

# The Relevance and Applicability of the Most-Favoured-Nation Treatment Clause in International Trade Agreements

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**Abstract:** - The paper examines the relevance and applicability of the Most-Favoured-Nation Treatment Clause in International Trade Agreement. The paper articulates other World Trade Organization (WTO) standards, such as National Treatment and the International Minimum Standards. The MFN is an instrument adopted by WTO to reduce discrimination and enhance transparency in international exchange of goods, services, investments, and property rights. The paper revealed that the MFN standards are substantive acknowledgement of the classical liberal approach to international trade, as expounded by Smith, Harberler, etc. The paper noted that developing countries have not benefitted sufficiently from the various treatment standards. First, trade have not been so liberalized by the industrialized countries because of protectionist regimes, while low capital, manpower and technological exports of the LDCs have limited the chances of the poor countries to benefit from trade agreements. A liberal trade agreement anchored on MFN and other standards of the multilateral institutions will culminate in an agreement between unequals. The LDCs do not have the investment capacity. Thus the opportunities provided by the various treatment standards are reaped by the superior partners on the agreement between the LDCs and the industrialized countries. The paper suggests that LDCs should explore more of Bi-lateral agreements. In Bi-lateral agreement the developing countries, using experts can negotiate trade agreement that will accommodate the economic policy of government and development plans. It is also instructive that African countries improve in the production of capital goods and technology for export. Export of tertiary goods and technology will launch African countries into the competitive world trade.

**Keywords:** Most-Favoured, Nation, Treatment, International, Standard, WTO, Trade Related Investment Measures, Intellectual Property Rights.

## I. INTRODUCTION

It is true that no nation in the world is totally self-sufficient, thus nations depend on one another for goods and services. Even the highly industrialized nations would need the raw-materials from the less developed nations to further its production (Anyanwu, 1997). The interdependence amongst nation states makes international trade critical in the political economy of nation states. International trade therefore plays a significant role as it enable States get needed goods and

services from one another and also supports sustainable development of States globally.

In international trade transactions, importers and exporters most times try to and indeed do actually use discriminatory regulations, such as tariff, taxes, quotas and other protection trade instruments to give undue advantage to their national economies. The arguments of the protectionists have been that nations could consciously manipulate their economy to promote growth and development; that high level of premium should be attached to attaining and retaining the wealth of nations, and that achievement in trade is measured on the basis of surpluses in the balance of payment (Nyong, 2005). But the discriminatory trade regulations which nations use to achieve its economic growth, sometimes affect competition between domestic and imported goods leading to reduction in nation's economic welfare. Adam Smith (1776) had advocated for a free non-discriminatory trade. According to him, a free-nondiscriminatory and transparent trade will benefit all the country and regions participating in trade. Other classicists such as Ricardo, 1817;Harberler, 1959.....

It is against this background that international multilateral instruments and institutions such as General Agreement on Tariff and Trade (GATT) and World Trade Organization (WTO) were established. The objective according to Soludo (1995) is to promote freer global trade and economic relationships among member states. GATT and the WTO, emphasizes non-discrimination and national treatment; the aim is to achieve freer trade and improve market access, through regular trade negotiations at which tariffs are lowered and implementation of trade agreements between nations.

The multilateral trade institutions subsequently became the platform for the international community to launch various treatment standards, including the Most-Favoured-Nation (MFN), the National Treatment, and the International Minimum Standards. These standards are instituted to liberalize trade to certain extent, discourage discrimination, promote transparency, and improve market access by the weaker nations of the world. But are the developing nations, through the MFN, National Treatment and International Minimum Standards, able to have access to world market and enhance the welfare of its people? What is the applicability of

these standards to the emerging markets? and in what ways can the standards work to enhance the chances of developing countries penetrate the world market with its attendant benefits? The second section of this paper constitutes the conceptual framework, the third section is a brief history of MFN treatment standard, while the fourth section analyzed the relevance of the MFN standard to international trade, the fifth section analyzed the applicability of MFN to LDC's and the conclusion in section six.

## II. CONCEPTUAL FRAMEWORK

### *The Most-Favoured-Nation Clause (MFN)*

The MFN clause began to play an important part in international trade in the first half of the 17<sup>th</sup> century. At the time, the reference to Most-Favoured-Nation clause (that is privileges granted to the beneficiary state) was no longer limited to named nations, but any third state.

