UNCTAD/ITCD/TAB/31

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT
Geneva

SMOKE AND MIRRORS: MAKING SENSE OF THE WTO INDUSTRIAL TARIFF NEGOTIATIONS

POLICY ISSUES IN INTERNATIONAL TRADE AND COMMODITIES
Study Series No. 30

3. The state of play in the WTO negotiations

UNITED NATIONS
New York and Geneva, 2006

Bank trade reform programmes. The explanation is related to the responsiveness (elasticity) of imports to tariff changes.

- A reduction in rates may reduce evasion (smuggling) to a significant degree. If tariffs fall, it may no longer be worthwhile evading normal trade procedures.

The conclusion is that while reductions in government revenues are a concern for developing countries in particular and even more so for some countries heavily dependent on this source, there are compensating factors that can partially or in some cases completely offset the revenue reductions for some level of reform. On the other hand, complete tariff elimination necessarily implies the elimination of the tariff revenue source. The main issues then are the speed and cost of implementing new tax laws and the associated changes in fiscal administration.

3. THE STATE OF PLAY IN THE WTO NEGOTIATIONS

Historically, there has been relatively little discussion during trade negotiations of the adjustment process and the fiscal effects of tariff liberalization, in part because, prior to the Uruguay Round, few demands were made on developing countries. However, the Uruguay Round saw increased active participation in the negotiations by the developing countries as demandeurs, and they were also asked to make substantial contributions. To some extent, the developing countries felt that they had not made much progress in opening up markets for their key exports by simply relying on special and differential treatment. In addition, they had also been making considerable strides towards the liberalization of their own economies, usually under World Bank/IMF lending programmes, and they felt that there was an opportunity to "cash in" on these reforms by active participation in the negotiations. On the other hand, the developed countries started to take a tougher line on seeking developing country reforms, both because they felt that this was good for the developing countries and because they saw that some developing countries were emerging as important markets.

In the aftermath of the Uruguay Round, developing countries began again to question the value of the efforts they had been making on trade reform. They felt that they had not benefited from the promises of big trade and welfare gains from the Uruguay Round, while they were taking on increasing and costly commitments. Moreover, in the wake of the economic crises of 1997-1998, many developing countries suffered serious setbacks with falling output and rising unemployment – even "de-industrialization" - some of which was attributed to the trade reforms. In addition, economists such as Rodrik and Stiglitz started to challenge the linkage between trade openness and economic growth, emphasizing institutional factors as a key to development.

Accordingly, in the current WTO negotiations, which are supposed to have a strong development component, the accumulation of disillusion and concern has led developing countries right from the start to seek some leeway or policy space regarding any new commitments that they may be required to undertake.

The WTO's Cancún Ministerial Conference was unsuccessful in finding consensus on non-agricultural market access, although the lack of success may have reflected other issues that are cross-linked through the "single undertaking" ("nothing is agreed until all is agreed"). Despite the intensive negotiations in the two years following Doha and the various proposals on the negotiating table, no agreement was achieved in Cancún on the modality or formula to be used for tariff reductions. Developed countries generally considered that there was not sufficient ambition in the proposed draft presented in Cancún and developing countries believed that it did not sufficiently reflect their interests and concerns. Nonetheless, had the Singapore issues and agriculture been resolved, it seems unlikely that non-agricultural market access would have been a stumbling block.

The state of the non-agriculture market access negotiations is largely unchanged since before Cancún, with the main focus still on finding a tariff-cutting formula that is acceptable to both developed and developing countries. Essentially, Doha requires Member States to reduce tariffs, especially those facing developing countries' exports; however, it also mandates less than full reciprocity from developing countries.

The Cancún Ministerial draft text on non-agricultural products was based on that of the Chairman of the Negotiating Group on Market Access: Revised Draft Elements of Modalities (TN/MA/W/35/Rev.1). The Chairman's text proposed a tariff reduction scheme similar to the "Swiss"/harmonizing formula with the maximum coefficient being a function of each country's national average tariff.[6] He also identifies seven sectors for complete liberalization: electronics and electrical goods; fish and fish products; footwear; leather goods; motor vehicle parts and components; stones, gems and precious metals; and textiles and clothing.

The United States, the European Union and Canada, in a joint contribution during the summer of 2003, prior to Cancún, had argued for a "single" harmonizing formula rather than a country-based average tariff reduction formula in order to achieve a real expansion of market access. They also proposed a provision that there would be an increase in the single coefficient as a result of members fully binding their tariffs and participating meaningfully through reductions in their binding overhang that effectively enhance market access.

