

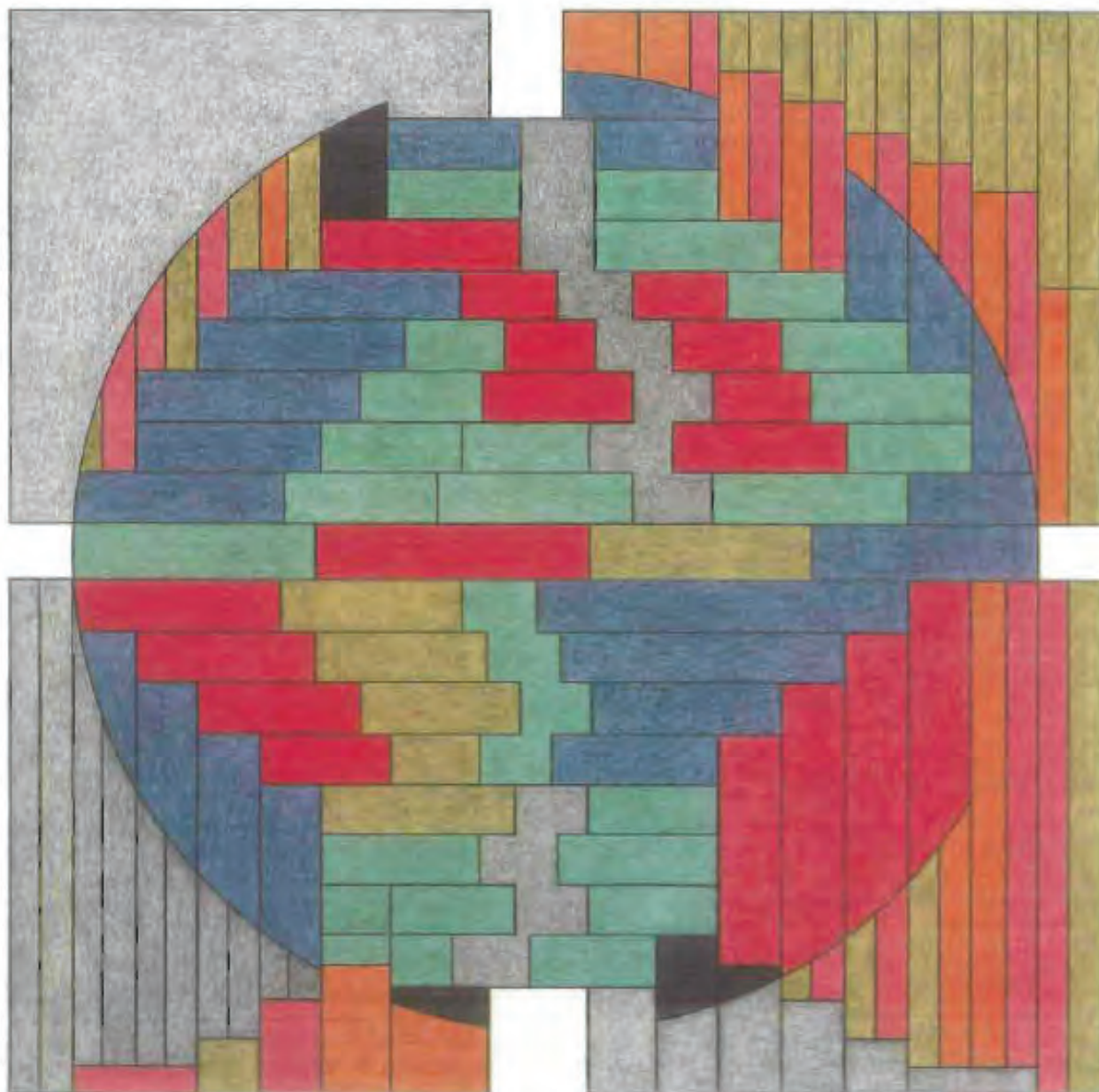
**THE OUTCOME OF THE URUGUAY ROUND:  
AN INITIAL ASSESSMENT**  
**SUPPORTING PAPERS**  
TO THE TRADE AND DEVELOPMENT  
REPORT, 1994



UNITED NATIONS

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UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT  
Geneva

# THE OUTCOME OF THE URUGUAY ROUND: AN INITIAL ASSESSMENT

## **SUPPORTING PAPERS** TO THE TRADE AND DEVELOPMENT REPORT, 1994

Report by the secretariat of  
the United Nations Conference on Trade and Development



UNITED NATIONS  
New York, 1994

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## Explanatory notes

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### Classification by country or commodity group

The classification of countries used in this Report generally follows that of the UNCTAD *Handbook of International Trade and Development Statistics 1993*.<sup>1</sup> It has been adopted solely for the purposes of statistical or analytical convenience and does not necessarily imply any judgement concerning the stage of development of a particular country or area.

The term "country" refers, as appropriate, also to territories or areas.

Generally speaking, sub-groupings within geographical regions and analytical groupings (e.g. Least developed countries (LDCs)) are those used in the UNCTAD *Handbook of International Trade and Development Statistics 1993*. References to "Latin America" in the text or tables include the Caribbean countries unless otherwise indicated. Designations of customs territories departing from general United Nations practice are used where required by the particular context (i.e. GATT instruments and bodies).

The terms "economies in transition" (or similar terminology) and "Central and Eastern Europe" refer to Albania, Bulgaria, the Czech Republic, Hungary, Poland, Romania, Slovakia and the former USSR (comprising the Baltic republics and the Commonwealth of Independent States (CIS)).

### Other notes

References in the text to *TDR* are to the *Trade and Development Report* (of a particular year). For example, *TDR 1993* refers to *Trade and Development Report, 1993* (United Nations publication, Sales No. E.93.II.D.10).

The term dollar (\$) refers to United States dollars, unless otherwise stated.

The term 'billion' signifies 1,000 million and 'trillion' 1,000 billion.

The term 'tons' refers to metric tons.

Annual rates of growth and change refer to compound rates.

Exports are valued f.o.b. and imports c.i.f., unless otherwise specified.

Use of a hyphen (-) between dates representing years, e.g. 1988-1990, signifies the full period involved, including the initial and final years.

An oblique stroke (/) between two years, e.g. 1990/91, signifies a fiscal or crop year.

Two dots (..) indicate that the data are not available, or are not separately reported.

A dash (-) indicates that the amount is nil or negligible.

A plus sign (+) before a figure indicates an increase; a minus sign (-) before a figure indicates a decrease.

Details and percentages do not necessarily add up to totals, owing to rounding.

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<sup>1</sup> United Nations publication, Sales No. E/F.94.II.D.24.

## Abbreviations

AMS	Aggregate Measurement of Support
BIS	Bank for International Settlements
CEFTA	Central European Free Trade Area
CIS	Commonwealth of Independent States
c.i.f.	cost, insurance and freight
DC	developing country
DMEC	developed market-economy country
DSB	Dispute Settlement Body (of the WTO)
DSU	Dispute Settlement Understanding (of the WTO)
EC	European Community (or Communities)
ECOWAS	Economic Community of West African States
ECU	European Currency Unit
EEA	European Economic Area
EEC	European Economic Community
EFTA	European Free Trade Association
EU	European Union
FA	Final Act
FDI	foreign direct investment
FIRA	(Administration of the) Foreign Investment Review Act (Canada)
f.o.b.	free on board
FOGS	Functioning of the GATT System
FTA	North American Free Trade Area (Canada-United States)
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNG	Group of Negotiations on Goods (of the Uruguay Round)
GNP	gross national product
GNS	Group of Negotiations on Services (of the Uruguay Round)
GSP	Generalized System of Preferences
HS	Harmonized Commodity Description and Coding System (Harmonized System)
ICAO	International Civil Aviation Organization
ILO	International Labour Organisation
IMF	International Monetary Fund
IPR	intellectual property right
ISO	International Organization for Standardization
ITCB	International Textiles and Clothing Bureau
ITO	International Trade Organization
ITU	International Telecommunication Union
LDC	least developed country
MFA	Multi-Fibre Arrangement
MFN	most favoured nation
MTA	multilateral trade agreement
MTN	multilateral trade negotiations
MTO	Multilateral Trade Organization
NAFTA	North American Free Trade Agreement (Canada-United States-Mexico)

<b>NGTC</b>	Negotiating Group on Textiles and Clothing (of the Uruguay Round)
<b>NICs</b>	newly industrializing countries
<b>NTB</b>	non-tariff barrier
<b>ODA</b>	official development assistance
<b>OECD</b>	Organisation for Economic Co-operation and Development
<b>OMA</b>	orderly marketing arrangement
<b>PGE</b>	permanent group of experts
<b>PPP</b>	Polluter Pays Principle
<b>PPP</b>	Product, Process and Production (method)
<b>PTA</b>	plurilateral trade agreement
<b>OEM</b>	original equipment manufacture
<b>R&amp;D</b>	research and development
<b>RBP</b>	restrictive business practice
<b>SCM</b>	subsidies and countervailing measures
<b>SDR</b>	Special Drawing Right
<b>SGA</b>	selling, general and administrative (expenses)
<b>SELA</b>	Sistema Economico Latinoamericano (Latin American Economic System)
<b>SITC</b>	Standard International Trade Classification
<b>TBT</b>	Technical Barriers to Trade (Agreement on)
<b>TMB</b>	Textiles Monitoring Body
<b>TNC</b>	Trade Negotiations Committee (of the Uruguay Round)
<b>TNCs</b>	transnational corporations
<b>TPRM</b>	Trade Policy Review Mechanism (of the WTO)
<b>TRIMs</b>	trade-related investment measures
<b>TRIPs</b>	trade-related intellectual property rights
<b>UNCTAD</b>	United Nations Conference on Trade and Development
<b>UNDP</b>	United Nations Development Programme
<b>USITC</b>	United States International Trade Commission
<b>VER</b>	voluntary export restraint
<b>VRA</b>	voluntary restraint arrangement
<b>WIPO</b>	World Intellectual Property Organization
<b>WTO</b>	World Trade Organization

The Supporting Papers in this Supplement to the Trade and Development Report, 1994, complement the Initial Assessment of the Outcome of the Uruguay Round, which is intended to assist the Trade and Development Board in conducting its assessment of the multilateral trade negotiations as provided for in paragraph 144 of the Cartagena Commitment. These papers attempt to provide a clearer understanding of the main features of the Final Act Embodying the Results of the Uruguay Round, and to set out the parameters of the comprehensive analysis and assessment of the outcome of the Round that will be undertaken once the market access results can be quantitatively analysed. The analysis in these papers is based on the text of the Uruguay Round Agreements and their negotiating history. The full implications of the impact of the agreements will become more evident, however, in the light of experience with their implementation and through cases brought to dispute settlement. The papers also provide the basis for the identification of the problems and opportunities facing developing countries and countries in transition to a market economy in increasing their participation in international trade in goods and services in the 1990s.