In a treaty between Great Britain and Portugal in 1942, the MFN clause acquired its most prominent posture. Britain was entitled to enjoy all the immunities accorded to the subjects of any nations whatever in treaty relation with Portugal. Again, in 1960, United Kingdom and France entered the Cobden Treaty, which in modern times included an unconditional MFN clause.

The MFN clause was a core obligation of commercial policy under the Havana Charter. Members were required to give due regard to the desirability of avoiding discrimination between domestic and foreign investors. It was the Havana Charter that provided for the establishment of the International Trade Organization (ITO), which later transform to the World Trade Organization (WTO).

### *National Treatment Standard*

The World Trade Organization introduced the National Treatment Standard agreement. It is also applicable in the General Agreement on Trade in Services (GATS) and the Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS). The National Treatment prohibits discrimination between imported and domestically produced goods with respect to internal taxation or other government regulations (Davis, 2008).

### *International Minimum Standard*

The International Minimum Standard seek to advance the interests of states in expanding trade and investment in territories with rudimentary forms of government or where local institutions and legal standards did not provide protection satisfactorily to capital exporting countries (Alwyn, 1938).

The international minimum standard was tied to the international law doctrine of state responsibility for injuries to aliens. IMS, provides that an injury done to an alien was an injury done to the alien's home state and permitted claims and protection by the home state when domestic recourse was

unavailable or exhausted. The nationality of the alien which encompassed corporations as well was the pivotal fact of the minimum standard. The state of the nationality not only owned the investor's claim, but could ignore it, pursue it, or settle the claims at its own discretion. The home state can even dispose any money or other benefits it could receive for the claim as it desired, without the permission of the investor (UNCTAD, 2010).

The minimum standards prescribe that investors must exhaust all remedies in the host state. If however the investor discovers the futility of pursuing local remedies, because of the uncivilized and arbitrary rules of the home state, and the capital exporting country subjected to an absolute minimum below international standards, then the capital exporting country could use its diplomatic muscle to protect its investor or request for payment of compensation to the investor.

### *Trade Related Investment Measures (TRIMS)*

This agreement was negotiated during the Uruguay Round. It applies to measures that affect trade in goods only. It seeks to prohibit the use of certain investment measures that can have trade-restrictive and distorting effects. It states among other things that no member shall apply a measure that is prohibited by the provisions of GATT Article III (National Treatment) or Article XI (Quantitative Restrictions). The agreement also establishes a committee on TRIMS to monitor the operation and implementation of its provisions.

### *Trade Related Aspects of Intellectual Property Rights (TRIPS)*

The TRIPS agreement introduced intellectual property law into the international trading system for the first time and it is the most comprehensive international agreement on intellectual property. TRIPS require WTO members to provide and protect copyrights and other intellectual property rights. TRIPS aim at contributing to the promotion of technological innovation and to the transfer and dissemination of technology to the mutual advantage of producers and users of technological knowledge. TRIPS specify enforcement procedures, remedies and dispute resolution procedures.

## III. THE RELEVANCE AND SCOPE OF MFN STANDARD IN INTERNATIONAL TRADE AGREEMENT

The Most-Favoured-Nation standard plays a critical role in international transactions. MFN covers the rights a state obtain when it engages in an international trade agreement with another state which may involve the exchange of capital, goods and services across international borders (Article XXIV of GATT). A country accorded MFN status may not be treated less advantageously than any other state with MFN status by the promising state. MFN ensures a level playing field between all trading partners and by which position it is the central pillar of international trading system.

The MFN standard also ensures for an equality of competitive conditions between foreign investors, who seek sufficient assurance that there will not be adverse discrimination, which

puts them at a competitive disadvantage. Such treatment includes the reduction of tariffs, customs duty for some investors, and maintaining same for other set of investors—resulting in discriminatory practices by the home state. The MFN standards thus help to establish equality of competitive opportunities between investors from different foreign countries. It prevents competition between investors from being distorted by discrimination based on nationality considerations; MFN thus follows the objective and purpose of the international trade.

