

The Justifications and Legal Framework for Liberalising Intra-OIC Trade

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This paper examines the justifications and legal framework for the liberalisation of intra-OIC trade. Before these factors are examined, this paper finds that intra-OIC trade is still low in volume and in proportion if compared to other trade systems. Intra-OIC trade is also concentrated in few OIC Member States and in certain types of products. These findings inform the discussions on the justifications of intra-OIC trade liberalisation and this paper finds that due to the economic conditions prevailing in most OIC Member States it is highly likely that such liberalisation results in trade diversion. Thus shallow integration was preferred by economists so that the OIC 'region' will still be open to flows of goods to and from non-OIC countries. This paper finds that the legal framework for intra-OIC trade liberalisation i.e. the TPS-OIC regime operates according to these principles despite its poor enforcement. However, this paper also finds that there are wider considerations that may require the TPS-OIC regime to balance between minimising the chance of trade diversion and improving the unfavourable economic and trade structures that prevail in most OIC Member States.

1. Introduction

There is rich literature on the pros and cons of regionalism by which States are united by certain common goals arguably defined by an 'identity'. However, within the quest for an identity for the Muslim world lies the dichotomy between the realist and liberal approaches towards justifying regionalism. To the realists, it is power which attracts

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States to regionalise but to the liberals, the economy is the factor for such State behaviour.²

Against these backdrops, the relevance of the Organization of the Islamic Conference (OIC) has always been questioned especially when in times of conflicts, it failed to promote unity and advance the political interests of the Muslim countries. At this juncture, economic integration has become a more favourable mechanism for Islamic regionalism. Such mechanism involves the promotion of trade among the OIC Member States (intra-OIC trade). However, as economic regionalism is always appraised in the context of the significance of trade liberalisation, the need to examine the mechanism created for facilitating intra-OIC trade liberalisation surfaces. As such, this paper will critically analyse the justifications and legal framework of the process which promotes the liberalisation of trade between OIC Member States.

The paper will start with a framework discussion on the stance of the OIC to trade liberalisation. Then, the paper will discuss the current state of intra-OIC trade. This will be followed by an analysis of the various justifications of intra-OIC trade liberalisation. Then the paper will elucidate the legal framework for such process. This brings the paper to the TPS-OIC regime. There will also be a discussion on the enforcement of such regime before the paper concludes.

2. Trade Liberalisation Agenda in the OIC Charter

The OIC which was established in 1969 was originally founded for the purpose of liberating the Al-Quds (Jerusalem) from Israeli occupation.³ However, the objectives of the OIC as stipulated in its Charter go beyond politics. Article II of the OIC Charter mentions economic cooperation as one of the objectives of the OIC. This objective has been expanded by the General Agreement on Economic, Technical and Commercial Cooperation which was adopted in 1977. Article 8 of that Agreement states:

² Higgot, R. (1998), The international political economy of regionalism – the Asia-Pacific and Europe compared in W. D. Coleman and G. R. D. Underhill (eds), *Regionalism and Global Economic Integration: Europe Asia and the Americas*, Routledge, London, pp. 43-47.

³ <http://www.oic-oci.org>.

“While keeping in view the obligations under other Agreements already concluded by them, the Member States will:

- (a) endeavour to apply equal and non-discriminatory commercial treatment towards one another with regard to foreign trade policies;
- (b) strive to enlarge and develop trade exchanges among themselves, inter alia through trade liberalisation, by reducing or removing the customs or other restrictions that are applied to export/import activities among them through bilateral or multilateral trade arrangements; and
- (c) give consideration to the special circumstances and situations of the least developed member states.

Article 8 defines the attitude of the OIC towards the liberalisation of trade between OIC Members. It also provides the legal basis for any trade-liberalising efforts to be taken by the OIC and its Members based on the GATT principles of non-discrimination. They include the establishment of the Standing Committee for Economic and Commercial Cooperation of the OIC (COMCEC) which acts as a forum for any economic and trade-related deliberations at the OIC level including those which are reflected in the Trade Preferential System among the Member States of the Organization of the Islamic Conference (TPS-OIC). The TPS-OIC regime is the legal framework selected in this paper for facilitating the liberalisation of intra-OIC trade.

3. The Current State of Intra-OIC Trade

The share of the OIC Member States in overall global trade is still small as compared to other regions. In 2005, total exports of the OIC Member States accounted for 9.47% of the world exports while total imports accounted for 7.38% of the world imports. However, in terms of commodity trade, there had been tremendous increase in both exports and imports values of the OIC Member States between 2004 and 2005 – 27.61% for the former and 19.72% for the latter. Increase in the prices of fuels and other extractive industries were cited as one of the reasons. However, it must be noted that there had been a significant decrease in exports and imports of machinery and transport equipments, chemicals and food products.

The share of intra-OIC trade of the overall trade of the OIC Member States also remains small. In 2005, the share was still 15.5% (however

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there was an increase from 14.5% in 2004). Intra-OIC exports share was 13.7% (from 13% in 2004) of overall exports of the OIC Member States and intra-OIC imports share was 17.3% (up from 15.9% in 2004) of overall imports of the OIC. As will be seen below, such pattern (i.e. small share of intra-OIC trade) is commonplace among some OIC Member States which are the major players not only in intra-OIC trade but also overall trade.

The product distribution of intra-OIC trade reveal that intra-OIC trade is still limited to low value added and labour intensive economic sectors which are prevalent in developing countries. It is worth noting the statement by UNCTAD - 'a number of developing countries continue to depend on the export of undynamic products with low income elasticity and low value added, from both the primary and manufacturing sectors. Many labour-intensive manufactures exported by developing countries are behaving increasingly like commodities, with a risk of market saturation that could lead to a fallacy of competition'.⁴ This statement is of much relevance to the situations underlying intra-OIC trade since the information on the economic position of OIC Member States suggests that most of them have less economic diversification and still depend on agriculture for domestic production. There are some Member States which have expanded their industrial activities but they are not doing well in the manufacturing sector except Malaysia and Indonesia.