These Supporting Papers concentrate on selected areas of particular interest in the Final Act, examining, *inter alia*, the following results of the Round which effectively place all countries at broadly comparable levels of obligation: (i) the strengthening of the existing disciplines which now establish much more detailed rules to govern a variety of trade policy measures, particularly those areas where weak or unclear disciplines had consistently been a source of trade tensions and the subject of trade disputes; (ii) the achievement of a substantial degree of tariff liberalization so as to maintain the momentum towards ever freer multilateral trade; (iii) the establishment of new multilateral trade rules to cover intellectual property and trade in services; and (iv) the interlinkage of all these agreements within the institutional framework of the newly established World Trade Organization (WTO) subject to an integrated dispute settlement mechanism. The papers study the impact of the Uruguay Round on the international trading system against the back-drop of long-run trends in the system, as

reflected in the efforts of individual countries and country groupings to amend the system so as to accommodate their national interests; the extension and proliferation of regional trade and economic integration agreements; the increasing recourse to bilateral and unilateral actions to solve trade problems; and the reduction in the scope of policy options. The liberalization of international trade as a result of the Round should help to stimulate global economic expansion in the 1990s, which is a prerequisite for alleviating unemployment problems in the North and facilitating economic adjustment, growth and development in the South.

Although the idea of the WTO was not foreseen in the Punta del Este Declaration which launched the Uruguay Round of multilateral trade negotiations in 1986, it was presented by its main proponents as a necessary means for implementing the results of the Round within a common institutional framework, as well as for imposing stronger discipline on unilateral trade measures, notably those taken by the United States. Chapter I of the Supporting Papers examines the Agreement Establishing the World Trade Organization, to which all substantive agreements and understandings as well as the Ministerial Decisions and Declarations are annexed, and which therefore embodies the single undertaking envisioned at Punta del Este and reaffirms multilateralism in international trade relations. The WTO provides the common institutional framework for the conduct of trade relations among its members in matters related to the agreements contained in the Final Act. As the Agreement is confined to institutional and procedural aspects, the role of the WTO is consequently more restricted than the role contemplated in the Havana Charter of 1948 for the proposed International Trade Organization, which encompassed all issues in the area of trade including employment and development. The functions of the WTO are to facilitate the implementation, administration and operation of the Uruguay Round agreements; to provide the forum for negotiations among members concerning matters dealt with in these agreements, as well as a forum for further negotiations among them; and to administer the integrated dispute settlement mechanism linking rights and obligations in trade in goods with

those in services and intellectual property rights, through trade sanctions. Chapter I will also briefly touch on the problems faced by countries that were not contracting parties to GATT 1947, the impact of the WTO on regional agreements, and differential and more favourable treatment in favour of developing countries as provided for by various agreements under the Final Act.

The crucial accomplishment of the Uruguay Round has been to address those areas where the absence of international consensus and workable rules and procedures had frequently given rise to trade tensions and to disputes that threatened to erode the multilateral system. The most important results in this context were the respective Agreements on Safeguards, Subsidies and Countervailing Measures, Anti-Dumping, Agriculture, and Textiles and Clothing.

The cumulative effect of the rules embodied in these agreements on the functioning of the multilateral trading system will largely determine whether the new system is indeed "rule-based", and whether the multilateral trading community will choose to implement the rules in the interest of open and free trade or use them as protectionist devices. In sharp contrast to the past, when the developing countries regarded themselves as victims of such instruments, many of these countries have already become aware of the need to develop national administering infrastructures so as to be able to deploy such remedies against unfair trade practices. The use of these instruments has become all the more important as developing countries themselves have reduced the overall incidence of their tariffs. The full implications of the rules, however, will become evident only with practical application and the development of jurisprudence, under both national implementing legislation and international procedures, including discussions in the WTO administering bodies, and the use of the dispute settlement mechanism. These issues are addressed in chapters II to VI.

Chapter II focuses on the Agreement on Safeguards, which contains detailed rules to ensure that members of GATT make proper use of Article XIX safeguard actions to put an end to the proliferation of "grey area" measures, e.g. voluntary export restraints, orderly

marketing arrangements and price monitoring, which have been threatening the credibility of multilateral trade disciplines. The Agreement provides for more transparent national procedures for the initiation of safeguard action, and the determination of serious injury and the threat thereof, clearly prohibits voluntary export restraints and confirms the most-favoured-nation (MFN) principle. A measure of flexibility is permitted, however, in certain circumstances, when quotas are being allocated under the so-called 'quota modulation' system, and this could lead to a certain selectivity although such departures would be subject to specific disciplines and surveillance.<sup>1</sup> The achievement of an effective and efficient multilateral safeguard system for the application of GATT Article XIX is of paramount importance for strengthening trade disciplines and improving security of access to markets, particularly for developing countries and weaker trading partners. Moreover, the Agreement grants differential and more favourable treatment for developing countries by means of a threshold clause under which safeguard measures will not be applied to a product of a developing country with an import share of less than 3 per cent, and the period of application of safeguard measures will be extended.

Since the 1960s efforts have been made to control the use of anti-dumping duties. During the Kennedy Round a code was negotiated which embodied detailed procedures, limited the use of preliminary measures and of retroactive application of anti-dumping duties, and required a test of injury to domestic industry before definitive duties could be levied. Despite these improvements, anti-dumping duties have continued to be used frequently and rigorously by major industrial countries partly because the test of injury to domestic industry was not difficult to meet. The Agreement on the Implementation of Article VI of GATT 1994, which is examined in chapter III, represents an attempt to improve on the imprecise formulations in the 1979 Code. In several instances, some rules have been clarified or made precise through the inclusion of numerical standards, e.g. the 5 per cent rule for the determination of dumping, quantitative criteria for immediate dismissal of anti-dumping cases through the use of *de minimis* dumping margins and import volumes,<sup>2</sup> and a "sunset clause" to

<sup>1</sup> Quota modulation provides that members may deviate from the MFN provisions when an overall import quota is imposed by an importing country against all sources of suppliers, in that the share allocated to countries found to be contributing more to global injury could be lower than the share allocated to them on the basis of recent trade patterns.

<sup>2</sup> These criteria, which should have been more meaningful, are as follows: the margin of dumping is *de minimis*, i.e. less than 2 per cent, expressed as a percentage of the export price; or the volume of dumped imports from a particular country accounts for less than 3 per cent of imports of the like product in the importing member. This rule will not be applicable when countries with less than 3 per cent of the imports of the like product in the importing country



terminate anti-dumping duties on a date no later than five years from their imposition. Procedural requirements are amplified and made more detailed, for example for initiation of investigations, evidence, and transparency. Attempts to control some controversial national practices have succeeded to a certain extent but at the price of codifying them into the Agreement (e.g. cumulative injury assessment). The Agreement also provides for the redefinition of the conventional definition of dumping - price discrimination - to include below cost of production dumping. Nevertheless, it has left some important questions unanswered such as circumvention of anti-dumping duties and the relevance of anti-dumping measures in the context of domestic competition policies for future negotiations. The standards of review on dispute settlement, which require greater deference to decisions by national administering authorities, constitute a controversial feature of the 1994 Agreement. Whether they will unduly insulate the national regulations of all WTO members from successful challenges will have to be weighed against complaints that panels have increasingly penetrated areas that governments would wish to reserve exclusively for themselves. The meaningfulness of the provisions of the Agreement will reside in their application in national laws and administrative practices. Whether the Agreement will effectively insulate normal price competition against unjustified anti-dumping actions in the context of the World Trade Organization will also depend on future cases and the automatic approval of panel reports. If anti-dumping measures become the preferred instrument of protection for many WTO members, the appropriate resources should be invested in national structures to administer anti-dumping investigations, particularly in countries that do not have a tradition of taking anti-dumping measures.

Chapter IV notes that, for the first time, under the Subsidies and Countervailing Measures Agreement, a definition of subsidies has been established, as involving a financial contribution by a government or any public body which thereby confers a benefit. Subsidies are classified into prohibited, actionable and non-actionable, which reflects an international consensus as to the appropriate role for governments in supporting production and exports. Specificity is a key concept in the Agreement in that remedies provided against prohibited subsidies in Part II, or against actionable subsidies under Part III, or countervailing measures in Part V, can be ap-

plied only if a subsidy is specific to an enterprise or industry or a group of enterprises or industries. Members will have three years to bring their existing programmes into conformity with the provisions of the Agreement, with flexibility given to developing countries and least developed countries. The Agreement will provide a degree of predictability in international trade as regards the use by governments of clearly prohibited subsidies and the fact that other subsidies have been categorized as permissible but actionable, with comprehensive guidance on determination of adverse effects and serious prejudice, along with detailed remedies. Some of the contentious issues in relation to prohibited and actionable subsidies (e.g. adverse effects, serious prejudice and the remedies to deal with such subsidies) may perhaps be negotiated outside the bounds of this Agreement, in particular with respect to steel and civil aircraft. The Agreement in general does not apply to subsidies on agricultural products, which have been dealt with in the Agreement on Agriculture, through the negotiation of quantitative limits on domestic and export subsidies. Chapter IV tackles some of these issues in its Annexes.

Chapter V covers the Agreement on Textiles and Clothing, which is of particular importance to developing countries, as this sector has served as the engine of growth for them. It accounts for nearly 45 per cent of the developed countries' imports from the developing countries. For over three decades trade in this area of critical export interest to developing countries had been subject to a derogation from the disciplines of GATT, which permitted developed "importing" countries to impose discriminatory restrictions (generally in the form of export restraints) against "low cost" developing country suppliers. These restrictions first took the form of the Short-Term Cotton Textile Arrangement in 1961, which became the Long-Term Cotton Arrangement in 1962, and eventually the Multi-Fibre Arrangement (MFA) in 1974, which expanded in country and product coverage at each renewal. For the first time, during the Uruguay Round, efforts were made to negotiate the termination of this long-standing derogation in a sector in which the developing countries have traditionally enjoyed comparative advantage and their exports have been discriminated against. The Agreement on Textiles and Clothing provides for the progressive phasing out of all MFA restrictions as well as other restrictions, and the integration of this sector into GATT 1994 in four stages over a non-renewable tran-

collectively account for more than 7 per cent of imports of the like product in the importing country; or where the injury is negligible.

sition period of 10 years. Since each importing member will select the products it wishes to be integrated into GATT unilaterally, it is difficult to foresee which of the MFA restrictions will be phased out in the early stages, although it may be expected that the most sensitive products, where the growth rates are lowest and quota levels filled, will be liberalized at the final stage. Thus, many developing countries will derive meaningful benefits in this sector only in the tenth year. However, the Agreement continues to allow MFA-type selective safeguard actions (i.e. on a member-by-member basis) to be applied during the transition period under so-called "transitional safeguards".

Another major outcome of the Uruguay Round has been the negotiation of the new multilateral disciplines devised in the areas of intellectual property rights and trade in services and their linkage with GATT through the integrated dispute settlement mechanism. The extension of multilateral trade obligations, and the attempts to use the TRIMs mandate to negotiate rules on investment, should be viewed in the context of a persistent theme in international economic debate: that of establishing multilateral rules for the protection of property rights. Chapters VI, VII and VIII address the results of these negotiations.

