powers the European Commission has over aid allocations, provides it with considerable leverage in the EPA negotiations. He foresees that with 'the engineered convergence of the process of programming of the 10<sup>th</sup> EDF with the final stages of the EPA negotiations process...the programming of the 10<sup>th</sup> EDF could well come to constitute the single largest 'institutional bribe' in history, with ACP finance ministers being 'encouraged' to 'put the arm' on reluctant trade ministers who remain unconvinced of the economic value of the type of EPAs which the European Commission is proposing (p. 147-8).' In other words, the European Commission will wait the ACP countries out and provide some face-saving sweeteners (e.g. expanded EPA-related adjustment support) to make ACP countries sign the European Commission's version of EPAs.

In the same paper, Goodison argues that the European Commission is being hypocritical when calling for simultaneous sequencing of aid and trade reforms in the EPA-process, while at the same time pursuing a policy of reform and restructuring first and market reform follows, internally in the EU – particularly in regard to the agricultural sector. Thus, in relation to its own market, the European Commission is following the same type of policies, that the ACP countries are requesting in relation to the EPAs, but are denied by the European Commission.

## CONCLUSION

The issue of aid in relation to the EPAs is a controversial one. Little agreement on core controversies between the two negotiating parties is evident. At the same time, NGOs seem in a cul-de-sac when formulating viable alternatives based on their harsh critique of the status-quo. Prompting aid-dependent ACP countries not to sign the 10<sup>th</sup> EDF appears ill-advised. Overall, each of the ACP regions express extensive frustration over the omission of aid from the formal negotiations and

requests additional resources for meeting adjustment costs and building and strengthening of the production and supply capacities, which they see as vital to making EPAs effective instruments for the promotion of development. Conversely, the European Commission rejects to provide aid commitments as integral parts of EPAs and seems to think that the ACP countries are overplaying the issue; the European Commission development commissioner, Louis Michel, has reportedly made statements to the effect that he was 'getting tired of hearing this cry that resources are not enough' and remarked that the EU is not 'Santa Claus'.

The root cause of the controversies is different perspectives on how EPAs are to become tools for development. The European Commission prescribes a scenario, in which EPAs will stimulate private sector development by creating regional markets and ensure that the policy climate is conducive to foreign investment and export generation. Pro-development EPAs will first and foremost focus on securing a time-table for removing distorting import restrictions in the form of tariffs, technical barriers to trade, and behind-the-border restrictive measures. Aid will play a role as facilitator of such policies; it is a means to an end. The ACP countries (and the NGOs even more so) have a different perspective. They see EPAs as a tool for the European Commission to 'strong arm' ACP countries into signing-up to policies, which will not work to their benefit, by threatening to stop preferential market access. To sell the agreements to the ACP countries and 'the public', the European Commission is wrapping EPAs in politically correct language of poverty alleviation and development. The A4T initiative is a good example of this: with no real substance, the European Commission is promising aid that it will not legally guarantee to deliver. Additionally, when the European Commission needs to flex its muscles in the negotiations, aid is used as a lever for persuasion.

Not surprisingly, these two perspectives have proved difficult to reconcile in the negotiations. If EPAs are to be signed on time (or at all for that matter), both parties will need to 'come out of their corner' and work on a compromise. However, optimism is hard to come by. This chapter has highlighted the core controversies, which need to be addressed for timely completion of the negotiations. Observers argue that, being the dominant partner, much will depend on how the European Commission will approach the negotiations in the coming months. Greater coordination between DG Trade, DG Development and the EU member states could help provide clarity in relation to:

- a clearer overview of the EU resources available for ACP countries to cover EPA-related needs and the additionality component of the EU commitments.
- the €2bn TRA pledge; as it will only cover trade policy and regulations and trade development activities, how will other needs arising from EPAs (such as trade-related infrastructure, building productive capacity and trade-related adjustment) concretely be addressed? Operationalisation of the A4T programmes by the EU could contribute to a timely completion of negotiations.