Smith (1776) had argued that the objectives of international exchange of goods, include, increases in total world output, and various options for the consumers in countries engaged in trade. Other objectives of external trade include specialization and efficient production of goods by trading nations and improvement of the welfare of citizens (Sodersten & Geoffrey, 1980). The MFN treatment also conforms to the Ricardian theory of trade. The MFN standard makes it possible for nations to import from the most efficient supplier in accordance with the principle of comparative advantage. For instance, if Nigeria can supply petroleum products at a lower price than Ghana, South Africa can increase its economic efficiency by importing from Nigeria. If South Africa applies higher tariff rates to petroleum product from Nigeria than to product from Ghana, South Africa may be forced to import petroleum product from Ghana, even though Ghana is not an efficient supplier. The act of importing from inefficient country will create trade distortion, reduce the welfare of South Africans and the entire world trade efficiency (Ricardo, 1817).

The MFN treatment clause may cover the substantive matters under transaction; define the beneficiaries, the covered phase of investment and any other applicable exceptions. MFN thus covers both the pre/post establishment phase of an investor's business in a foreign land. The exception in MFN agreement can be generic or country-specific exceptions.

It is important to note that MFN standard clause in trade agreements include specific qualification of clarification in order to provide certainty and guidance so as to facilitate its interpretation and application as intended by the contracting parties. MFN treatment thus extends to investors and their investments.

An MFN standard clause in a trade agreement may include specific qualifications or clarification; these are however not meant to limit the scope of application per se, but constitute mere guidance and clarification on how the clause is supposed to be applied. Economic agreements in recent times put more emphasis on MFN treatment clause, for instance, the specifications of the method for compassing the treatment afforded to foreign investors of different nationalities, or indicating the specific activities within the covered phase to which the treatment applies.

The MFN standard clause in international trade agreement in modern times re-echoes the classical approach to international

trade; which emphasizes free trade, economic liberalization and non-discrimination among trading nations (Smith, 1776; Ricardo, 1817). However, there are circumstances, in which the relevance of MFN becomes subjective, thus create exceptional cases to the MFN Treatment Standard.

#### *Exceptions to MFN Clause*

Regional economic bodies such as ECC, ECOWAS, etc. impose customs unions, free trade areas to liberalize trade among the member states; and maintain certain trade barriers for non-member countries. The activities of the regional economic blocks may run contrary to the principle of liberal trade and MFN. In other words, countries that are outside the regional blocks are treated differently. This will affect free trade and welfare of citizens.

Article XXIV of GATT provides that regional economic blocks can conform to MFN rule under certain conditions. First, tariffs, quotas, custom duties and other trade barriers must be eliminated in all trade transactions within the region. Secondly, the tariffs and other barriers to trade applied to outside country must be higher or more restrictive than they were prior to regional integration.

The 1979 GATT decision on “Differential and more favourable treatment, reciprocity, and fuller participation of developing countries is against the letters of MFN clause. By the Generalized System of Preferences (GSP), developing countries' products are granted lower tariff rates than those enjoyed under MFN standards. The GSP privileges are accorded to developing countries by the industrialized countries, because of special relationship, or poor economic indices. In the case of non-application, the benefits enjoyed by other members are not provided to the country of non-application. This is against Article XIII of the World Trade Organizations.

The Marrakesh Agreement which establish the WTO states clearly that “agreement and the Multilateral Trade Agreement in Annexes 1 and 2 shall not apply as between any member and any other member; when at the time the WTO was established, Article XXXV of GATT is been implemented and enforced between original members of the WTO, which are also members of GATT as at 1947”.

Part II chapter 1 of the MFN treatment principle also state that under WTO Article IX:3, countries may, with the agreement of other members, waive their obligations under the agreement. While Article IX:3 stipulates that in exceptional circumstances, the terms and conditions governing the application of the waiver and the date on which the waiver will be terminated shall clearly be stated ([www.mefi.go.jp/english/report/downloadfiles/gcTo202e.pdf](http://www.mefi.go.jp/english/report/downloadfiles/gcTo202e.pdf))

#### IV. APPLICABILITY OF MFN TO THIRD WORLD COUNTRIES' TRADE

##### *Agreements*

The Most-Favoured-Nation (MFN) and its related clauses, such as national standard and TRIPS, have become critical instruments in trade negotiation/agreement among nations. MFN status, once accorded a state, entitles that state to be treated no less advantageously than any other state with MFN status by the promising state. MFN clause thus apply to group of countries in trade agreement, but most importantly on exchange of capital goods, and other technical goods and services across international borders.

In this respect, developing countries, more often than not are limited in the application of MFN. Greater number of LDCs engage in international trade exports basically in raw-material and semi-processed goods. In labour, they export unskilled labour that cannot benefit from MFN clauses. As a matter of fact, most unskilled labour find their way to Europe through informal routes that cannot be recorded, documented, for MFN application in their export.