Chapter VI studies the Agreement on Trade-Related Investment Measures (TRIMs) which codifies existing practice under GATT. Developing countries were successful in blocking efforts aimed at negotiating an agreement on investment *per se*, including right of establishment and national treatment for investors. In fact, the only concessions on investment are not contained in the TRIMs Agreement but in the General Agreement on Trade in Services (GATS), which sets out a framework for negotiations on national treatment and market access through commercial presence mode of supply. The TRIMs Agreement relates to trade in goods only and provides an illustrative list of TRIMs that are mandatory or enforceable under domestic law or administrative rulings or with which compliance is necessary to obtain an advantage. The list covers TRIMs that are inconsistent with the obligations of national treatment and of general elimination of quantitative restrictions of Article XI:1 of GATT, which relate in particular to local content requirements, trade balancing requirements, exchange restrictions and domestic sales requirements. The Agreement does not define a TRIM or provide an objective test for identifying such measures; it will therefore be

for the notifying country to judge which of its TRIMs are prohibited. The discussions in the TRIMs Committee under the WTO Agreement and the dispute settlement mechanism may provide clearer guidelines in this respect. Although developing countries succeeded in circumscribing the scope of the TRIMs Agreement to the codification of the Canadian FIRA case,<sup>3</sup> Article 9 on review of the operation of the Agreement provides for consideration of whether the Agreement should be complemented with provisions on investment policy and competition policy.

Chapter VII looks at the major results obtained by the extension of multilateral disciplines to the new area of trade in services. The unique feature of the General Agreement on Trade in Services (GATS) is the extension of the scope of multilateral trade rights and obligations to cover such diverse measures as those relating to foreign direct investment, and movement of persons and of electronic data across national frontiers, as well as professional qualifications, thus making these legitimate subject-matters for inclusion in future trade negotiations. This chapter examines in considerable detail the General Agreement on Trade in Services and the problems of assessing the impact of the results of the negotiations on specific commitments. GATS contains the first agreed definition of "trade in services", which can be accomplished through the four "modes of supply" of cross-border movement, movement of consumers, commercial presence, and the presence of natural persons. The main body of GATS consists of general obligations and disciplines, including unconditional MFN treatment and increasing participation of developing countries. Market access and national treatment, however, are not general obligations, being confined to sectors and subsectors, and modes of supply, on which specific commitments are made. Development is an obligation and an inherent objective of the Agreement, and thus is not a special treatment granted for a specific time-frame. The developing countries are required to liberalize, but to a lesser degree, and market access granted by them is conditional upon measures to assist them to strengthen their services sectors, *inter alia*, through access to information networks and distribution channels.

Most countries provide a standstill in their schedules of commitments. The extent to which the commitments actually provide a rollback of restrictions can only be determined by an analysis of the legislative changes introduced by members to implement their conces-

<sup>3</sup> Foreign Investment Review Act. See GATT, *Basic Instruments and Selected Documents (BISD)*, Thirtieth Supplement.

sions. However, even the consolidation of the status quo through the application of the MFN clause, and the specific market access and national treatment commitments made in particular sectors and subsectors by guaranteeing security of access, will expand trade and investment in services. The degree of development of the services sector is reflected in the coverage of the sectors offered in the schedules of specific commitments. The majority of the offers cover tourism services. Sectors with a high degree of coverage include business services, transport services, communications services and financial services. Sectors with a low degree of coverage include construction, distribution, education, environment, health and recreational services. The modes of supply most frequently included in schedules of commitments are those of commercial presence and movement of consumers. The mode of supply of natural persons, which is of particular interest to developing countries, has been offered in nearly all schedules through horizontal commitments in the limited category of intracorporate transferees and business visitors, which is linked to commercial presence. A few countries have offered access for additional categories of natural persons. In general therefore, movement of persons in categories of interest to developing countries is not offered. It is difficult to establish criteria and parameters for an evaluation of the value of concessions and an estimate of their trade impact. The major impediment to assessing the impact of commitments is the lack of disaggregated statistics on trade, production and investment in the services sector.

Chapter VIII on trade-related intellectual property rights (TRIPs) analyses the key features of the Agreement on the subject and evaluates its implications in terms of its effect on the volume and costs of transfer and diffusion of technology in developing countries and on the costs associated with the implementation and enforcement measures. It underlines the fact that the Agreement introduces profound changes in the traditional standards of intellectual property rights, which will influence competition in the world economy, as well as the generation and diffusion of technological innovations, and, ultimately, the technological prospects of developing countries. Through the Agreement, the basic GATT principles of national treatment and MFN treatment are applied to intellectual property rights, the provision of effective enforcement measures for those rights, multilateral dispute settlement and transitional arrangements. The Agreement establishes minimum standards on patents, copyrights, trademarks, industrial designs, geographical indications, layout designs for integrated circuits and protection of undis-

closed information, which are enforced through a comprehensive set of provisions, building upon and, in certain cases, going beyond the provisions of existing WIPO instruments. It establishes that all products or processes in all fields of technology are patentable. The "General obligations" (Part III, section 1) call on countries to make available, under their laws, enforcement procedures and remedies to enable right holders to take action against any infringement of intellectual property rights. One of the most significant provisions is that the judicial authorities should be empowered to order, without hearing the alleged infringer, provisional measures, *inter alia*, to prevent infringement and to preserve evidence. In respect of each category of intellectual property rights, the Agreement builds upon the existing international conventions and specifies a number of higher and additional standards of protection. Countries may, however, adopt measures to protect public health and nutrition and to promote public interest in sectors of vital importance to their socio-economic and technological development. It is also envisaged that appropriate measures may be needed to prevent the abuse of intellectual property rights or practices that unreasonably restrain trade or adversely affect the international transfer of technology in accordance with certain established criteria. The Agreement provides, for the first time in an internationally binding instrument, a number of rules on restrictive practices in licensing contracts. Countries are thus free to specify, in their legislation, licensing practices or conditions that may constitute an abuse of intellectual property rights and have an adverse effect on competition in the market concerned.

One of the controversial issues which the Agreement provides for is compulsory licensing under the patent system, which requires a patent to be worked in the territory where the patent has been granted, within a specified period of the grant. The Agreement sets conditions under which compulsory licensing may be granted, such as public health and nutrition, national emergency and extreme urgency, public non-commercial use, anti-competitive practices such as monopolistic pricing and the exploitation of a dependent patent.

The implementation of the Agreement on TRIPs would incur costs for developing countries, not only with respect to the imported technology but also administrative costs owing to the necessity of significant legal, administrative and institutional reforms, which would require complementary international support in the form of improved financial flows, investment and technology transfer. Identifying the parameters of healthy competition, which is

necessary for all players in an integrated world market, will require comprehensive rules on anti-competitive practices in a post-TRIPs economic environment.

Chapter IX covers the integrated dispute settlement mechanism which links goods, services and intellectual property. The Understanding on Rules and Procedures Governing the Settlement of Disputes was negotiated to give confidence to all participants that they would have the means to assure the proper fulfilment by other WTO members of the obligations contained in the Final Act and to provide a solid safeguard against unilateral action by any member. The Dispute Settlement Body, which is entrusted with the administration of the Understanding and with consultation and dispute settlement provisions of the covered agreements, has the authority to establish panels, adopt panel and appellate body reports, maintain surveillance of implementation of rules and recommendations and authorize suspension of concessions and other obligations under the covered agreements. Its decisions will be taken by consensus, which should facilitate the adoption of panel reports. Moreover, the Understanding provides for a time-frame for the entire dispute settlement procedure, which establishes the automatic nature of the Understanding, and would ensure permanent monitoring of the implementation of adopted recommendations or rulings. There is also provision for particular attention to be paid to matters affecting the interests of developing

country members with respect to measures that have been subject to dispute settlement. The commitment exists to provide developing countries with the means both to press for the early removal of third-country measures that are harmful to their export trade, and to claim leeway in terms of their own import measures that have been found to be inconsistent with their obligations.

Chapter X examines the emerging trade policy agenda for negotiations among which environment and competition issues are perhaps the most clearly defined at present. This chapter, drawing on previous work in UNCTAD and elsewhere, attempts to provide a clearer understanding of the evolution of selected issues that could form the future agenda of the WTO. The common theme for the developed countries in these areas is "levelling the playing field" by requiring certain minimum norms to be included in domestic policies that impinge on economic competitiveness. The developing countries, on the other hand, are concerned that the new issues, particularly any link between trade and labour rights, could be used for protectionist purposes. Many developing countries, both in the implementation of the Final Act and in the negotiations on the future agenda, will face serious challenges with respect to institutional and negotiating capacity, human resource development and information management, and will require increased support in these respects through technical assistance programmes. ■

# AGREEMENT ESTABLISHING THE WORLD TRADE ORGANIZATION

## A. Introduction

The Final Act Embodying the Results of the Uruguay Round of the Multilateral Trade Negotiations was signed at the Ministerial Meeting of the Trade Negotiations Committee on 15 April 1994.<sup>4</sup> It provides that the Agreement Establishing the World Trade Organization, to which all substantive agreements and understandings are annexed, as well as the Ministerial Declarations and Decisions adopted at Marrakesh, and the Understanding on Commitments in Financial Services, form an integral part of it. For practical purposes, therefore the participants, in signing the Final Act, made a commitment to place the entire package of the Uruguay Round results before their competent national authorities, which, according to their respective domestic constitutional procedures, would act with the aim of approving or ratifying it. Thus, the Final Act stipulates that the participants, *inter alia*, agree to "submit, as appropriate, the Agreement Establishing the World Trade Organization for the consideration of their respective competent authorities with a view to seeking approval of this Agreement in accordance with appropriate procedures of the participant concerned." Other elements of the Final Act are:

- the agreement to adopt the Ministerial Declarations and Decisions;
- the agreement on the desirability of acceptance of the WTO Agreement by all participants with a view to its entry into

force by 1 January 1995, or "as early as possible thereafter". It was also agreed that the WTO Agreement must be accepted as a whole without any exceptions;

- the agreement to convene a Ministerial Meeting not later than late 1994 to decide on the international implementation of the Uruguay Round results, including the timing of their entry into force, in accordance with the final paragraph of the Punta del Este Declaration;
- the agreement that, before accepting the WTO Agreement, participants in the Uruguay Round which are not contracting parties to the GATT must first have concluded their accession negotiations and become GATT contracting parties. For them, schedules of concessions in goods and services are not definitive and will be completed for the purposes of their accession to GATT and acceptance of the WTO Agreement.

The WTO Agreement was opened for acceptance at Marrakesh and participants which were GATT contracting parties were invited to sign it, for which full powers were required from their national authorities.

At the Marrakesh Ministerial Meeting a total of 111 countries out of 125 formal participants in the Uruguay Round signed the Final Act. The WTO Agreement was signed by 104

<sup>4</sup> The signature of the Final Act conformed to the procedures foreseen in Article 10 of the Vienna Convention on the Law of Treaties as regards the establishment of the authentic and definitive text of a treaty.

participants in many cases subject to further ratification or approval. Seven countries (Australia, Botswana, Burundi, India, Japan, Republic of Korea and the United States) did not sign the WTO Agreement because of their respective national legislative procedures.

In addition, several Ministerial Decisions were adopted at Marrakesh to ensure the tran-

sition from the GATT to the WTO. In particular, the Decision on the Establishment of the Preparatory Committee for the WTO envisages a transitional organizational structure and a programme of action, including seeking solutions to various administrative, procedural and legal matters to ensure the efficient operation of the WTO as of its entry into force.

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## B. Background to the Negotiations

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Neither the Punta del Este Declaration nor the 1988 Mid-Term Review Agreement foresaw that the results of the Uruguay Round would be implemented through the establishment of a new organization. At Punta del Este it was agreed that "when the results of the Multilateral Trade Negotiations in all areas have been established, Ministers meeting also on the occasion of a Special Session of CONTRACTING PARTIES shall decide regarding the international implementation of respective results". The participants agreed also that the Uruguay Round constituted a "single undertaking" in the sense that partial results limited to certain items would not be acceptable. Some participants considered that this could be implemented only through an organizational arrangement.