The data in the tables 1 and 2 above show there was no clear disparity between trade in primary and manufactured goods among OIC Member States. However, it shows that intra-OIC trade was still concentrated in the 'traditional sector' *i.e.* mineral fuels which accounted for 38.6% and 32.01% of total intra-OIC exports and imports respectively. Saudi Arabia was the largest exporter with 41.55% of intra-OIC total exports of mineral fuels. The products with the second-largest share of intra-OIC trade were manufactured articles classified according to the raw material (17.47% for export and 19.2% for import). Both types of products accounted for half of the products traded intra-OIC. Other manufactured products with a substantial share in intra-OIC trade were chemicals (9.25% of total intra-OIC exports and 10.24% of intra-OIC imports), machinery and transport equipments (9.84% (exports) and

⁴ UNCTAD (2002), *Trade and Development Report, 2002 – Chapter II (The Multilateral Trading System after Doha)*, United Nations, New York/Geneva, p. 33.

11.99% (imports)), and miscellaneous manufactured products (under Section 8 of SITC) (5.16% (exports) and 5.17% (imports)). Here, special emphasis needs to be placed on the latter two types of products which are high-value-added and have high technological profile, and the statistics shows that their share of overall intra-OIC trade was still low.

Table 1: Intra-OIC Exports According to SITC⁵ Product Classifications (2005)

Type of Products According to the Relevant Sections of SITC	Share of Intra-OIC Exports (%)
Mineral fuels (Section 3 of SITC)	38.6
Manufactured articles classified according to the raw material (Section 6 of SITC) ⁶	17.47
Food products & live animals for human consumption (Section 0 of SITC)	10.78
Machinery and transport equipments (Section 7 of SITC)	9.84
Chemicals (Section 5 of SITC)	9.25
Miscellaneous manufactured products (Section 8 of SITC) ⁷	5.16
Oils and fats (Section 4 of SITC)	2.84
Non-edible raw materials (Section 2 of SITC)	2.52
Manufactured products like personal articles, weapons and arts objects (Section 9)	2.49
Beverages and tobacco (Section 1)	1.05

Source: ICDT⁸ Report on Trade among OIC Member States (2007)

⁵ SITC here refers to the Standard International Trade Classification issued by the Department of Economic and Social Affairs of the United Nations Secretariat.

⁶ Such articles include paper, textile, iron and steel, rubber manufactures.

⁷ Such products include clothing, electric, music products, furniture, textile fabrics, footwear, cameras, medicine & their spare parts.

Table 2: Intra-OIC Imports According to SITC Product Classifications (2005)

Type of Products According to the Relevant Sections of SITC	Share of Intra-OIC Exports (%)
Mineral fuels (Section 3 of SITC)	32.01
Manufactured articles classified according to the raw material (Section 6 of SITC)	19.1
Machinery and transport equipments (Section 7 of SITC)	11.99
Chemicals (Section 5 of SITC)	10.24
Food products & live animals for human consumption (Section 0 of SITC)	8.99
Miscellaneous manufactured products (Section 8 of SITC)	5.17
Non-edible raw materials (Section 2 of SITC)	4.86
Manufactured products like personal articles, weapons and arts objects (Section 9 of SITC)	3.75
Oils and fats (Section 4 of SITC)	3.22
Beverages and tobacco (Section 1 of SITC)	0.67

Source: ICDT Report on Trade among OIC Member States (2007)

Surprisingly the same applies to trade in food products and other related products (including oil and fats and beverages and tobacco). The share of such trade was only 14.67% for export and 12.88% for import. This implies that most of such products were still exported to and imported from non-OIC Members. This must also be read in light of the fact that the contribution of agriculture to the domestic product of overall OIC

⁸ ICDT is the acronym of the Islamic Centre for Development of Trade.

Member States is small. Where such contribution is big, the countries concerned generally fall under the category of low-income countries.⁹

The geographical distribution of intra-OIC trade shows that there are only a few players among OIC Member States. In 2005, 10 OIC Member States accounted for 74.71% of intra-OIC exports and 59.27% of intra-OIC imports. The countries are Saudi Arabia, UAE, Turkey, Malaysia, Indonesia, Iran, Pakistan, Kuwait, Oman and Nigeria.

Table 3: Main Intra-OIC Exporters in 2005

Country	Intra-OIC Exports in Million USD	Share of Intra-OIC Exports in the Total Exports of the Country (in %)	Share in Intra-OIC Total Exports (in %)
Saudi Arabia	30446.79	41.07	22.66
UAE	15902.92	17.43	11.84
Turkey	13047.88	17.76	9.71
Malaysia	10088.33	7.7	7.51
Indonesia	8340.27	10.09	6.21
Iran	6527.02	12.00	4.86
Kuwait	5021.71	14.25	3.74
Pakistan	4367.20	27.22	3.25
Nigeria	3500.66	8.44	2.61
Oman	3119.46	17.92	2.32
Total (10)	100362.24		74.71

Source: ICDT Report on Trade among OIC Member States (2007)

⁹ According to the Statistical, Economic and Social Research and Training for Islamic Countries (SESERIC), as of 2005, the agricultural sector has the largest share in the GDP of 13 OIC Member States. The 5 most agriculture-dependent Member States are in Sub-Saharan Africa (*i.e.* Guinea-Bissau – 60.26%, Comoros – 51.02%, Sierra Leone – 45.7%, Togo – 43.63% and Mali – 36.58%). This reflects the low level of industrialisation within those countries. It must also be noted that Guinea-Bissau had the lowest income among all OIC Member States in 2006. See SESERIC's statistics database webpage at http://www.sesercic.org/stat_database.php.