Clarity on these issues combined with a more 'open' European Commission approach could pave the way for EPAs based on real compromises made by both parties. On the other hand, the European Commission could adopt (or continue) an approach of exerting leverage on the ACP countries. To this end, additional aid could be used as face-shaving sweetener to 'sugar the pill' (perhaps combined with relaxed rules of origin). Conversely, the threat of 'reprogramming' already promised aid in the absence of a signed EPA could work as an efficient 'broker' to the signing of EPAs by reluctant ACP countries.



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# Appendix 1.

## Measuring Restrictiveness and its Consequences

Since 2000 a literature has emerged seeking to give more substance to the broadly-accepted understanding that PTA RoO act as barriers to trade. This is in the context of a turn in the economic literature on under-utilisation of North-South PTA preferences. While historically this was seen as a product of the (in)efficiency effects of their non-reciprocal character, today it is seen largely in terms of their compliance costs. The latter may reduce real margins of preference to negligible levels. The new literature on RoO restrictiveness therefore has two components: firstly an effort to quantify restrictiveness as such and demonstrate its relation to preference under-utilisation, and secondly one to translate measures of restrictiveness into costs falling on exporters. A sub-component of the first of these efforts examines the compatibility of restrictive PTA RoO with Art. XXIV of GATT (on Free Trade Agreements).

### Quantifying Restrictiveness

Quantification of the restrictiveness of PTA RoO was initiated by Estevadeordal (2000), in relation to NAFTA. Estevadeordal developed a rating system whereby specific RoO were attributed a score between 1 (least restrictive) and 7 (most restrictive). In allocating scores to rules, two basic principles were followed (i) for CTC rules, change at the level of chapter was considered more restrictive than at the level of heading, change at the level of heading more restrictive than at the level of sub-heading, and so on; (ii) VA and TR conditions added to a CTC were considered to be more restrictive than a CTC alone.

In a comparison of NAFTA and EU PTA rules, Estevadeordal and Suominen (op. cit.) conclude that, while both sets of rules are restrictive, NAFTA RoO have a higher overall level of restrictiveness than the EU's. This result represents a comparison of averages of restrictiveness ratings across 20 HS Sections. The EU's ratings are highest for fruit and vegetable products (6.6), textiles and clothing (6.1) and food products (5.0), while NAFTA's are highest for textiles and clothing (6.9), fruit and vegetable products (6.0) and leather goods (5.6). The NAFTA average for all 20 sections is 5.1 and the EU PTA one is 4.5. At the same time, NAFTA RoO show a higher level of variance in their restrictiveness than the EU's, which are consistently 'moderately restrictive' or 'restrictive'.

A critical point in the quantitative literature is that a correlation exists at product level between high levels of RoO restrictiveness and high margins of preference. In other words, where incentives for preference utilization are highest, the highest barriers to their utilisation are found. This is demonstrated by Cadot et al (2005a) using a modified version of Estevadeordal's method. Cadot et al (op. cit.) compare levels of restrictiveness of RoO for tariff lines where there are MFN tariff peaks and

those for tariff lines on which low tariffs are applied.<sup>1</sup> The NAFTA average scores for high and low tariffs are 6.2 and 4.8, respectively, while the EU PTA averages are 4.2 and 3.4 respectively.

Cadot et al (op.cit.) go on to demonstrate an association between RoO restrictiveness at product level and preference under-utilisation. Cadot et al (2005b), examining this relation for the ESA grouping in the EPA negotiations, show that the main losers are non-LDCs, since these are the countries most capable of exporting the value-added products to which restrictive rules most typically apply. Annual losses for the four ESA non-LDCs, represented by the export of goods under EU MFN RoO rather than Cotonou ones, are computed at €201 million (or equivalent to 16% of the value of the preferences for the tariff lines concerned).

Estevadeordal's method has been subject to criticism for the arbitrariness of its assumptions by Erasmus et al (2004). According to these authors, because gradations in the Harmonised System of Tariff Classification was not mainly designed to reflect differences in levels of processing at product level, inputs and outputs of particular processes are often found at the same sub-heading level. Likewise, TRs are not restrictive per se, only specific TRs are. Finally, a combination of less restrictive conditions may be less restrictive than a single more restrictive one. On the other hand, Rivas (2006) reporting the use of an alternative and somewhat more nuanced method for measuring restrictiveness, comes to conclusions broadly consistent with those of Cadot et al.