The WTO Agreement is based on the proposals submitted in 1990 by the European Communities and Canada, which envisaged a new organization as the most effective and pragmatic mechanism for: (a) implementing the results of the Uruguay Round; (b) incorporating the results in new areas (Trade in Services and Trade-Related Intellectual Property Rights-TRIPs) into the multilateral framework of trade rights and obligations; (c) introducing amendments to certain GATT Articles and some of the Tokyo Round Codes; (d) correcting the fragmentation of the GATT legal system which resulted from the implementation of the Tokyo Round agreements; and (e) obtaining the "definitive" application of GATT by member countries. The proposed organization should be endowed with a permanent and solid institutional status to enable it to play a greater role in global economic policy-making in coop-

eration with the International Monetary Fund and the World Bank.

On 9 July 1990 the European Communities formally submitted a proposal to the Negotiating Group on the Functioning of the GATT System (FOGS) advocating the establishment of a Multilateral Trade Organization (MTO).<sup>5</sup> It should be purely institutional in character, and act as an umbrella for the administration of the GATT and other multilateral trade agreements emerging from the Uruguay Round. The EC proposal later served as a basis for the draft MTO Agreement included in the Draft Final Act of 20 December 1991.

Canada had communicated similar ideas informally in April 1990, stressing the need for an institutional structure adapted so as to resolve the problems arising in incorporating the agreements that were expected to be reached on trade in services and trade-related aspects of intellectual property rights (TRIPs) into the multilateral framework of trade rights and obligations, in resolving the legal and procedural problems involved in introducing amendments to GATT, and in revising the Tokyo Round Codes and clarifying their relationship with GATT.

Switzerland<sup>6</sup> pursued a somewhat different approach in proposing to the FOGS Group the strengthening of both GATT as an institution and its cooperation with the Bretton Woods institutions. The Swiss submission aimed at establishing GATT as the authority with the knowledge and experience to conduct a meaningful trade policy dialogue, advocating a review of the GATT Secretariat in order to reinforce its independent analytical capacity.

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<sup>5</sup> GATT document MTN.GNG/NG14/W/42, 9 July 1990.

<sup>6</sup> GATT document MTN.GNG/NG14/W/41, 17 May 1990.

The United States presented a formal proposal to the FOGS Group on 18 October 1990 suggesting the establishment of a GATT Management Board with a view to improving the overall effectiveness and decision-making of the General Agreement.<sup>7</sup>

The Draft Final Act presented to the Brussels Ministerial Meeting of the Trade Negotiations Committee in December 1990 envisaged that work would be initiated towards the establishment of an organizational agreement, although square brackets in the text indicated disagreement with respect to virtually all relevant aspects of this issue.<sup>8</sup>

The Agreement establishing the Multilateral Trade Organization (MTO) formed an integral part of the Draft Final Act embodying

the results of the Uruguay Round, as contained in document MTN.TNC/W/FA of 20 December 1991. In January 1992 a "four-track approach" was adopted for the concluding phase of the Uruguay Round. "Track three" consisted of work to ensure the legal conformity and internal consistency of the agreements constituting the Draft Final Act. The Legal Drafting Group was set up for this purpose.

In 1993 work on the draft MTO Agreement progressed in an informal setting. This was basically concluded by mid-November 1993, although negotiations on several difficult points proceeded until literally minutes before the general deadline of 15 December. Finally, at the last moment, the title of the new organization was changed to "World Trade Organization".

## C. Main provisions of the Agreement

### 1. Content and functions

The WTO Agreement consists of a preamble, sixteen Articles and four Annexes. Other than general references contained in its preambular paragraphs, it does not incorporate any substantive multilateral rules and disciplines (concerning, for example, MFN treatment, non-discrimination, national treatment, etc.).

The preamble is a redrafting of the GATT 1947 preamble, and is the only place in the Agreement where substantive matters are touched upon. In particular, it introduces the notion of sustainable development in the following words: "allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development", and expands the scope of the

Agreement to trade in services. It also recognizes the "need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development", which is the only reference to the special problems of the developing countries in the Agreement. The penultimate preambular paragraph states the determination of members to develop "an integrated, more viable and durable multilateral trading system encompassing the General Agreement on Tariffs and Trade, the results of past trade liberalization efforts, and all of the results of the Uruguay Round of Multilateral Trade Negotiations".

Multilateral Trade Agreements (MTAs) (the Multilateral Agreements on Trade in Goods, the General Agreement on Trade in Services and the Agreement on Trade-Related Aspects of Intellectual Property Rights) form Annexes 1A, 1B and 1C respectively of the Agreement.<sup>9</sup>

<sup>7</sup> This proposal recalled that the Havana Charter made provision for an Executive Board in the ITO, and suggested that the GATT Management Board should be established at the Ministerial level with wide functions, including primary responsibility for developing an outline, for the consideration of the contracting parties, of a successor organization to GATT (MTN.GNG/NG14/W/45, 18 October 1990).

<sup>8</sup> MTN.TNC/W/35:Rev.1, 3 December 1990.

<sup>9</sup> *Annex 1A* covers: (i) the "GATT 1994", which consists of (a) the provisions in the "GATT 1947" as rectified, amended or otherwise modified by the terms of legal instruments which have entered into force before the date of entry into force

Annex 2 covers the Understanding on Rules and Procedures Governing the Settlement of Disputes, while Annex 3 contains the text on the Trade Policy Review Mechanism (TPRM). Plurilateral Trade Agreements (PTAs) are to be found in Annex 4.<sup>10</sup>

The Agreements in Annexes 1, 2 and 3 are binding on all members of the WTO, and, in fact, their acceptance, along with specific schedules of concessions on goods and services, is a strict condition for membership in the WTO. Annex 4 agreements may have *limited membership*, and create rights and obligations only for members that have accepted them.

The WTO Agreement stipulates that GATT 1994 and GATT 1947 are two different agreements (they are "legally distinct"), although GATT 1994 consists of the text of the GATT 1947 and its legal instruments, as well as of several Understandings on interpretations and modifications of GATT Articles, and the Marrakesh Protocol containing schedules of concessions on goods. In the Uruguay Round, the participants, pressured by the time factor, could not accomplish the delicate legal task of drafting those parts of the GATT 1947 which are to be superseded by the WTO Agreement. The pragmatic solution found was to incorporate the GATT 1947 by reference through inclusion of an incorporation clause in Annex 1A of the WTO Agreement.

The WTO will thus provide the common institutional framework for the conduct of trade relations among its members in matters related to the agreements and associated legal instruments included in the above-mentioned annexes. Among its functions are: (1) facilitation of the implementation, administration and operation of the annexed agreements; (2) provision of *the* forum for negotiations among its members concerning their multilateral trade relations in matters dealt with under the annexed agreements, and of *a* forum for further negotiations among its members concerning their multilateral trade relations, as well as a

framework for the implementation of the results of such negotiations; (3) administration of the Dispute Settlement Body; (4) administration of the Trade Policy Review Mechanism; and (5) cooperation, as appropriate, with IMF and the World Bank and its affiliated agencies with a view to achieving greater coherence in global economic policy-making.

## 2. Organizational structure

The WTO organizational structure, which is open to all WTO members, consists of a Ministerial Conference, meeting at least once every two years and a General Council, meeting as appropriate. The General Council will also carry out the functions of a Dispute Settlement Body and a Trade Policy Review Body. Other bodies include a Council for Trade in Goods, a Council for Trade in Services, and a Council for TRIPs. A Committee on Budget, Finance and Administration, a Committee on Trade and Development, and a Committee on Balance-of-Payments Restrictions will be established by the Ministerial Conference. The Council for Trade in Goods, the Council for Trade in Services, and the Council for TRIPs will establish their respective rules of procedure subject to the approval of the General Council, and any subsidiary bodies they may set up will establish their respective rules of procedure subject to the approval of their respective Councils. The Council for Trade in Goods will oversee the functioning of the MTAs as set out in Annex 1A. The Council for Trade in Services will oversee the functioning of the General Agreement on Trade in Services as set out in Annex 1B, while the Council for TRIPs will oversee the functioning of the Agreement on TRIPs as set out in Annex 1C.

of the WTO Agreement, except the Protocol of Provisional Application; (b) the provisions of the legal instruments that have entered into force under GATT 1947 before the date of entry into force of the WTO Agreement such as protocols relating to tariff concessions, protocols of accession, excluding provisions related to the Protocol of Provisional Application, waivers granted under GATT 1947 and still in force on the date of entry into force of the WTO Agreement and other decisions under GATT 1947; (c) the Understandings reached in the Uruguay Round concerning interpretations to several articles of GATT; (d) the Marrakesh Protocol containing schedules of concessions on market access in goods; (ii) the Tokyo Round Codes as they result from the Final Act of the Uruguay Round and their associated legal instruments, except those Codes and Arrangements found in Annex 4; (iii) new Agreements reached in the Uruguay Round (Agreement on Safeguards, Agreement on Trade-Related Investment Measures, Agreement on Preshipment Inspection; Agreement on Rules of Origin, Agreement on Agriculture, Agreement on Textiles and Clothing, etc.);

*Annex 1B* covers the General Agreement on Trade in Services, and its associated legal instruments;

*Annex 1C* covers the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs).

<sup>10</sup> *Annex 4* covers: (i) the Agreement on Trade in Civil Aircraft; (ii) the Agreement on Government Procurement; (iii) the International Dairy Arrangement; and (iv) the International Bovine Meat Arrangement.



The General Council of the WTO will make arrangements with other intergovernmental organizations that have related responsibilities to provide for effective cooperation, as well as with non-governmental organizations for consultation and cooperation on matters related to those of the WTO.

There will be a secretariat of the WTO headed by a Director-General. The financial regulations of the WTO will be based, as far as practicable, on the regulations and practices of the GATT 1947. The WTO will have legal personality and will be accorded by its members such legal capacity as may be necessary for the exercise of its functions. It will enjoy privileges and immunities similar to those stipulated in the Convention on the Privileges and Immunities of the Specialized Agencies, approved by the General Assembly of the United Nations on 21 November 1947.

### **3. Decision-making procedures**

The Agreement foresees that the WTO will continue the GATT practice of decision-making by consensus. A decision by consensus is deemed to have been taken if no member, present at the meeting when the decision was taken, formally objected to the proposed decision. However, when a decision cannot be arrived at by consensus, the matter will be decided by voting. In this respect, different procedures have been established depending on the issue involved. Each member will have one vote at meetings of the Ministerial Conference and the General Council, except that the European Communities will have a number of votes equal to the number of their member States which are members of the WTO, but in no case will the overall number of votes of the EC exceed the number of its member States.

In general, decisions of the Ministerial Conference and the General Council that require a vote will be taken by a majority of the votes cast; however, in the case of an interpretation of the WTO Agreement or the Multilateral Trade Agreements, the decision will be taken by a three fourths majority. The Ministerial Conference and the General Council have the exclusive authority to adopt such interpretations. In the case of an interpretation of an MTA in Annex 1, the above authority will be exercised on the basis of a recommendation by the Council overseeing the functioning of that Agreement.