Table 4: Main Intra-OIC Importers in 2005

Country	Intra-OIC Imports in Million USD	Share of Intra-OIC Imports in the Total Imports of the Country (in %)	Share in Intra-OIC Total Imports (%)
Pakistan	9698.75	39.73	11.13
UAE	12659.02	13.29	9.23
Oman	3238.56	37.36	7.07
Malaysia	8418.41	7.48	7.05
Indonesia	9367.13	17.77	6.83
Iran	9670.30	22.19	6.14
Turkey	15261.71	13.09	5.60
Nigeria	2097.57	9.33	2.36
Saudi Arabia	7682.89	12.89	2.31
Kuwait	3171.16	20.64	1.53
Total (10)	81265.50		59.27

Source: ICDT Report on Trade among OIC Member States (2007)

Table 3 shows clear disparity between the largest intra-OIC exporter *i.e.* Saudi Arabia and other OIC Member States. In 2005, Saudi Arabia contributed to 22.66% of overall intra-OIC exports. Saudi Arabia was also the largest exporter in world trade among the OIC Member States. It was the 18th largest exporter in the world and its exports value was USD181.4 billion.¹⁰ Exports of mineral fuels which topped the list of intra-OIC exported products explained why Saudi Arabia had the largest share in terms of intra-OIC total exports. In 2005, 41.55% mineral fuels exported to other OIC Member States were from Saudi Arabia. Statistics also shows the country's dependence on such product for its intra-OIC exports where in the same year, 72.95% of its intra-OIC exports were mineral fuels. The individual share of other main players (except UAE) accounted for less than 10% of intra-OIC total exports (the share of UAE was 11.84% and the export of mineral fuels was once again one of the contributing factors for such figure).

¹⁰ See http://www.wto.org/english/res_e/statis_e/its2006_e/its06_overview_e.pdf, p. 17.

There is however more even distribution in intra-OIC imports as can be seen from Table 4. Pakistan topped the list with 11.13% share of intra-OIC total imports. This is followed by UAE (9.23%), Oman (7.07%) and Malaysia (7.05%). This is in tandem with the lower share of the ten largest intra-OIC importers *i.e.* 59.27% as compared to intra-OIC exports (74.71%).

It is also important to note the share of an OIC Member State's intra-OIC exports and imports in their total exports and imports. There is a common feature for both exports and imports – none of the main players traded with any other OIC Member States in more than half of their total trade in 2005. In terms of exports, only Saudi Arabia and Pakistan had the share of their intra-OIC exports exceeded 20% in their total exports. However, the figure for Saudi Arabia was impressive where 41% of their total exports were intra-OIC. This was followed by Pakistan whose share of intra-OIC exports was 27.22% of its total exports. Interestingly, Malaysia was the fourth largest intra-OIC exporter but the share of intra-OIC exports in its total exports was only 7.7%. In the same year, Malaysia was the 19th largest exporter in world trade and the second largest exporter among OIC Member States after Saudi Arabia.¹¹ On this, Malaysia's traditional trading partners have been the US and the countries in South East Asia and East Asia.¹²

In term of imports, the variance was lesser where Pakistan which was the largest intra-OIC exporter also had the largest share of intra-OIC imports in its total imports (*i.e.* 39.73%). This was followed by Oman (37.36%), Iran (22.19%) and Kuwait (20.64%). Again, Malaysia which was the fourth largest intra-OIC importer and the 17th largest importer worldwide in 2005 maintained a low share of intra-OIC imports in its total imports (*i.e.* 7.48%). Like exports, the fact that Malaysia's traditional trading partner have been the US, South East Asia and East Asia.¹³

¹¹ *ibid.*

¹² In 2005, the largest country where Malaysia's exports were destined to was the US (19.7% of overall exports). This was followed by Singapore (15.4%) and Japan (8.9%). In terms of imports, Japan came first capturing 14.5% of overall Malaysia's imports. This was followed by the US (12.9%) and China (11.5%). Also note that Indonesia had the largest share among OIC Member States in terms of Malaysia's destinations of exports and its sources of imports (2.4% and 3.8%). See <http://www.miti.org>.

¹³ *ibid.*

4. The Justifications for Liberalising Intra-OIC Trade

Before delving into the discussion on whether intra-OIC trade liberalisation is justified, it is important to note that there are pros and cons of regional trading arrangements (RTAs). RTAs are the vehicles used to realise economic integration at the regional level (that includes the OIC). To the supporters of RTAs, they constitute 'a step along the way to liberalizing multilaterally'.¹⁴ An RTA is useful for it allows small countries to pool resources in facing competition in world trade from big countries.¹⁵ An RTA can also widen the markets for products originating from participating members which can contribute to increased efficiency, productivity, technological sophistication *etc.* This can be beneficial for developing countries which are on the path of industrialisation. They may utilise an RTA to prepare their nascent industries for further liberalisation and competition.¹⁶ Additionally, it can speed up the WTO trade liberalisation agenda which is easier to be worked out in smaller groups.¹⁷

However, to its opponents, an RTA is against the MFN principle of non-discrimination and can create trading blocs, trade frictions and 'rising trade barriers between blocks'.¹⁸ Regional trading arrangements can always be used to mask protectionism such as that the impact of the rule of origin in NAFTA excludes foreign inputs from being used in the manufacturing of a good.¹⁹ The same applies to the Common Agricultural Policy which has slowed free trade in Europe and beyond

¹⁴ Krueger, A. O. (1997), Problems with Overlapping Free Trade Areas in T. Ito and A. O. Krueger (eds), *Regionalism Versus Multilateral Trade Arrangements*, Univ. of Chicago Press, Chicago, p. 10.

¹⁵ Lawrence, R. and R. Litan (1990), 'The World Trading System after the Uruguay Round' 8 *Boston University International Law Journal*, 8, 247 cited in Trebilcock, M.J. and R. Howse, *The Regulation of International Trade*, Routledge, London, 3rd ed., 2005, p. 195.

¹⁶ Das, D. K. (2001), *Regional Trading Arrangements and the Global Economy: An Asia-Pacific Perspective*, Centre for International Development – Harvard, Cambridge, Mass., p. 7. Available online at <http://www2.cid.harvard.edu/cidtrade/Issues/das4.pdf>.

¹⁷ Griswold, Daniel, 'Bilateral Deals are no Threat to Global Trade', *The Financial Times*, 28 July 2003, p. 13.