#### Restrictiveness and compatibility with GATT Art. XXIV

Rivas's contribution (op. cit.) is aimed mainly not at measurement of preference under-utilisation, but at providing an empirical demonstration of the effects of restrictiveness that could support an argument that certain PTA RoO are incompatible with the provisions of GATT Art. XXIV: 5(b), on 'Other Rules of Commerce' (ORCs) within PTAs. This states that ORCs shall not become more restrictive in the transition from one PTA regime to another, unless this prevents the new regime's creation or integrity. Examples are provided of two NAFTA rules, relative to the rules of the earlier Canada-US FTA, where rules have been changed in a more restrictive direction in the absence of such grounds.<sup>2</sup> Rivas does not suggest what remedy could be applied via WTO (or any other forum) in these cases, though.

<sup>1</sup> 'Tariff peaks' were operationalised as tariff levels three times or more higher than average tariff levels, while low tariffs were operationalised as tariffs one third or less of the average.

<sup>2</sup> South Africa's insistence on tightening SADC RoO for several product groups (described in Erasmus et al 2004) would also be WTO incompatible according to this reasoning.

## Restrictiveness and compliance costs

Having demonstrated a relationship between RoO restrictiveness and preference under-utilisation, Cadot et al (2005a) provide estimates of overall trade-weighted costs of compliance with the NAFTA and EU PTA regimes. Prior to this work, most discussion of the subject had relied on extrapolations from Waer's (1992) calculation that compliance costs were equivalent to 3% of the value of EFTA exports to the EU under the old EU-EFTA PTA. Based on a model using reference utilization rates as a proxy, Cadot et al (op. cit.) arrive at a trade-weighted cost of compliance with EU PTA RoO of 8.0% of the value of exports under these PTAs (the cost of compliance with NAFTA is 6.8%). Why EU PTA RoO should have significantly higher compliance costs than NAFTA, despite NAFTA RoO being more restrictive, is attributed to the much higher administrative costs of the EU PTA RoO. These are estimated as 6.8% of EU PTA exports, as opposed to only 1.9% of NAFTA's. In other words, although the restrictiveness of RoO imposes costs considerably higher than would be the case with 'neutral' RoO, in the case of the EU, actual costs of conformity are outweighed by costs of proving conformity.

Almost identical estimates of RoO compliance costs into the US and EU markets for Sub-Saharan African beneficiary countries are arrived at using a slightly different model by Brenton and Ikezuki (2006). They estimate African exporters' compliance costs for AGOA and the US GSP at 6.7% ad valorem, while those for Cotonou are estimated at 8.4%.





## Appendix 2.

# The EU PTA Rules for Fish and Clothing

Although EU PTA RoO generally have been subject to broad and repeated criticism from ACP governments, NGOs, and academics, those for fish/fish products and clothing have attracted the most comment. In the case of fish/fish products this is firstly because elements of them are claimed to depart from the guidelines provided in the WCO Kyoto Convention, in addition to which they appear to openly benefit EU fishing interests. In the case of clothing it is mainly because of adverse comparisons with AGOA on trade creation effects. Not surprisingly, given the earlier discussion, fish/fish products and clothing are subject to either relatively high average tariffs (MFN tariffs for clothing average 12%) and/or to tariff peaks (MFN tariffs for e.g., whole and processed tuna are 22% and 24%, respectively).

### Fish/fish products

The method for determining the origin of fish/fish products is whether they are wholly obtained / produced. All fish caught within a beneficiary country's 12 nautical mile territorial waters and landed in that country are considered to be 'wholly obtained', regardless of the nationality of the vessel it is caught by. The problem is that there is very little commercial stock of fish remaining in territorial waters in the ACP. Therefore most fish are caught in beneficiary countries' EEZs, which extend as far as 200 nautical miles offshore. Under Cotonou, for a fish caught in these waters to be considered wholly obtained, it has to be caught by a vessel registered and flagged in the beneficiary country or the EU or an EU overseas territory (EUOT). The vessel must also be at least 50% owned by nationals of or a company based in the same countries. At least half of the crew (including master and officers) must be nationals of the beneficiary country or the EU or EUOTs. Nationals of these countries may charter vessels belonging to citizens of third countries, but only when a joint EU-ACP committee approves this as 'building local capacity', and where the EU Distant Water Fleet has been offered access by the country concerned and has declined it.