An obligation imposed on a member by the WTO Agreement or any of the Multilateral Trade Agreements can be waived by the Ministerial Conference on the basis of consensus in the case of the Agreement itself or a decision by a three fourths majority once a given period of time for consideration has elapsed (90 days). A decision to grant a waiver in respect of an obligation subject to a transition period or a period for staged implementation that the requesting member has not performed by the end of the relevant period will be taken only by consensus. A request for a waiver under the MTAs will be initially submitted to the respective Councils for their consideration over not more than 90 days, after which the relevant Council will report to the Ministerial Conference. A decision granting a waiver must be justified by exceptional circumstances, the terms and conditions of the waiver, and the date of its termination. Any waiver granted for more than one year must be reviewed annually by the Ministerial Conference which, on the basis of its findings, may extend, modify or terminate the waiver.

It is envisaged that the Ministerial Conference will establish at its first session a revised list of waivers including those granted under GATT 1947 after 15 December 1993 and before the date of entry into force of the WTO Agreement, and will delete those that will have expired by then. A separate Understanding in Respect of Waivers of Obligations under GATT 1994 provides additional rules for waivers, including (a) that any waiver in effect on the date of entry into force of the WTO Agreement will terminate on the date of its expiry or two years from the date of entry into force of the WTO Agreement, whichever is earlier; and (b) that any member considering that a benefit accruing to it under GATT 1994 is nullified or impaired as a result of the failure of the member to whom a waiver was granted to observe its terms or conditions, or the application of a measure consistent with waiver's terms and conditions, may invoke dispute settlement procedures.

Decisions on interpretations and waivers under PTAs will be governed by the provisions of such Agreements.

Several other decision-making procedures have been established: (a) the WTO financial regulations and annual budget estimates will be adopted by the General Council by a two thirds majority, comprising more than half of the WTO members; (b) decisions by the General Council acting as the Dispute Settlement Body will be taken only on the basis of consensus as foreseen in Article 2:4 of the Dispute Settlement Understanding; and (c) decisions on ac-

cession to the WTO will be approved by the Ministerial Conference by a two thirds majority of the WTO members.

#### 4. Procedures for amendment

Procedures regulating initiation, consideration and adoption of amendments to the WTO Agreement as well as to the MTAs have a complex decision-making mechanism of their own. Initiation of a proposal to amend the provisions of the WTO Agreement or the MTAs may be made by any member or by the Council that oversees the MTA to be amended through submission to the Ministerial Conference. During a period of 90 days (or longer by decision of the Ministerial Conference) after a proposal has been formally tabled, any decision by the Ministerial Conference to submit the proposed amendment to the members will be taken by consensus. If consensus is not reached within the established period, the Ministerial Conference will decide by a two thirds majority of the members whether or not to submit the proposed amendment.

Amendments to provisions of the WTO Agreement (except Articles IX and X) and to the provisions of the MTAs in Annexes IA (except Articles I and II of GATT 1994) and IC (except Article II:1 of GATS), and of the Agreement on TRIPs (except Article 4), that are of a nature that would alter the rights and obligations of the members, will take effect for the members that have accepted them upon acceptance by two thirds of the members and thereafter for each member upon acceptance by it. The Ministerial Conference may also decide by a three fourths majority of the members that any amendment made effective under this general rule is of such a nature that any member which has not accepted it within a period specified by the Ministerial Conference in each case will be free to withdraw from the WTO or to remain a member with the consent of the Ministerial Conference. The same procedures will apply with respect to amendments to Parts I, II (except for Article II:1), and III of the General Agreement on Trade in Services and the respective annexes.

In dealing with amendments to the WTO Agreement, GATT 1994 and other MTAs in Annex IA and the Agreement on TRIPs, that are of a nature not requiring alteration of the rights and obligations of the members, the Ministerial Conference should first decide by a three fourths majority whether the amendment

in question is of such a nature. If it is, it will take effect for all members upon acceptance by two thirds of the members.

Special procedures have been established to deal with amendments to the specific provisions of the WTO Agreement and MTAs, such as:

- Amendments which require acceptance by all members involve (1) articles in the WTO Agreement dealing with decision-making and amendments; (2) Articles I and II of GATT 1994 (MFN treatment); (3) Article II:1 of the General Agreement on Trade in Services (MFN treatment); and (4) Article 4 of the Agreement on TRIPs (MFN treatment);
- Amendments to Parts IV, V and VI of the General Agreement on Trade in Services and the respective annexes will take effect for all members upon acceptance by two thirds of the members;
- Amendments to the Agreement on TRIPs meeting the requirements of its Article 71 (paragraph 2) may be adopted by the Ministerial Conference without further formal acceptance procedures. This provision relates to amendments "merely serving the purpose of adjusting to higher levels of protection of intellectual property achieved, and in force, in other multilateral agreements and accepted under those agreements by all WTO members".

It is envisaged that members accepting an amendment to the WTO Agreement or MTAs in Annex 1 will deposit an instrument of acceptance with the Director-General of the WTO within the period of acceptance specified by the Ministerial Conference.

The WTO Agreement contains specific procedures in dealing with amendments concerning its Annex 2 (Dispute Settlement) and Annex 3 (Trade Policy Review Mechanism). Decisions to approve amendments to Annex 2 will be made by consensus. They will take effect for all members upon approval by the Ministerial Conference, as will decisions to approve amendments to Annex 3.

In relation to the Plurilateral Trade Agreements (PTAs) in Annex 4, it is stipulated (a) that the Ministerial Conference, at the request of the members parties to a trade agreement, may decide exclusively by consensus to add a PTA to Annex 4 or to delete a PTA from the same Annex; (b) that amendments to PTAs will be governed by their provisions.

## 5. Original membership and accession

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The WTO Agreement stipulates that the contracting parties to GATT 1947 as of the date of entry into force of this Agreement, and the European Communities, which accept the Agreement and the MTAs, and which have submitted their schedules of concessions on goods (annexed to GATT 1994) and services (annexed to GATS), are eligible to become original members of the WTO. There is an exemption from that basic requirement related to the least developed countries which will only be required to undertake commitments and concessions to the extent consistent with their individual development, financial and trade needs or their administrative and institutional capabilities.<sup>11</sup>

The provision on accession is similar to that of GATT 1947, except in the case of a separate customs territory. Under Article XXVI:5 of GATT 1947, accession of a separate customs territory was achieved by sponsorship through a declaration by the responsible contracting party. In the WTO Agreement no distinction is made between a State or a separate customs territory in that both are entitled to become WTO members provided that the latter has full autonomy in the conduct of its external commercial relations. In the Explanatory Notes to the WTO Agreement, the terms "country" or "countries" as used in the WTO Agreement or the MTAs are understood to include any customs territory member of the WTO.

Accession to the PTAs will be governed by their own provisions.

## 6. Definitive application

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The WTO Agreement contains the obligation that "each member shall ensure the conformity of its laws, regulations and administrative procedures with its obligations as provided in the annexed Agreements". Bearing in mind the complexities of the legal relationship between the GATT and national law in some major trading countries, this provision could

be open to different interpretations. In this context, WTO members will have an option to resolve such differences through recourse to the new dispute settlement mechanism. However, no previously applied "grandfather rights" through the Protocol of Provisional Application of GATT 1947 and the respective protocols of accession to the latter are permitted any longer, except for one exclusion as defined in point 3(a) of the Explanatory Notes to Annex IA of the WTO Agreement. This exclusion stipulates that the provisions of Part II of GATT 1994 will not apply to measures taken by a member under specific mandatory legislation, enacted by that member before it became a contracting party to GATT 1947, that prohibits the use, sale or lease of foreign-built or foreign-reconstructed vessels in commercial applications between points in national waters or the waters of an exclusive economic zone (the United States "Jones Act").

## 7. Other provisions

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The non-application provision of the Agreement can be applied to original WTO members only if Article XXXV of GATT 1947 had previously been invoked and was effective at the time of entry into force of the WTO Agreement for the members concerned.<sup>12</sup> It can be applied against a new WTO member only if the member not consenting to the application has so notified the Ministerial Conference before the approval of the terms of accession of the former. The requirement in GATT Article XXXV that it could only be invoked if the countries concerned had not previously entered into tariff negotiations has been eliminated. Non-application of PTAs will be governed by their own provisions.

The Agreement stipulates that in the event of a conflict between its provisions and those of any of the MTAs annexed to it, the provisions of the WTO Agreement will prevail.

The Agreement, together with the MTAs annexed to it, will remain open for acceptance for a period of two years following the date of the Agreement's entry into force. An acceptance after that date will enter into force on the 30th day following the deposit of the instrument of acceptance. A member which accepts the Agreement after its entry into force is required to implement those concessions and ob-

<sup>11</sup> See annex 1 below.

<sup>12</sup> See annex 3 below.

ligations in the MTAs that contain time periods starting with the entry into force of the WTO Agreement as if it had accepted this Agreement on the date of its entry into force (retroactive application of certain obligations).

Withdrawal from the WTO Agreement applies also to the MTAs and will take effect upon the expiration of six months from the date on which written notice of withdrawal is received by the Director-General of the WTO.

## D. Implications

### 1. General observations

The WTO Agreement does not establish a minimum number of members or a minimum percentage of world trade as a condition for its entry into force (this contrasts with Article XXVI of GATT 1947 which provided for entry into force upon acceptance by countries accounting for 85 per cent of the total trade of the countries shown in its Annex H). Countries that become WTO members will also remain as contracting parties to the GATT 1947 (and thus bound by two legally distinct sets of multilateral obligations) if they do not withdraw simultaneously from the latter.

### 2. Increase in levels of obligations and problems of accession

The establishment of the WTO will introduce substantial modifications of relevance for the overall system of trade rights and obligations. Thus, contracting parties to GATT 1947 which become members of the WTO will be required to accept all MTAs, incorporated in Annexes 1, 2 and 3 of the WTO Agreement, without any exceptions or reservations, as well as to submit their Schedules of concessions on goods, and of specific sectoral and sub-sectoral concessions with respect to market access and national treatment for trade in services. This would lead to a substantial increase in the scope of obligations for all GATT contracting parties, but developing countries, in particular,

will be faced with a dramatic increase in the level of their obligations as most emerge from the Round with a much higher level of tariff bindings, in some cases across-the-board, particularly in agriculture, and have accepted new obligations flowing from the revised Tokyo Round Codes,<sup>13</sup> which had previously been accepted by a minority of developing countries, as well as new obligations in the areas of trade in services and, in particular, intellectual property rights. The very strict conditions for accession to the WTO will therefore be a serious challenge to them. The WTO will substantially reduce the flexibility which developing countries have enjoyed under the multilateral trading system with respect to their trade policies and in certain areas considered to fall in the domestic policy sphere. These obligations are somewhat mitigated by the provisions on differential and more favourable treatment, which offer even greater flexibility to the least developed countries.

In addition, the WTO Agreement eliminates the possibility for those developing countries and territories which apply de facto GATT rules in their foreign trade to accede, as is now the case, by a simple declaration under GATT Article XXVI:5 (c).<sup>14</sup> The process of accession will also be much more difficult, including for those developing countries and economies in transition now negotiating their terms of accession to GATT, as they will need to adapt to the new agreements negotiated in the Uruguay Round. For example, they will have to negotiate an "entry fee" on both goods and services, accept a variety of Agreements that until now have been optional (i.e. most Tokyo Round Codes as revised), and commit themselves to a set of new multilateral rules and disciplines in

<sup>13</sup> As of May 1994, 15 developing countries were parties to the Agreement on Technical Barriers to Trade; 2 to the Agreement on Government Procurement; 13 to the Subsidies Code; 11 to the Anti-Dumping Code; 12 to the Customs Valuation Code; 12 to the Agreement on Import Licensing; 2 to the Civil Aircraft Agreement; 10 to the International Bovine Meat Arrangement and 4 to the International Dairy Agreement.