¹⁸ Das, *op. cit.*

¹⁹ Krueger, *op. cit.*, pp. 15-16.

whereby the very idea of European integration was supposed to complement the WTO trade liberalisation agenda.²⁰

The legality of RTAs in the eyes of the WTO will be dealt with when the legal regime overseeing intra-OIC trade liberalisation is analysed. But it is the economic justification of RTAs that must be examined as it sheds some light on the factors which hinder the proliferation of trade between OIC Member States.

In general, RTAs should be justified only if they create trade (the term commonly used by economists is trade creation as opposed to trade diversion). In other words, they should not be encouraged if they have trade diverting effects. Most commentators²¹ quote Viner who distinguished between the trade creating and trade diverting consequences of RTAs.²² In simple terms, an RTA is trade creating if it shifts trade from a high cost non-member (of the RTA) to a low cost member. In contrast, it is trade diverting if it shifts trade from a low cost non-member to a high cost member.²³ In short, the issue whether an RTA is trade-creating or trade diverting boils down to economic efficiency and consumer welfare although the discussions on such issue may have to be reconciled with the benefit of regionalism to developing countries in terms of safeguarding the interests of their nascent industries.

The question now is whether the OIC can oversee an RTA despite the challenges facing RTAs. Many economists are concerned with the inadequacies of the RTAs in which developing countries participate.²⁴ And such inadequacies explain why many are sceptical of the feasibility of efforts to boost intra-OIC trade. They view that the size of the OIC is

²⁰ *ibid.*

²¹ See for example Trebilcock and Howse, *op. cit.*, p. 195. In the OIC context, see Ariff, M. (1998), 'Proliferation of Regional Groupings: Policy Options for the OIC', *Journal of Economic Cooperation Among Islamic Countries* 19 (1-2), 15-29, p. 24, Ruzita M. A., Zarinah H. and Norma, M.S., 'Economic Integration Among the Members of the League of Arab States: An Empirical Evidence' (2005), *Journal of Economic Cooperation Among Islamic Countries*, 26(3), 77-102, p. 77.

²² Viner, J. (1950), *The Customs Union Issue*, Carnegie Endowment for International Peace, New York.

²³ See Trebilcock and Howse, *op. cit.* Ariff, *op. cit.* and Ruzita, Zarinah and Norma, *op. cit.*

²⁴ Ariff, *op. cit.*, p. 20.

too big to become an effective RTA. The OIC region spreads across a huge geographical area which can increase transportation costs for those involved in intra-OIC trade.²⁵ However that may be an advantage if the diverse climatic conditions contribute to enriched agricultural production and trade. The ineffectiveness caused by the geographical outlook of the OIC can be overcome by 'sub-regionalisation'²⁶ which creates smaller groupings based on commonly shared criteria such as geographical affinity, level of development, nature and level of trade *etc.* However this is still subject to the economic conditions within the respective OIC Member States.

They also view that OIC Member States are at different stages of development and have variable natural endowments.²⁷ A few of them are considerably developed like Malaysia, Turkey and Indonesia but most of them are either least developed and have low national income or have high national income but are dependent on mineral fuels for export. As such, majority of OIC Member States are heavily dependent on low valued added, labour intensive and low-skilled economic activities for production and thus for export. At the same time, they import high value added products from industrialised countries. The information on the current state of intra-OIC trade provides empirical evidence supporting these suggestions.

The issue now is whether an OIC trade arrangement is trade-creating or trade-diverting. There is almost consensus among economists that intra-OIC trade at present is trade-diverting.²⁸ The transportation costs arising from the geographical spread of the OIC region explain the argument that the OIC being a 'natural trading initiative'²⁹ (*i.e.* based on comparative advantage) is questionable. This is further aggravated by the types of economic activities prevailing in OIC Member States and the resulting inadequacies of the results of such activities (*i.e.* the goods traded) and they provide further disincentives to intra-OIC trade.

²⁵ Dabour, N. M. (2004), 'Implications of Establishing An Islamic Common Market: Gradual Integration and Possible Consequences', *Journal of Economic Cooperation Among Islamic Countries*, 25(1), 71-98, p.79, Ariff, *op. cit.*, p. 23.

²⁶ Ariff, *op. cit.*, p. 27.

²⁷ Dabour, *op. cit.*, pp. 79-81, Ruzita, Zarinah and Norma, *op. cit.*, pp. 97-98, Ariff, *op. cit.*, p. 21.

²⁸ Ariff, *op. cit.*, pp. 24-25, Ruzita, Zarinah and Norma, *op. cit.*, p. 77.

²⁹ Ariff, *op. cit.*, p. 23.

It must be noted that, majority of OIC Member States still maintain high tariff and non-tariff barriers. This is clear from various reports including the IMF Trade Restrictive Index which shows that the regions where most of OIC Member States are located (namely the Middle East, North Africa, Sub-Saharan Africa and “Rest of Asia”³⁰) have higher rating of tariffs and non-tariff barriers.³¹ This indicates the possibility of OIC markets being generally costlier than the markets of more industrialised regions and if OIC products are sold within the OIC “zone”, a shift of trade from a more efficient market to a less efficient one is taking place resulting in trade diversion.

However, an intra-OIC trade arrangement can be used to gradually reduce trade restrictions among members when there is loose integration in place.³² In this way, the short-run trade diverting effects of such arrangement can be compensated by gradual reductions of trade barriers by OIC Member States. Of course, this is subject to the choice of an appropriate model of economic integration by those countries which takes into consideration the costs and benefits of liberalisation and integration.³³ Nevertheless trade liberalisation should not be the only mechanism for it must be accompanied by efforts by public and private players to diversify economic activities and boost domestic production. On this point, it is understandable that some writers prefer informal arrangements (like business-to-business arrangements) to formal

³⁰ The Rest of Asia includes Pakistan and Bangladesh but it excludes the fast-growing countries of East Asia such as Malaysia and Indonesia which have considerably industrialised and lowered their trade barriers.