For processed fish, the catch must also be wholly obtained or it can be 'cumulated' from any other ACP country (providing its origin in this country can be proved). 'Diagonal' cumulation is also possible from some but not all neighboring developing countries that are not Cotonou signatories. In the cases both of fish and fish products there is a 15% De minimis, applied on a 'per consignment' basis (i.e., any given consignment can contain up to 15% non-originating material but there cannot be, e.g., separate production runs of originating and non-originating processed fish). For tuna, special rules apply allowing a quota of 2,000 tonnes of loins and 8,000 tonnes of canned tuna to be exported by beneficiary countries without regard to the RoO. This is divided between 9 ACP countries and is administered by the ACP itself.

According to Block and Grynberg (2005), the rules for processed fish depart from the provision of Annex D1 of the Kyoto Convention. Here it is stated that where two or more countries have taken part in the production of a good, then its origin should be determined by the method of substantial transformation (rather than that of whether it is 'wholly obtained'). The authors go on to argue that the EU choice of 'wholly obtained' is designed to provide a subvention to the EU Distant Water Fleet. On its basis, the fleet obtains near-exclusive or exclusive access to ACP waters while at the same time obtaining a very high preference margin for its 'exports' – or a substantial premium where it sells its catch to canneries in the few ACP countries with a significant canning industry.<sup>1</sup>

## Clothing

The Cotonou rule for clothing comprises a TR for 'double transformation'. That is, for clothing to be considered as originating both production of fabrics or cloth and production of items of clothing itself have to take place within the same beneficiary country. Bilateral and full ACP cumulation is possible, as is diagonal cumulation from three regional groupings of developing countries (ASEAN, SAARC and the Andean groups). Value added in the beneficiary country carrying out the final export must however exceed value added in the countries from which origin of thread, fabric, cloth or components are cumulated. The rule is mitigated by a 15% de minimis allowance.

Traditionally the Commission defended the Cotonou clothing rule in terms of its designed aim of stimulating vertical integration in ACP countries.<sup>2</sup> In reality vertical integration in the ACP was achieved only by Mauritius, where earnings from sugar exports, permissive bank lending practices and local community ties to Hong Kong favoured large-scale local and foreign investment. Elsewhere, until the late 1990s when Mauritians began investing in neighboring Madagascar to take advantage of cheap labour, there was very little wider supply response. The Commission's position was widely criticised, in its own terms, for failing to acknowledge changes in the organization of the global clothing trade in the years following 1975, when the Lomé Convention was originally signed. These changes entail a model where production of textiles and clothing on a geographically separate basis is normal and where there is relatively little competitive advantage in vertical integration.

Late in 2000 the US government introduced AGOA. Under this arrangement, distinct RoO were applied to Mauritius, South Africa, Botswana and Namibia<sup>3</sup> on the one hand and to other Sub-Saharan African countries (so-called 'lesser developed beneficiary countries')<sup>4</sup> on the other. Origin-

<sup>1</sup> Papua New Guinea, Mauritius, Seychelles, Ghana, Senegal and Namibia.

<sup>2</sup> Similar arguments were advanced by South Africa for a the highly restrictive SADC clothing RoO, see Erasmus et al (2004).

<sup>3</sup> Botswana and Namibia were subsequently admitted to this second category.

<sup>4</sup> Note that this group included non-LDCs such as Kenya.

ating products from the first group were faced with a three stage ('yarn forward') TR.<sup>5</sup> This group could cumulate from the US or any other AGOA beneficiary and had access to a 10% de minimis. For the second group there was a time-limited derogation (currently extended until 2012) allowing origin to be conferred on the basis of 35% local value added. This is currently limited by a quota ceiling of 3.5% of all US imports by volume. As noted earlier, conformity requirements are strict. In the context of the relatively generous quota ceiling, this is the most neutral clothing RoO applied by any large trading country in a PTA.