<sup>14</sup> These countries were formerly colonies or dependent territories. At present, there are still 13 developing countries and territories in this category.

the areas of agriculture, subsidies, and intellectual property rights, among others.

### 3. Cross-sectoral retaliation

The WTO foresees, through its dispute settlement mechanism, "cross-sectoral retaliation" between market access concessions and rule-making obligations in the area of goods and new obligations in the areas of intellectual property and trade in services, as well as any new areas for which members decide to negotiate multilateral obligations.<sup>15</sup> Cross-sectoral retaliation, under which restrictive action can be taken against exports of goods in a compensatory "suspension of concessions" for measures that members might apply in other areas under the Agreement (TRIPs and services), may be authorized under the Understanding on Rules and Procedures Governing the Settlement of Disputes, although procedural devices determine that this would arise only as a last resort. Cross-sectoral retaliation was a major objective of major trading countries; the extent to which it could have positive aspects in defending weaker countries' positions will have to be seen in practice.

### 4. Plurilateral Trade Agreements

Annex 4 of the WTO Agreement "Plurilateral Trade Agreements", while originally intended to provide legal cover for Tokyo Round Codes not renegotiated in the

Uruguay Round, including those applied on a "conditional" MFN basis among signatories, could imply the creation of a legal mechanism for negotiating future multilateral trade agreements of limited membership. The possibility is provided for in relation to the addition of a new PTA to Annex 4 although this must be decided by the Ministerial Conference exclusively by consensus. However, there are no specific rules dealing with the initiation of such plurilateral negotiations.

The possible proliferation of PTAs would limit the application of unconditional MFN and non-discrimination in the international trading system, since they would create rights and obligations only for members that accepted them. Annex 4 could eventually be used as a legal justification to negotiate new agreements among a few members of the WTO, the benefits of which would not need to be extended to other members. It should be noted that the WTO Agreement does not contain an unconditional most-favoured-nation clause, which has instead been included respectively in GATT 1994, GATS and TRIPs Agreement.

PTAs could eventually be adopted in cases where multilateral negotiations do not lead to consensus among all WTO members, paving the way for individual WTO member countries with likeminded positions to legalize their relations on specific trade issues under the coverage of the WTO. There are already candidates for future PTAs such as the Multilateral Steel Agreement (MSA), as well as the proposed new agreement covering antitrust issues.<sup>16</sup> Paradoxically, PTAs could lead to a further fragmentation of the multilateral trading system, creating within one organization different levels of rights and obligations as well as two categories of members.

## E. Conclusions

The WTO Agreement is of a purely institutional and procedural character. Basically, its main functions are administration of GATT 1994 plus the multilateral trade agreements negotiated in the Uruguay Round, and negoti-

ation of further agreements in any area of multilateral trade relations which could permit any trade-related subject to be covered by future trade negotiations. Other important functions of the WTO include dispute settlement

<sup>15</sup> See, for example, "President Clinton's submission to Congress of documents concerning the Uruguay Round Agreement, December 15, 1993", *International Trade Reporter*, Vol. 10, Washington, D.C., 22 December 1993, p. 2164.

<sup>16</sup> See "Draft International Antitrust Code as a GATT-MTO Plurilateral Trade Agreement", International Antitrust Code Working Group, Munich, Germany, July 1993.

and the trade policy review mechanisms, the latter providing a forum for regular monitoring of trade policies of members. Thus, the WTO will have an open-ended, evolving substantive mandate.

On the other hand, the WTO will inherit decisions, procedures and "customary practices" followed by the contracting parties of GATT 1947, although it will not be a successor agreement to GATT in a legal sense. At this stage the major accomplishment of the WTO will be to provide a link between multilateral rights and obligations relating to market access with those on intellectual property and trade in services. The open-ended scope of the WTO ensures that this link will be maintained with multilateral agreements that may be negotiated in new areas. This would indicate that the negotiation of any future agreements in the WTO will largely depend on its members' willingness to link their policies in those areas to a set of multilateral trade rules and disciplines subject to an integrated dispute settlement system, thus exposing those policies to possible retaliatory trade actions. The reluctance of governments in this respect, which is already being observed in such areas as labour standards, may inhibit any rapid expansion of the scope of WTO obligations in future negotiations.

The WTO clearly strengthens multilateral obligations in the sense that, to become members, all countries must accept all of the MTAs. By establishing multilateral obligations in new areas and linking them to a unified dispute settlement mechanism, it should reduce the freedom that countries have had in the past to resort to unilateral approaches, such as the Section 301 actions under the United States trade law, through the commitment of its members to ensure the conformity of their laws, regulations and administrative procedures with their obligations under those Agreements.

Various views have been expressed as to the role the WTO will play in the "new world order". One view, which emerged immediately after the agreement on the Uruguay Round final package on 15 December 1993 and was reflected in several of the Ministerial statements at Marrakesh, portrayed the WTO as finally

taking the place of the stillborn ITO envisaged in the Havana Charter, and constituting the "missing pillar" of the postwar world economic system, a third "Bretton Woods" institution.<sup>17</sup> However, other competent opinions have been voiced to the effect that "the WTO has no more real power than that which existed for the GATT under previous agreements",<sup>18</sup> and that the new organization will be "no different in character from the existing GATT secretariat, nor is it expected to be a larger, more costly organization"<sup>19</sup> (it has been described as a "mini-charter" and not as the ITO of the Havana Charter).<sup>20</sup> The differing views expressed as to the significance of the WTO naturally reflect the particular political context in which they are expressed.

In this context, the position of the WTO vis-à-vis the United Nations and other international organizations remains to be defined. The United Nations General Assembly, which has been considering for the last several years issues related to strengthening international organizations in the area of multilateral trade, and is expected to pay special attention to this matter at its forthcoming forty-ninth session,<sup>21</sup> could be viewed as the proper forum for defining actions needed to ensure the effective cooperation and complementary roles of these organizations.

It should also be noted that the recent Agreed Conclusions 410 (XL) adopted by the Trade and Development Board after the Marrakesh Ministerial meeting recognize that there should be constructive and effective cooperation between UNCTAD and the WTO based on the complementary functions of the two organizations. Furthermore, in the Mid-term Review of the Cartagena Commitment of UNCTAD VIII, conducted in May 1994 by the Trade and Development Board, the institutional framework within which such complementarity could be developed was strengthened when three new UNCTAD inter-governmental Ad Hoc Working Groups were created: on Trade, Environment and Development; on the Role of Enterprises in Development; and on Trading Opportunities in the New International Trading Context. ■

<sup>17</sup> See the Address by Peter D. Sutherland to the World Economic Forum, Davos, 28 January 1994.

<sup>18</sup> See *International Trade Reporter*, Vol. 11, 13 April 1994, p. 596, quoting Professor John Jackson of Michigan University.

<sup>19</sup> See "President Clinton's submission to Congress... ", *International Trade Reporter*, *op. cit.*.

<sup>20</sup> Testimony prepared by Professor John Jackson for the hearing of 14 June 1994 of the United States Senate Committee on Foreign Relations, 14 June 1994.

<sup>21</sup> See General Assembly resolutions 45/201, 46/207, 47/184 and 48/54.

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*Annex 1 to chapter I*

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## DIFFERENTIAL AND MORE FAVOURABLE TREATMENT FOR DEVELOPING COUNTRIES

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### A. Introduction

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The General Principles governing the negotiations, as contained in the Punta del Este Declaration, particularly stipulated that:

... (iv) ... the principle of differential and more favourable treatment embodied in Part IV and other relevant provisions of the General Agreement and in the Decision of the CONTRACTING PARTIES of 28 November 1979 on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries applies to the negotiations.

... (v) The developed countries do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of developing countries, i.e. the developed countries do not expect the developing countries, in the course of trade negotiations, to make contributions which are inconsistent with their individual development, financial and trade needs. Developed contracting parties shall therefore not seek, neither shall less-developed contracting parties be required to make, concessions that are inconsistent with the latter's development, financial and trade needs.

The Declaration also stipulated that "special attention shall be given to the partic-

ular situation and problems of the least developed countries and to the need to encourage positive measures to facilitate the expansion of their trading opportunities".

In general, the Uruguay Round agreements, with some exceptions, provide for differential and more favourable treatment for developing countries. However, all Uruguay Round obligations, including GATT 1994, the General Agreement on Trade in Services and the Agreement on TRIPs, are contained in a single legal instrument (i.e. the Agreement Establishing the World Trade Organization), which must be accepted in its entirety. This will have the effect of: (i) establishing roughly the same set of obligations for all WTO members; and (ii) linking all such rights and obligations to trade concessions. The only flexibility to be enjoyed by developing countries will be that spelled out in the respective Agreements themselves. In this context, the provisions on differential and more favourable treatment for developing countries were established on firmer legal ground. There are also "horizontal" Ministerial Decisions stipulating special measures in favour of least developed countries and defining measures concerning the possible negative effects of the reform programme in agriculture on least developed and net food-importing developing countries.

## B. Provisions on differential and more favourable treatment

The provisions on differential and more favourable treatment in agreements on trade in goods (Annex 1A of the WTO Agreement), as well as in the Agreement on TRIPs (Annex 1C) and the Understanding on Rules and Procedures Governing the Settlement of Disputes (Annex 2) can be classified into several categories, such as:

- time-limited derogations from obligations and longer periods for implementing obligations;
- higher or lower thresholds for undertaking certain commitments, depending on the specific agreement;
- flexibility in obligations and procedures;
- "best endeavour clauses";
- technical assistance and advice.

### 1. *Time-limited derogations and longer periods for implementing obligations*

The Agreement on Agriculture exempts least developed countries from making reduction commitments; other developing countries will have the flexibility to implement their reduction commitments over a period of 10 years as compared to six years in the case of developed countries.

The Agreement on Sanitary and Phytosanitary Measures establishes longer time-frames for compliance with sanitary or phytosanitary protection to be accorded to products of interest to developing countries, where such protection allows scope for phased introduction. Specified, time-limited exceptions in whole or in part from the obligations under the Agreement may be granted upon request by developing countries. The least developed contracting parties may delay application of the provisions of the Agreement for five years following the entry into force of the WTO Agreement with respect to their sanitary or phytosanitary measures affecting importation or imported products. Other developing countries may also delay application of certain provisions of the Agreement for two years, where

such application is prevented by a lack of technical expertise, technical infrastructure or resources.

The Agreement on Technical Barriers to Trade stipulates that specified and time-limited exceptions in whole or in part from the obligations under the Agreement may be granted to developing countries, upon request.

The Agreement on Trade-Related Investment Measures (TRIMs) authorizes a developing country to deviate temporarily from a general provision requiring that no member will apply any TRIM that is inconsistent with the provisions of Article III or Article XI of GATT 1994, to the extent and in the manner permitted by Article XVIII of GATT 1994, the Understanding on the Balance-of-Payments Provisions of GATT 1994, and the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes. As to the period of elimination of TRIMs, a longer time-frame of five years is provided for developing countries (this period being extendable upon request), and seven years for least developed countries, also extendable upon request (as compared to two years for developed countries).