³¹ The IMF Trade Restriction Index, 2000 shows that the Middle East and North Africa had the highest rating of 5.6 followed by the Rest of Asia (5.0), Sub-Saharan Africa (4.7). However, the fast-growing countries of East Asia which include Malaysia and Indonesia had a lower rating *i.e.* 3.4. In terms of average tariff, Sub-Saharan Africa had the highest rate *i.e.* at 19.2% followed by Middle East and North Africa (18.1%) and the Rest of Asia (13.8%). Also note the low rate for the fast-growing countries of East Asia (7.2%). See IMF *World Economic Outlook* (2001) as quoted in ‘Slow road to globalization’, *Business Middle East* (2002, January 16), pp. 6-7. Both are cited in Ruzita, Zarinah and Norma, *op. cit.*, p. 97.

³² Dabour, *op. cit.*, pp. 89-91.

³³ Ariff for example proposes looser integration model hence the inappropriateness of customs union for the OIC due to the different level of development and differing external economic policies (some have import-substitution policy and some have export-orientation policy. See Ariff, *op. cit.*, p. 25.

arrangements (including RTAs) as the best model for enhancing intra-OIC trade.³⁴

However, a formal mechanism for liberalising intra-OIC trade is still important. As said, most OIC Member States are still dependent on agriculture or if they have diversified economically, they are still confined to low-skill, low-technology and labour-intensive sectors. In view of the high tariff walls surrounding most OIC Member States, there is a need for a regulatory framework which can improve market access to fellow members.

4.1. Strategic and Political Considerations

The strategic and political considerations underlying the intra-OIC trade liberalisation agenda stems from the realist view of regionalism which draws upon the importance of promoting security and protecting security.³⁵ Here, the symbiotic relationships between political and economic considerations mandate the establishment of regional arrangements. These arrangements may impact greatly on developing countries. These countries are politically and economically inferior to the developed countries, and their sovereignty and security are prone to external and internal threats. As suggested by Levy and Barnett, security threats are more about 'weakness in the domestic political economy' than 'more narrowly defined and autonomously generated political threats'.³⁶ By entering into these arrangements, such threats can be minimised not only through political but also economic measures.

Likewise the same discourse may affect the OIC since one of its purposes was to liberate Al-Quds and the issue of Al-Quds has become (to some extent) a security issue to many OIC Member States particularly those in the Arab world. As noted by Dabour, the OIC

³⁴ See for example Ariff, *op. cit.*, p. 27.

³⁵ Acharya, A. (2002), Regionalism and the Emerging World Order in Breslin, S. (eds et. al.), *New Regionalism in the Global Political Economy*, Routledge, London, pp. 21-24.

³⁶ See Levy J. S. and M. M. Barnett (1992), 'Alliance Formation, Domestic Political Economy and Third World Security', *Jerusalem Journal of International Relations*, 14, 4. Also see Hout, W. (1999), 'Theories of international relations and the new regionalism' in Grugel J. and W. Hout, *Regionalism Across the North-South Divide: State Strategies and Globalization*, Routledge, London/New York, p. 15.

Charter's aim covers both original political objectives and also ultimate economic integration.³⁷ However, there is no reference in the OIC economic and commercial cooperation framework to security or sovereignty issues although the preamble to the General Agreement for Economic, Technical and Commercial Cooperation among OIC Member States espouses the desire to strengthen the bonds between Member States in *all* spheres, in order to achieve their common interests. The preamble allows us to widen the scope of integration to be undertaken by the OIC and its agencies promoting both the political and economic interests of the OIC Member States. In return, it resonates one of the realities of international relations *i.e.* economic (including trade) cooperation is not as politically sensitive as military or political cooperation. In the same way, it can attract less disagreement among Muslim countries

Of course, the possibility of finding an identity to be commonly shared by all OIC Member States is explained by the argument that the faith of Islam can be a uniting factor for the OIC. However as noted by Ariff, Muslim countries have been reluctant to increase the existing slow pace of economic integration and trade liberalisation due to the lack of political will.³⁸ This is on top of the reasons for continued pessimism in a workable Islamic economic integration. He thus suggests a less formal, less ambitious and outward looking model for such integration.³⁹

These observations show that despite the relative ease in economic integration compared to political integration, the OIC is far from ready to witness the former spearheading the latter. However, it must be remembered that the OIC integration process should be transitive where a learning curve should be permitted to all players who will draw upon the complementarities between political and economic considerations and promote the common interests of the Islamic world. Intra-OIC trade liberalisation can fit into such framework especially if its economic justifications are taken into account.

³⁷ Dabour, *op. cit.*, p. 73.

³⁸ Ariff, *op. cit.*, p. 21.

³⁹ *ibid.*, p. 27.

5. The Legal Framework for Liberalising Intra-OIC Trade

The economics of RTAs as it affects the OIC has been examined in the previous sections. Now, the paper examines the legal framework which can be utilised to liberalise intra-OIC trade. This brings us to the discussion on the legal aspects of such issue. First, it is important to define RTAs. The legal definition of RTAs is found in the GATT. But the taxonomy of RTAs must be first unravelled.

RTAs can be classified according to the degree of integration involved. They are preferential trade arrangements (PTAs), free trade areas (FTAs), customs unions (CUs), common market and economic union. PTAs are the least integrated RTAs where 'partial preference is given only to trading partners' while in FTAs, all tariffs, quantitative restrictions and non-tariff barriers are eliminated for all trading partners. FTAs on the other hand are less integrated than CUs for the latter apply a common level of trade barriers 'vis-a-vis non-members' but not free movements of factors of production which exist in a common market. Finally, the most integrated RTAs are economic unions in which national economic policies are integrated.

At the same time, the WTO rules⁴⁰ only acknowledge two forms of regional trading arrangements – customs unions and free trade areas. Article XXIV(8) of GATT defines a customs union as:

- '...the substitution of a single customs territory for two or more customs territories, so that
- (i) duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and,
 - (ii) subject to the provisions of paragraph 9, substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union'.