Whereas the Chairman's text envisages exempting LDCs from tariff reduction commitments, the joint United States, European Union and Canada text proposes that additional provisions be included for LDCs as well as those members with a binding coverage of non-agricultural productcs of less than 35 per cent of their tariff universe. These members would be exempted from making tariff reductions arising from the application of the formula, and, with the exception of LDCs, would be expected to bind 100 per cent of non-agricultural tariff lines at the overall level of the average bound tariffs of all developing countries after full implementation of current concessions.

The draft Cancún Ministerial text proposes a non-linear formula applied on a line-by-line basis. With reference to other issues, such as sectoral tariff elimination and increasing binding coverage, the draft contains proposals similar to those presented by the Chairman of the Non-agricultural Market Access Negotiating Group.

The Hong Kong, China, Ministerial Conference in December 2005 confirmed an approach based on the so-called "July Package" adopted by the General Council of WTO in August 2004 (referred to as the

[6] The Swiss formula cuts high tariffs more dramatically. This represents a problem for developing countries that tend to have higher initial tariffs and would therefore be required to make larger cuts under a harmonizing formula. The proposal attempts to addresses this concern by raising the Swiss formula maximum coefficient according to the average tariff. This provides for the "less than full reciprocity" to the extent that developing countries have higher initial tariffs, but countries with the same average tariffs are treated in the same fashion, irrespective of whether they are developed or developing.

"NAMA Framework" in the Hong Kong, China, Ministerial Declaration). In practice the "July Package" of 2004 set the stage for the end-game in the NAMA negotiations. From that point, discussion became more focused on variations in the "Swiss" formula of the earlier Tokyo Round, by which a pre-selected coefficient would establish a maximum rate, while reducing higher rates by a greater proportion than lower rates. An alternative proposal[7] sets the coefficient at the national average (or a multiple thereof). Other proposals are based on the idea of a "Simple Swiss" formula, with one coefficient for developed countries and another, higher coefficient for developing countries. Some variations would depend on the use of other flexibilities, e.g. on binding. Consensus on participation in sectoral elimination was still lacking, awaiting a decision in the formula. The provisions for special and differential treatment for developing countries also needed further refinement. No transition period had been agreed for implementation of the Agreement. On a more detailed level, several key questions remained, such as whether trade-weighted or simplae average tariffs should be used for binding rate calculations.

4. EXISTING LEVELS OF PROTECTION

Tariffs cuts for non-agricultural products in the Uruguay Round were comparable in scope and depth to those achieved in the earlier Tokyo and Kennedy Rounds, and there was the most important agreement to phase out restrictions on trade in textiles and clothing under the Multifibre Arrangement by the end of 2004 (but where the main liberalization was "back loaded" to the end of the implementation period). The agreed approach required developed countries to reduce their bound tariffs by one third and developing countries by one fourth, and this was to be achieved by "request and offer", that is line-by-line negotiations between all possible combinations of interested trading partners. In the end, both developing and developed countries cut around 30 per cent of their tariff lines (Finger and Schuknecht, 1999). Not only did developing countries make deeper absolute cuts than developed countries because they were starting from a higher base, but also the depth of industrial tariff cuts is higher even in percentage terms.[8] Although it had been proposed that developing countries be granted recognition for the recent unilateral liberalization, it was made clear that this would have to be bound, and there is no explicit on-the-record evidence of such treatment being granted.

Emerging from the Uruguay Round the result was the continued disproportionate bias in protection against developing country exports through tariff peaks and escalation (UNCTAD, 2003). Tariff rates remained dispersed and a number of very high rates, tariff peaks, emerged especially among developed countries.[9] The importance of tariff peaks on products of interest to developing countries still remains a priority in the multilateral trade agenda. Nearly 10 per cent of developed country tariff lines are in excess of three times the national average (table 3).

[7] Proposal by Argentina, Brazil and India, based on an earlier draft by the Swiss Chairman of the Negotiating Group on Market Access, Ambassador Pierre-Louis Girard, also known as the "Girard" proposal, TN/MA/W/35/Rev.1.

[8] The Finger and Schuknecht (1999) study shows that the depth of industrial tariff cuts (dT/(1+T)) was 1 percentage point for developed countries and 2.7 percentage points for developing countries.

[9] There is no unique definition of a high tariff or tariff peak. It is usually understood that a domestic or national tariff peak is a tariff line three times higher than the national average. International tariff peaks are the tariff lines more than 15 per cent above the international average.