The MFN standard helps to establish equality of competitive opportunities between investors from different foreign countries. It also prevents competition between investors from being distorted by discrimination based on national discrimination.

But investors from the LDCs suffers discrimination from the domestic economic policies, for instance, investors from the LDCs suffers dealer in shipment of goods, illegal taxes and political harassment. At the exporting destination, the advance countries, introduce other conditions for exporters. In 2017, shipment of yams from Nigeria was rejected in the UK, based on alleged packaging conditions/preservations. These are clear discrimination, not captured in MFN and other related trade agreements.

In the context of Africa, one crucial factor concerning the protection of foreign investment as specified in MFN, need to be highlighted. The mutual relationship called for in MFN, NT, IT and TRIPS, assumes that investors of states in agreement can invest in territories of each other. In reality however, it is one sided agreement. Africa states do not have investors who can meaningfully invest in the territories of the developed countries. The unequal status in terms of investment capability, denies the LDCs the benefits of the international trade instruments designed to eliminate discrimination and ensure trade transparency in trade transactions among nations (Okogbule, 2012).

In the EAC-EU EPA trade negotiation, the MFN clause as contain in Article 16(2) has been the obstacle to the conclusion of the talks. The EAC partner group, made up of Burundi, Kenya, Tanzania and Uganda, have protested against the inclusion of an MFN clause in paragraph 2, which is about the EU proposed inclusion of an MFN clause requiring the EAC to extend to the EU any more favourable treatment that it may give in the future to other trading partners (<https://www.ictsd.org>). These are aspectsof the MFN, the advance countries exploit to benefit from trade agreements between them and the LDCs, not just in the immediate, but

even in the future. In Nigeria, the oil majors have exploited the WTO trade instruments to tie the sector permanently under their control in agreements as far back as a century.

But MFN clause is not condition precedent to partners to make trade agreements a WTO compatible agreement. African countries can resort Bilateral Trade Agreements. In BITs, countries will apply the best rules that comply to local policies and law, and compatible with national economic plans and future development of the country.

African countries to benefit from MFN and other related WTO trade standards produce and export manufactured goods, technology and investments that is critical to the development of the industrialized countries. Export of industrialized goods, will give the LDCs the competitive edge in trade negotiation/agreements.

LDCs must also begin to train manpower on trade negotiations, particularly at the multilateral levels. Trade negotiation has become complex. It heeds experts to negotiate trade agreements, to enhance the opportunities of LDCs in the import, export, business. Nigeria in particular must block all illegal routes through which materials and manpower leak outside the country. In trade negotiation, the statistics/recovers only legal goods/ investment delivered through the borders and seaports. Goods and manpower sneaking into the industrialized countries through the borders are not documented and is a leakage that undermines the trading strength and not accommodated by the privileges conferred by MFN standards, while negotiating trade agreements.

## V. CONCLUSION

The importance of the Most-Favoured-Nation (MFN) Clause in international trade negotiation/agreement cannot be over-emphasized. As an advanced classical liberal concept in international trade, the MFN has branched out to other trade liberal concepts, such as the National treatment, International minimum standard, trade related investment measures, trade related aspects of intellectual property rights to mention a few. The MFN encourages free trade, non-discrimination and transparency in international exchange of goods, services and property rights.

As a standard rule of the World Trade Organization, nations are expected to give to all other countries, the preference they give to one, whether at the multilateral or bilateral agreements. The exception to this rule however lies on specific arrangement among group of nations, such as EU, ECOWAS, that have decided to give specific preference to member States. The conditions may conform to WTO standards, thus creating preferential treatment and discrimination, which negates the philosophy behind the Most-Favoured-Nation Clause of the World Trade Organization.

The MFN Clause applies to all nations of the WTO, however, the LDCs are limited by low exports to the advanced

economies, and available exports are raw-materials and semi-processed goods. The advanced countries export capital equipment's, technology, etc. This imbalanced exchange reflects in trade agreements, that the LDCs in deficit position. Investors in the LDCs do not also have resources to invest in the advanced economies. Thus the benefits of trade agreements are not fully harnessed by the developing countries.

It is therefore incumbent on the LDCs to improve the quality of exports, empower their investors and provide enabling environment for overall external performance.

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