⁴⁰ These refer to Article XXIV of GATT which is supplemented by the Understanding on the Interpretation of Article XXIV.

The same provision defines a free trade agreement as:

‘...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.’

Both provisions above show that there are specific conditions for RTAs (FTAs and CUs namely) to be WTO-consistent including that they must not violate the Most Favoured Nation (MFN) principle which prohibits discrimination between one country and another.

5.1. The Pathology of the Framework Agreement on TPS-OIC

The Framework Agreement on TPS-OIC (hereinafter referred to as the TPS-OIC Agreement or the Agreement) was adopted by the COMCEC in 1990. By virtue of the Agreement, a trade preferential system (the TPS-OIC) was created. Such system aims to promote trade between OIC Member States through reductions of various tariff and non-tariff forms of trade barriers.⁴¹ These (the reductions) are carried out by the granting of trade (primarily tariff)⁴² concessions which are to be negotiated among the participating OIC Members and later embodied in the schedules of concessions which are part of the TPS-OIC Agreement. There are rules in the Agreement on the negotiations of such concessions⁴³ as well as their modifications and withdrawals.⁴⁴ Trade concessions are the result of a State’s commitment to reduce its tariffs (or other trade barriers) on the products from another State in return for the reduction of the other State’s tariffs on its own product.

The granting of trade concessions by and to the participating OIC Members will be based on the Most Favoured Nation (MFN) rule where any trade concession by one participating Member to another

⁴¹ It must be noted that the term para-tariffs is used in the Agreement on TPS-OIC. Unlike tariffs and non-tariff barriers, such term which refers to border charges and fees other than tariffs is not commonplace within the WTO literature.

⁴² This is due to the mention of para-tariff and non-tariff concessions alongside the tariff ones even though most concessions negotiated among trading partners are about tariffs.

⁴³ See Articles 4 and 5 of the Agreement on TPS-OIC.

⁴⁴ See Article 8 of the Agreement on TPS-OIC.

participating Member must be extended to the rest.⁴⁵ The Agreement also prohibits the use of tariff, para-tariff and non-tariff barriers impairing or nullifying any concessions granted unless they correspond to internal taxes on similar products.⁴⁶ This indicates the invocation of another WTO non-discrimination principle in the TPS-OIC Agreement – the national treatment rule.

Yet the same provision which embodies the national treatment rule provides another exception to the prohibition of impairing or nullifying concessions – anti-dumping and countervailing measures. This is despite the inclusion of non-tariff barriers in the types of trade restrictions covered by the TPS-OIC regime.⁴⁷ However, the TPS-OIC Agreement has a specific provision on safeguard measures which are also non-tariff barriers and interestingly takes a different approach from the WTO safeguards regime. Unlike the WTO safeguards regime, which merely alludes to surge in imports causing serious injury to domestic producers as a precondition for the corresponding trade-restrictive measures,⁴⁸ the TPS-OIC safeguards provision goes further in characterizing such trade condition (surge in imports) as including serious deterioration in the balance of payments, dumping and even export subsidies.⁴⁹

There are no provisions on technical barriers to trade (TBT) and sanitary and phytosanitary measures (SPS). However, there are provisions on rules of origin, special treatment for least developed Member States (LDCs) and dispute settlement.⁵⁰

The TPS-OIC Agreement is supplemented by the Protocol on the Preferential Tariff Scheme for TPS-OIC (PRETAS). The PRETAS provides the rules to be followed by participating OIC Members in their tariff-reducing commitments and in removing para-tariffs and non-tariff barriers.

⁴⁵ See Article 6 and Article 2(3) of the Agreement on TPS-OIC.

⁴⁶ See Article 7.

⁴⁷ Compare Article 7 with Article 3.

⁴⁸ See Article XIX of GATT 1994 and the WTO Agreement on Safeguards.

⁴⁹ See Article 10 of the TPS-OIC Agreement.

⁵⁰ See Articles 9, 11 and Chapter VI of the TPS-OIC Agreement respectively.

One must remember that in relation to tariff reduction, the PRETAS only requires tariffs to be reduced between the range of 10% and 25%.⁵¹ Moreover, the reductions only cover 7% of each participating Member's total Harmonized System (HS) lines.⁵² For Members with 90% of such lines at between 0% and 10% tariffs, their required coverage of reductions is only 1% of their total HS lines.⁵³ At the same time, it is possible for participating Members to further deepen their concessions on voluntary basis through the fast track tariff reduction scheme.

In relation to para-tariffs, the commitments undertaken by participating Members are in the form of the removal of such measures either upon entry into force of the PRETAS or within 3 years therefrom for LDCs. No new para-tariffs can be introduced.⁵⁴ The same rules apply to non-tariff barriers.⁵⁵ However the PRETAS adopts a non-intrusive approach to anti-dumping and countervailing measures in the sense that both measures can be used by participating Members according to the rules of WTO regime.⁵⁶ As regards safeguard measures, the PRETAS lays down (simple) procedures to be followed before such measures can be imposed. Like the TPC-OIC Agreement, the PRETAS is silent on TBT and SPS.

The position of the PRETAS (and the TPS-OIC Agreement) on these measures can confuse what is envisaged by both instruments (the PRETAS and TPS-OIC Agreement) regarding the need for participating Members to reduce their non-tariff barriers. It is a common usage that non-tariff barriers refer to anti-dumping, countervailing, safeguard, TBT and SPS measures.⁵⁷ Even so, there is a broad definition for the term 'non-tariff barriers' in the TPS-OIC Agreement and PRETAS. Both define non-tariffs as 'any measure, regulation, or practice, other than

⁵¹ See Article 3 of the PRETAS.

⁵² The HS is a system harmonizing tariff nomenclatures which are explained a code system. A tariff line on the other hand refers to a product characterized such system. See Das, B.L. (1999), *The World Trade Organization – A Guide to the Framework for International Trade*, Zed Book Ltd, New York, p. 57. Also see www.wto.org.

⁵³ See Article 3 of the PRETAS.

⁵⁴ See Article 6 of the PRETAS.