The Agreement on Implementation of Article VII (Customs Valuation) reconfirms the developing countries' right to delay application of its provisions for up to five years.

The Agreement on Import Licensing Procedures permits a developing country to delay the application of provisions relating to automatic import licensing by not more than two years from the date of entry into force of the WTO Agreement for that country.

The Agreement on Subsidies and Countervailing Measures foresees that: (a) the prohibition of export subsidies contingent upon export performance will not apply to the least developed countries. Nor will it apply to certain developing countries whose GNP is below US\$1,000 per capita. However, if these countries reach export competitiveness in one or more products, they will gradually phase out such export subsidies over eight years. For developing countries other than the above, the phase-out period for export subsidies will be within eight years from the entry into force of the WTO Agreement, and two years if export competitiveness is reached in any given prod-



uct. The period for phase-out is extendable; (b) the prohibition of subsidies contingent upon the use of domestic over imported goods will not apply to developing countries for a period of five years, and to least developed countries for a period of eight years, from the date of entry into force of the WTO Agreement.

The Agreement on Safeguards envisages that: (a) developing countries will have the right to extend the period of application of a safeguard measure for up to two years beyond the maximum period of eight years for other WTO members; (b) they will also have the right to apply a safeguard measure again to an imported product previously subject to such a measure, taken after the date of entry into force of the WTO Agreement, after a period of time equal to half that during which such a measure has been previously applied, provided that the period of non-application is at least two years (for other WTO members, a period of non-application will be equal to that during which such a safeguard has been previously applied, while the minimum period of non-application will also be at least two years).

The Agreement on Trade-Related Aspects of Intellectual Property Rights stipulates that: (a) any developing country is entitled, with some exceptions, to delay for a further period of four years the date of application of the provisions of the Agreement; (b) to the extent that a developing country is obliged by the Agreement to extend product patent protection to areas of technology not protectable in its territory on the general date of application of this Agreement, in the case of that country the application of the provisions related to patents may be delayed for an additional period of five years; (c) least developed countries will not be required to apply the provisions of the Agreement, with some exceptions, for a period of 10 years from the date of its application. The Council on TRIPs will accord extensions of this period.

## 2. More favourable thresholds

Agreement on Agriculture: there will be lower rates of tariff and subsidy reduction for developing countries (other than least developed countries) in measures affecting agriculture, provided that the result is no less than two thirds of that specified for developed countries, as follows: (a) in market access - 24 per cent reduction in bound tariffs on a simple average basis, with a minimum rate of reduction of 10 per cent for each tariff line (as compared to 36

per cent and 15 per cent respectively for developed countries). In the case of unbound customs duties, developing countries will have the flexibility of offering ceiling bindings. In addition, a developing country may retain restrictions on imports of "a primary agricultural product that is the predominant staple in the traditional diet", provided that it gives minimum access opportunities of 1 per cent of domestic consumption to be increased to 2 per cent after five years and to 4 per cent after 10 years. Negotiations should be held if such a developing country wishes to extend this "special treatment" beyond the 10-year period; (b) in domestic support - 13.3 per cent reduction in domestic subsidies (20 per cent for developed countries) except for "green box" subsidies, which should not exceed 10 per cent of the total value of production of a basic product in the case of product-specific support or of the value of total agricultural production in the case of sector-wide aggregate measures of support (AMS), as compared to 5 per cent for developed countries; (c) in export competition - reductions of 24 per cent in the value of export subsidies and 14 per cent in volume (as compared to 36 per cent and 21 per cent respectively for developed countries). In addition, during the implementation period, developing countries will not be required to undertake commitments in respect of two export subsidy practices (involving subsidies to reduce some defined costs of marketing exports of agricultural products; and internal transport and freight charges on export shipments, provided or mandated by Governments, on terms more favourable than for domestic shipments).

Agreement on Subsidies and Countervailing Measures: a more favourable application of remedies against subsidization involving products from developing countries is foreseen:

- Any countervailing duty investigation will be terminated if (a) the overall level of subsidies granted upon the product in question does not exceed 2 per cent of its value calculated on a per unit basis (*de minimis* provision) as compared to 1 per cent in cases involving developed countries' subsidization; (b) the volume of the subsidized imports represents less than 4 per cent of the total imports for the like product in the importing signatory country, unless imports from developing country signatories, whose individual shares of total imports represent less than 4 per cent, collectively account for more than 9 per cent of the total imports for the like product in the importing country;
- For those developing countries which have eliminated export subsidies prior to the

expiry of the period of eight years and also for least developed signatory countries and developing countries whose GNP per capita is less than \$1,000 per annum, the figure for *de minimis* subsidization will be 3 per cent. However, this provision will expire eight years from the date of entry into force of the WTO Agreement.

Agreement on Safeguards: safeguard measures will not be applied against a product originating in a developing country as long as its share of imports of the product concerned does not exceed 3 per cent, provided that developing countries with an import share of less than 3 per cent collectively account for not more than 9 per cent of total imports of the product concerned.

### 3. Flexibility in obligations and procedures

Understanding on Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade 1994: simplified consultation procedures may be held in the case of least developed contracting parties or in the case of developing countries pursuing liberalization efforts. Simplified balance-of-payment consultations may also be held when a developing country is scheduled for a Trade Policy Review in the same year as the date fixed for consultations.

Agreement on Agriculture: (a) in respect of domestic support commitments, it is agreed that government measures of assistance, whether direct or indirect, to encourage agricultural and rural development are an integral part of the development programmes of developing countries. These policy measures will be exempt from reduction commitments;<sup>22</sup> (b) the provisions relating to disciplines on export prohibitions and restrictions will not be applied to developing countries, unless such a measure is taken by a developing country which is a net food-exporter of the specific foodstuff concerned.<sup>23</sup>

Understanding on Rules and Procedures Governing the Settlement of Disputes: (a) if a

complaint is brought by a developing country, that developing country may choose to apply certain other alternative procedures; (b) in consultations, members should give special attention to the particular problems and interests of developing country members; (c) when a dispute is between a developing and a developed country, the panel will, if the developing country so requests, include at least one panelist from a developing country member; (d) in the context of consultations involving a measure taken by a developing country, the parties may agree to extend the periods set for establishment of panels; (e) where one or more of the parties is a developing country, the panel's report will explicitly indicate the form in which account has been taken of relevant provisions on differential and more favourable treatment for developing countries under the covered agreements; (f) in surveillance of implementation of recommendations and rulings particular attention should be paid to matters affecting the interests of developing countries with respect to measures which have been subject to dispute settlement; (g) if the case is brought by a developing country, the Dispute Settlement Body, in considering what appropriate action might be taken, will take into account not only the trade coverage of measures complained of, but also their impact on the economy of developing countries concerned; (h) at all stages of the determination of the causes of a dispute and of dispute settlement procedures involving a least developed country, particular consideration will be given to the special situation of least developed countries, including the exercise of due restraint by the complaining party, and the offer of good offices, conciliation and mediation by the WTO Director-General or the Chairman of the Dispute Settlement Body.

### 4. "Best endeavour clauses"

Agreement on Agriculture: (a) in implementing commitments on market access, developed countries will take fully into account the particular needs and conditions of developing countries by providing for a greater improvement of opportunities and terms of access for

<sup>22</sup> Such measures include: (a) investment subsidies which are generally available to agriculture; (b) domestic support to producers to encourage diversification from the growing of illicit narcotic crops; and (c) agricultural input subsidies, whether in cash or kind, provided to low-income or resource-poor producers, defined using clear and objective criteria, and which are available to all producers meeting these criteria;

<sup>23</sup> These disciplines stipulate that when a member institutes any new export prohibition or restriction on foodstuffs in accordance with Article XI of GATT 1994, it shall (a) give due consideration to the effects of such prohibition or restriction on importing members' food security, and (b) before imposing such a measure, give notice in writing to the Committee on Agriculture containing information on the nature and the duration of the measure concerned and shall consult, upon request, with any other member having a substantial interest as an importer with respect to any matter related to the measure in question.

agricultural products of particular interest to these countries, including the fullest liberalization of trade in tropical agricultural products and products of particular importance to the diversification of production from the growing of illicit narcotic crops. Account may also be taken of concessions and other liberalization measures implemented by developing countries.

**Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least-Developed and Net Food-Importing Developing Countries:** appropriate mechanisms will be established to ensure that the implementation of the results of the Uruguay Round on trade in agriculture does not adversely affect the availability of food aid at a level which is sufficient to continue to provide assistance in meeting the food needs of developing countries, especially least developed and net food-importing developing countries. It is envisaged that the provisions of the Decision will be subject to regular review by the Ministerial Conference.

**Agreement on Textiles and Clothing:** meaningful improvement in access will be provided to those countries whose exports were subject to restrictions on the day before the entry into force of the WTO Agreement and whose restrictions represent 1.2 per cent or less of the total volume of the restrictions applied by an importing country. Least developed countries will be accorded treatment significantly more favourable than that provided to other groups. Small suppliers will be accorded differential and more favourable treatment in the fixing of restraint levels. In the case of wool-producing developing countries, special account will be taken of their export needs when quota levels, growth rates and flexibility are being considered.

**Agreement on Anti-Dumping:** special regard should be given by developed countries to the special situation of developing countries when considering the application of anti-

dumping measures. Possibilities of constructive remedies provided by the Code will be explored before applying anti-dumping duties where they might affect the essential interests of developing countries.

**Agreement on Import Licensing Procedures:** in considering the import performance of the applicant when allocating non-automatic import licences, special consideration should be given to those importers that import products originating in developing countries, in particular the least developed countries.

**Agreement on Subsidies and Countervailing Measures:** upon request by an interested developing country, the Committee on Subsidies and Countervailing Measures will undertake a review of a specific countervailing measure applicable to this developing country.

**Agreement on TRIPs:** developed countries will provide incentives to enterprises and institutions in their territories for the purpose of promoting and encouraging technology transfer to least developed countries.

## **5. Provisions on technical assistance**

Technical assistance for developing countries is envisaged in the following agreements and understandings: Understanding on the Balance-of-Payments Provisions of the GATT 1994; Agreement on the Application of Sanitary and Phytosanitary Measures; Agreement on Technical Barriers to Trade; Agreement on Implementation of Article VII of the GATT 1994 (Customs Valuation); Agreement on Preshipment Inspection; Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs); Understanding on Rules and Procedures Governing the Settlement of Disputes, and the Trade Policy Review Mechanism.

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## **C. Specific provisions related to developing countries in the General Agreement on Trade in Services (GATS)**

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In general, GATS recognizes the particular needs of the developing countries, and especially the least developed among them, and endeavours to facilitate their increasing participation in international trade in services and the expansion of their service exports, *inter alia*, through the strengthening of their domestic

services capacity and its efficiency and competitiveness. In this context, GATS provides for the increasing participation of developing countries in world trade in services through negotiated specific commitments related to the strengthening of domestic services capacity, *inter alia*, through access to

technology on a commercial basis, improved access to distribution channels and information networks, and the liberalization of market access in sectors and modes of supply of export interest to them.