	1999	2000	2001	2002	2003	2004	2005	2006
AGOA	2.8	2.7	359.5	803.3	1202.1	1613.5	1418.4	1255.6
Non-AGOA	619.2	786.5	638.5	333.0	349.9	142.6	46.0	36.2
Total	622.0	789.2	998.0	1136.3	1552.0	1756.4	1464.4	1291.8
M&SA %SSA	359.1 57.7%	420.5 53.3%	450.8 45.2%	469.7 41.3%	538.7 34.7%	408.0 23.2%	270.6 18.5%	165.8 12.8%
SSA – M&SA	262.9	368.7	547.2	666.6	1013.3	1348.4	1193.8	1126.0

Key: M: Mauritius; SA: South Africa; SSA: Sub-Saharan Africa

	1999	2000	2001	2002	2003	2004	2005	2006*
Total	959.2	1035.7	1015.3	839.9	932.8	1007.7	916.2	1035.9
M&SA %SSA	741.3 77.3%	708.0 68.4%	670.9 66.1%	643.2 76.6%	703.8 75.4%	710.7 70.5%	600.0 65.5%	640.2 61.8%
SSA – M&SA	217.9	327.7	344.4	196.7	229.0	297.0	316.0	395.7

Key: \*EU 25 ; for other abbreviations see key to Table 1.

<sup>5</sup> Yarn to thread, thread to fabric, fabric to clothing.

Unlike Cotonou, AGOA has been successful in generating a substantial supply response. Sub-Saharan Africa's exports to the EU have remained practically stationary since 2000. The share of the two 'traditional' African exporters, Mauritius and South Africa, has remained in a range between 62% and 77% of all Sub-Saharan African clothing exports to the EU, while exports from all other countries have remained in a range between \$300-400 million per year. Exports to the US on the other hand increased by over \$500 million between 2000 and 2006. The whole of this increase has come from non-traditional producers, while exports to the US by traditional exporters have declined. Following removal of quotas on China total Sub-Saharan African exports to the US have declined since 2004 – but more than two thirds of this decline is accounted for by the traditional producers. Thus, there are grounds to believe that a US-directed clothing sector will persist in non-traditional producing countries in Sub-Saharan Africa in the long-term (post-Multifibre Arrangement) environment. This case appears to demonstrate a link between neutral RoO, trade creation and export diversification.

# Appendix 3.

## Early European Commission definition of trade-related assistance

Source: EC (2003)

**Category 1 – Trade policy and regulation.** Support with a direct focus on the Multilateral trading system (MTS) and the development of an appropriate trade policy environment. This is likely to include technical assistance, capacity building and institutional strengthening to enable the development of effective trade policy, primarily at public sector/government level. This could include work to develop understanding of and ability to implement multilateral rules in any one of the areas below.

- dispute settlement
- customs valuation
- TBT and SPS
- TRIPs
- trade mainstreaming in proposals/development plans
- tariff negotiations – non-agric
- trade and environment
- trade and investment
- trade and competition
- trade facilitation
- transparency and government procurement
- accession
- market access
- agriculture
- services
- rules
- tariff reform
- trade-related training education
- negotiation capacity
- regional trade agreements (RTAs)

**Category 2 – Trade development.** A broadening of the definition to include activities aimed at some of the supply-side constraints which impact directly on a country's ability to exploit its international trading potential and in particular private sector development from an institutional perspective. This could include support in any one of the areas below.

- trade promotion strategy design and implementation
- market analysis and development
- business support services and institutions
- public-private sector networking
- e-commerce
- trade finance

Category 3 – is likely to be critically important for successful trade reform and is an area in which the Commission is active. Activities should include ‘indirect’ actions such as support for the macro-economic and fiscal adjustment process that may be necessitated by new trade policy measures such as tariff reductions. For example, a review of other taxation mechanisms such as VAT may be appropriate following trade policy reform. Interim budget support measures may also be necessary to facilitate adjustment.

Category 4 – is trade capacity in its broadest sense aimed at diverse long-term supply-side issues, which could include development assistance for infrastructure and to sectors such as health and education, all of which can have long-term effects on poverty and competitiveness.