⁵⁵ See Article 7 of the PRETAS.

⁵⁶ See Article 8 of the PRETAS.

⁵⁷ See for example the usage by Mavroidis, P.C. (2005), *The General Agreement on Tariffs and Trade – A Commentary*, Oxford Univ. Press, Oxford, p. 8; Das, *op. cit.*, p. 5 and Trebilcock and Howse, *op. cit.*, p. 24-25.

tariffs and para-tariffs'.⁵⁸ It may thus be argued that though all three types of trade barriers are mentioned, the TPS-OIC regime only concentrates on tariff reduction.

Finally some aspects of the TPS-OIC Agreement and the PRETAS may be construed beyond the principle of economic efficiency. Such principle draws upon what is Pareto-optimal and is associated with objectives like maximisation of consumer welfare, the pursuit of free market and competition, the attainment of comparative advantage *etc.* In its preamble, the TPS-OIC Agreement clearly mentions 'development', 'optimal use of resources' and the improvement of 'the standard of living of peoples' as something to be achieved through such agreement. The preamble also makes reference to the special needs of the least developed Member States of the OIC and is supported by Article 11 of the Agreement requiring special concessions to be extended the least developed Member States in bilateral or multilateral negotiations. This reference is reflected in various provisions of the PRETAS which afford special and differential treatment to the least developed Member States in terms of tariff and non-tariff reductions.⁵⁹ However, the realisation of the non-efficiency objectives other than the provision of special and differential treatment to LDCs is still not found within the TPS-OIC Agreement and PRETAS.

5.2. The TPS-OIC Regime as a WTO-Consistent RTA

Based on the analysis of the TPS-OIC regime in the previous section, it is clear that such regime takes the form of preferential trade arrangement (PTA) which is the least integrated category of RTAs. This is explained by the fact that the TPS-OIC regime requires partial elimination of trade barriers *i.e.* tariffs. It does not require elimination of all tariffs and non-tariff barriers. Regarding tariffs, as discussed above, there are very limited thresholds for tariff reduction commitments to be undertaken by Member States both in terms of the rate of reduction and the goods subject to it. Regarding non-tariff barriers, the TPS-OIC regime does not cover anti-dumping and countervailing measures, TBT and SPS.

The issue now is whether the TPS-OIC regime falls within the ambit of the WTO rules regulating RTAs (including Article XXIV of GATT

⁵⁸ See Article 1 of the TPS-OIC Agreement and Article 1

⁵⁹ See, for example, Article 4(2) (regarding tariff reduction), Article 6 (regarding removal of para-tariffs) and Article 7 (regarding elimination of non-tariff barriers).

1947). As stated in the previous section, such rules only acknowledge two types of RTAs – FTA and CU. Does this mean that the TPS-OIC regime which seems not to fulfil the criteria of either of them is subject to the application of such rules? An observation of the relevant literature suggests that the distinctions between PTAs and FTAs have been blurred as far as the application of the WTO rules on RTAs. As a result, commentators tend to extend the applicability of the rules regulating FTAs to PTAs though they acknowledge the existence of the term PTA.⁶⁰

Applying the analysis to the TPS-OIC regime, it is clear that the provisions of Article XXIV which govern FTAs are applicable to such regime. Alternatively, one may argue that the regime is an 'interim agreement necessary for the formation of a free trade area', which is also mentioned in and regulated by Article XXIV. The TPS-OIC regime may also attract the application of the Enabling Clause which allows RTAs to be formed among less developed countries for mutual reduction of tariffs.⁶¹

Within the WTO system, the RTAs are an exception to the non-discrimination principle particularly the MFN rule. However, there are rules stipulated in both Article XXIV and the Enabling Clause. To borrow from Krueger, they require FTAs (and interim agreements) to create trade preferences to member countries which are '(1) 100 percent, (2) cover substantially all trade, (3) do not raise protection against third countries, and (4) have a definite timetable for implementation.'⁶² Looking at these propositions, the rules are clear that any FTA (including the TPS-OIC) must complement the WTO system so that the incentives that they provide should not lead to higher trade barriers which can impair or nullify the rights available to any WTO Member arising from the WTO agreements. However, as noted by Krueger, to implement them is not easy so that to find any RTA (especially the one

⁶⁰ See Trebilcock and Howse, *op. cit.*, pp. 196-200, Krueger, *op. cit.*, pp. 10-14 (note that Krueger uses the term PTA in the same way as RTA giving the former a rather general meaning).

⁶¹ It must be noted that the Enabling Clause is a general provision which allows special and differential treatment to less developed countries as an exception to the principle of non-discrimination in Article I of GATT 1947.

⁶² Krueger, *op. cit.*, p. 13.

which involves the US or EU) in contravention of the rules is also difficult.⁶³

The concern may not be an increase in trade barriers. States may join RTAs to reduce such barriers beyond what has been undertaken within the WTO. To non-members, this creates a disadvantage to them unless they join other RTAs for the same reason. In the end, the proliferation of such exercises may lead to the lowering of tariffs world-wide.

As far as the TPS-OIC regime is concerned, there is clear reference in both the TPS-OIC Agreement that its application is subject to the MFN principle. However, whether the entry into the Agreement (as well as PRETAS) can lead to the lowering of tariffs as among the OIC Member States remains to be seen. As will be seen below, the enforcement of the TPS-OIC legal instruments has been slow. Second, the extent and rate of tariff reductions within such regime are lower than other RTAs. This reflects the shallow integration underlying the TPS-OIC regime although the OIC 'region' is among those with the highest trade barriers in the world.

5.3. The Enforcement of the TPS-OIC Regime

It must be noted that the TPS-OIC regime does not bind each and every OIC Member States. This is because many OIC Members (including the important ones) have not signed and ratified not only the PRETAS but also the TPS-OIC Agreement. The membership of both agreements is illustrated by the table below.

Table 5 indicates that as of October 2007, 30 out of 57 OIC Member States have signed the TPS-OIC Agreement. In other words, only 53% of the Member States participated in intra-OIC trade liberalisation efforts. The non-participating States are Afghanistan, Albania, Algeria, Azerbaijan, Benin, Brunei, Comoros, Ivory Coast, Djibouti, Gabon, Guinea-Bissau, Guyana, Kazakhstan, Kyrgyz Republic, Maldives, Mali, Mauritania, Mauritius, Mozambique, Niger, Sierra Leone, Somalia, Suriname, Tajikistan, Togo, Turkmenistan, Uzbekistan and Yemen. In terms of regional distribution, non-participation is highest in Sub-Saharan Africa and Central Asia. But this does not mean that economic regionalism is alien to such regions due to the existence of various

⁶³ *ibid.*, p. 14.

regional arrangements covering such regions (including the Economic Community of West African States (ECOWAS) for Sub-Saharan Africa and the Economic Cooperation Organization (ECO) for Central Asia). Perhaps, deeper analysis on the limited participation in such regions is necessary but due to time and space constraints, it falls outside the scope of this research.

Table 5 - OIC Members which Have Signed and/or Ratified the TPS-OIC Agreement and PRETAS (as of October 2007)

Name of Member States	TPS-OIC		PRETAS	
	Signed	Ratified	Signed	Ratified
Bahrain	X			
Bangladesh	X	X	X	
Burkina Faso	X			
Cameroon	X	X	X	
Egypt	X	X	X	
Gambia	X			
Guinea	X	X		
Indonesia	X			
Iran	X	X		
Iraq	X			
Jordan	X	X	X	X
Kuwait	X			
Lebanon	X	X		
Libya	X	X		
Malaysia	X	X	X	X
Maldives		X		
Morocco	X	X		
Nigeria	X			
Oman	X	X		
Pakistan	X	X	X	
Palestine	X			
Qatar	X	X		
Saudi Arabia	X			
Senegal	X	X		
Sudan	X			
Syria	X	X	X	
Chad	X			
Tunisia	X	X	X	
Turkey	X	X	X	
UAE	X	X	X	
Uganda	X	X		

Source: ICDT Report on Trade among OIC Member States (2007)

Table 5 also shows that only 20 OIC Member States have ratified the TPS-OIC Agreement making the Agreement binding on only 35% of the OIC Member States. Ratification is a more persuasive indicator to inform the enforcement of the TPS-OIC regime as being a signatory does not make a participating Member State bound by the relevant treaty unless the State ratifies such treaty. The Member States which have not ratified the TPS-OIC Agreement include Bahrain, Burkina Faso, Gambia, Indonesia, Iraq, Kuwait, Nigeria, Palestine, Saudi Arabia, Sudan and Chad. It is worth noting that some of these countries (on top of those which have not signed the TPS-OIC Agreement) are big players in intra-OIC trade. They are Indonesia (holding 6.21% of intra-OIC total exports and 6.83% of intra-OIC total imports in 2005⁶⁴), Kuwait (holding 3.74% of intra-OIC total exports and 1.53% of intra-OIC imports) and Nigeria (holding 2.61% of intra-OIC total exports and 2.36% of intra-OIC total imports). More importantly, the biggest intra-OIC exporter *i.e.* Saudi Arabia whose intra-OIC exports accounted for 22.66% of intra-OIC total exports has also not ratified thus not bound by the TPS-OIC Agreement.

The participation of the OIC Member States in the PRETAS is even poorer. Table 5 reveals that only 10 OIC Member States (17.5% of total OIC Member States) have signed the PRETAS. These countries are Bangladesh, Cameroon, Egypt, Malaysia, Pakistan, Jordan, Syria, Tunisia, Turkey and the UAE. Yet only 2 of them (Malaysia and Jordan) have ratified the PRETAS. Notably, 4 of the countries which have signed the PRETAS are main intra-OIC trading partners (*i.e.* Malaysia, Pakistan, Turkey and the UAE). Regarding the countries which have ratified the PRETAS, only Malaysia can be considered to be a main intra-OIC trading partner.

In short, the enforcement the TPS-OIC regime is constrained by low level of ratifications of the two main legal instruments of such regime – the TPS-OIC Agreement and the PRETAS. The situation regarding the latter is even more discouraging whereby only 2 Member States have ratified it. This means that the TPS-OIC regime is binding and enforceable on only those States as it is the PRETAS which enforces the TPS-OIC Agreement. Such enforcement is also constrained by the limited participation of major players of intra-OIC trade. And this is

⁶⁴ All subsequent figures denoting the shares of the OIC Member States in intra-OIC total trade are as of 2005.

most visible when one considers that Saudi Arabia which was the biggest intra-OIC exporter⁶⁵ has not signed the TPS-OIC Agreement (as of October 2007).

6. Conclusion

The discussions above show that efforts have been taken to establish a regional trade arrangement at the OIC level which is known as the TPS-OIC regime. At the same time intra-OIC trade is fast-growing although its volume is still low. This increases the importance of the liberalisation of such trade which is supported by strong strategic and political justifications. However, there is a concern that the process of integrating the OIC region through the TPS-OIC regime may trump the trade liberalisation agenda of the WTO by diverting trade from more efficient markets to the less efficient ones. Thus suggestions were made that the OIC should adopt a shallow integration approach which does not create a closed OIC economic region. At the moment the legal framework which promotes intra-OIC trade liberalisation (the TPS-OIC regime) operates along this line. But as mentioned in this paper, the conditions leading to the structure of trade in most OIC Member States reflect a less advanced structure. Thus it is proposed that the concern of trade diversion arising from the TPS-OIC regime must be reconciled with the need to smoothen trade between many OIC Member States which are less developed and still maintain high trade barriers. This requires the enforcement of the regime to be more aggressive and comprehensive. Of course the TPS-OIC regime is not the only solution. The OIC Member States may sub-regionalise and establish bilateral and plurilateral trade arrangements. In the end, intra-OIC trade liberalisation will not be an end in itself. It will complement other programs which strive to strengthen the political, economic and social well being of the Muslim ummah.

⁶⁵ This was in 2005.

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