In addition, GATS requires the developed countries (and to the extent possible other WTO members) to establish special contact points within two years from the date of entry into force of the WTO Agreement to facilitate the access of developing countries' service suppliers to information related to their respective markets concerning commercial and technical aspects of the supply of services; the registration, recognition and obtaining of professional qualifications, and the availability of services technology.

Particular account will be taken of serious difficulties faced by the least developed countries in accepting negotiated specific commitments.

In its provisions on economic integration, which are equivalent to Article XXIV of GATT, GATS gives more flexibility to developing countries parties to agreements liberalizing trade in services to reflect a wider process of economic integration or trade liberalization among the countries concerned. Any WTO member may enter into such an agreement on condition it has substantial sector coverage and provides for the absence or elimination of substantially all discrimination. In the case of an agreement involving only developing countries, more favourable treatment may be granted to juridical persons owned or controlled by na-

tural persons of the parties to such an agreement.

On the issue of subsidies, GATS provides for future negotiations with a view to developing the necessary multilateral disciplines to avoid the possible trade-distortive effects of subsidization. Such negotiations will be required to recognize that such negotiations should recognize the role of subsidies in relation to the development programmes of developing countries and take into account the needs of WTO members, particularly developing country members, for flexibility in this area.

GATS stipulates that the process of progressive liberalization of trade in services through successive rounds of negotiations should take place with due respect for national policy objectives and the level of development of individual WTO members, both overall and in individual service sectors. In addition, appropriate flexibility will be accorded to individual developing countries for opening fewer sectors, liberalizing fewer types of transactions, progressively extending market access in line with their development situation and, when making access to their markets available to foreign service suppliers, attaching conditions aimed at achieving the objectives established in Article IV of GATS. Special treatment of the least developed countries in these negotiations will also be envisaged.

GATS establishes that the WTO Secretariat will provide technical assistance to developing countries.

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## D. The case of the least developed countries

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In addition to special provisions in the various agreements, the Ministers at Marrakesh adopted a Decision on Measures in Favour of Least-Developed Countries, which adds operational content to those provisions. In this Decision, recognition is given to the need to ensure the effective participation of this category of countries in the world trading system and their specific need for continued preferential access to markets as an essential means of improving their trading opportunities. Most importantly, the Decision allows the least developed countries, as long as they remain in that category, flexibility to undertake commitments and concessions solely to the extent consistent with their individual development, financial and trade needs, or their administrative and institutional capabilities provided they

comply with the general rules set out in the various instruments. In this spirit, the Decision grants the least developed countries an additional time of one year from 15 April 1994 to submit their schedules as required in Article XI of the WTO Agreement.

In examining the provisions in some of the agreements relating to specific, differential and more favourable treatment for the least developed countries, their overall impact can be gauged by identifying the form they take.

The least developed countries have been granted longer transitional periods before assuming obligations for those agreements where the level of obligations is the same for all the members. Where this is the case, the intention

would seem to be to allow for the preparation of the necessary implementing legislation and/or the rectification of inconsistent legal and administrative practices. This applies particularly to the Agreement on TRIPs and, to a lesser extent, the Agreement on TRIMs. Certain provisions exempt the least developed countries from specific obligations as long as they remain in that category. This applies to the exemptions from the reduction commitments in the agricultural reform programme and to the exemption from the obligation prohibiting export subsidies contingent upon export performance in the Agreement on Subsidies. Yet another set of provisions caters for time-limited derogation from specific obligations after which the least developed countries assume the same level of obligations as all other members. A case in point is the prohibition of subsidies granted contingent upon the use of domestic over imported goods (local content requirement), which will not apply to the least developed countries for eight years following the date of entry into force of the WTO Agreement.

The Ministerial Decision on Measures in Favour of the Least-Developed Countries opens the way for a review, in the appropriate WTO Councils and Committees, of the transitional provisions applicable to these countries in the various agreements of the Uruguay Round. It must be noted, however, that the decision-making procedures under the WTO require a consensus for waivers concerning transitional periods or a period for staged implementation of an obligation which has not been carried out at the end of the granted period.

In the Uruguay Round the least developed countries, and indeed all developing countries, sought to introduce maximum flexibility into the various agreements to allow for (a) undertaking commitments commensurate with their capacity to implement them, (b) the use of various policy instruments to respond to needs peculiar to their level of development, and (c) building domestic capacities in critical areas that would gradually enable them to draw benefits from the trading system commensurate with their overall obligations. Guided by these criteria, the least developed countries obtained specific provisions in the Agreement on Agriculture whose effect would be to encourage domestic food production and rural development as an integral part of their development programmes. Similarly, the TRIMs Agreement, by permitting deviation from GATT Articles III and XI to the extent allowed by Article XVIII in respect of prohibited TRIMs, the least developed countries would retain flex-

ibility in resorting to otherwise prohibited trade-related investment measures.

GATS constitutes a unique case in that, in Article IV, it imposes a contractual obligation on members to give priority to the least developed countries when taking specific capacity-building measures to increase the participation of developing countries in world trade in services. These measures can be given effect only when included in the schedules of concessions of developed countries through the deliberate negotiating efforts of the least developed countries.

Commitments by developed countries oriented towards capacity-building in favour of the least developed countries are also to be found in the Agreement on TRIPs. Under Article 66, the developed countries are required to provide incentives to enterprises and institutions in their territories for the purposes of promoting and encouraging technology transfer to least developed countries to enable them to create a sound and viable technological base. However, other than the transitional period to allow them to bring their legislation into conformity with their obligations and several "best endeavour clauses", there are no special provisions in favour of the least developed countries in the TRIPs Agreement. It is thus a uniquely "development-neutral" agreement to the extent that the obligations take little account of different levels of development. This may be explained by the overriding objectives pursued in the negotiations of achieving a universal set of standards and norms for the protection of intellectual property rights and of providing an effective universal enforcement regime.

Capacity-building measures in favour of the least developed countries take the form of technical assistance which in most cases is focused on assisting these countries in the preparation of laws and regulations for compliance with the obligations established in the various agreements. This applies, for example, to the TRIPs Agreement, the Agreement on Preshipment Inspection, the Agreement on the Application of Sanitary and Phytosanitary Measures and some of the revised Tokyo Round Codes which are part of the Multilateral Agreements on Trade in Goods in Annex IA to the WTO Agreement.

The Ministerial Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least-Developed and Net Food-Importing Developing Countries recognizes that, in the short to medium term, reduced production in developed countries and the lags in expanding agricultural production in

developing countries could lead to higher world food prices. In order to mitigate the ensuing hardships and ensure acceptable levels of essential imports for these countries, food aid in grant form combined with financial and technical assistance for improving agricultural productivity and infrastructure are envisaged during the implementation of the agricultural reform commitments. The impact of the implementation of these commitments will be regularly monitored by the Committee on Agriculture.

Measures to offset the anticipated negative impact of trade liberalization in the case of agriculture seem to be an innovative way not only to ensure a balance in the outcome of negotiations but also to operationalize and give concrete meaning to the principle of special and differential treatment.

Acceptance of the entire results as a single undertaking has signified a major sacrifice on the part of the least developed countries that has nevertheless been necessary for the credibility of a multilateral trading system that must ensure the integration of these countries into its mainstream. In accepting the entire Uruguay Round package, these countries have assumed important commitments relative to their level of development, some of which only a few years ago had hardly been acceptable even to industrialized countries. A few of them are worth citing here:

- increased scope of tariff bindings and establishment of a tariff schedule on goods as a requirement for becoming an original member of the WTO;
- acceptance of tighter disciplines in the application of balance-of-payments measures, which entails giving preference to price-based measures as opposed to quantitative restrictions;
- acceptance of the general obligations in GATS, including the establishment of schedules on initial commitments on services as a condition for obtaining original membership in the WTO;
- acceptance of the same level of obligations as all other countries in respect of the Agreement on TRIPs, extending the scope of protection to new areas of intellectual property never covered before by their national IP regimes;
- acceptance of multilateral disciplines in the use of investment measures inconsistent with GATT Articles III and XI, including notification of such measures;
- increased transparency in their trade policies, particularly through the Trade Policy Review Mechanism.

Although a positive shift can be observed in the treatment of the concerns of the least developed countries from statements of principles and the "best endeavour" type of measure to action based on contractual and measurable obligations subject to review, the impact of the relevant provisions in favour of the least developed countries in various agreements should be assessed against the criteria governing the changes in their share of the growth of international trade during the implementation phase. The translation of these provisions into opportunities that enhance these countries' domestic capacities to overcome export supply constraints will be crucial for their participation in such growth. The flexibility allowed to them in complying with the obligations is intended to ensure that the latter do not in themselves act as a constraint to the success of this effort. The crucial question in the post-Uruguay Round phase is whether the least developed countries possess, or will be in a position to create, the means necessary to take maximum advantage of the relevant provisions for special and differential treatment.

The least developed countries are expected, within recognized limitations, to respect the multilateral trade rules which they have accepted and from which they stand to gain more as the weakest trading partners. As long as they remain in this category, however, it is imperative for these rules to provide for continued support not only in improving market conditions for them, but, what is equally important, in creating domestic capacities with the assistance of the international community, including international organizations, in the following areas:

- development of natural endowments to add more local value to exports, expand the export base and diversify their exports;
- strengthening of their technological capacities;
- promotion of subregional and regional trade;
- promotion of foreign and domestic private direct investment.

This implies, therefore, that in addition to the provisions for differential and more favourable treatment in their favour, complementary measures must be envisaged by the international community in order to (a) gradually enhance their capacity to draw benefits from trade liberalization; (b) mitigate the adverse effects and overcome the limitations on their development options caused by some of the disciplines in the various agreements; (c) lighten the burden of adjustment to the new

### SPECIAL SITUATION FACING AFRICAN COUNTRIES

Although most of the trade of African countries enjoyed duty-free access or faced tariff rates between 0 and 5 per cent in their major export markets either under the GSP or Lomé Convention arrangements, in the Uruguay Round they attached importance to trade liberalization, which would put market access on a more predictable basis while enabling them to progress in dealing with tariff escalation and removal of the tariff peaks to which some of their products were still subjected. In subscribing to the objective of trade liberalization it was quite clear to them that further reduction of MFN tariffs for the products that benefited from preferential access would inevitably result in a loss of their margin of preference and a possible loss of competitiveness. This concern was voiced by African countries sufficiently early in the market access negotiations to secure offsetting market access concessions from their trading partners.

It has become evident from the analysis of the new market access conditions resulting from the Round that erosion of preferences has actually taken place and is most significant in the case of tropical products followed by natural resource-based products. On a trade-weighted basis the average overall loss is 50 and 60 per cent in GSP margins for the two product sectors respectively in the three major markets of the EU, Japan and the United States. In the case of ACP margins, the loss is somewhat less - 30 and 16 per cent - reflecting a comparatively lower overall average percentage cut in MFN tariffs by the EU in the products of interest to African countries in these sectors. The overall averages, however, mask significant differences in individual products in which the erosion of preferential margins could be as high as 100 per cent, for example, for coffee and cocoa beans in the case of ACP margins under the EU preferential access provided for in the Lomé Convention.

The relatively greater concern on the part of African countries for the losses incurred in respect of preferential tariff margins is explained by their high dependence on exports of tropical and agricultural products, which account for a significant share of their export trade. The share of seven categories (which formed the basis of the negotiations on market access liberalization in this sector) of tropical products in total merchandise exports ranges from 50 per cent to 100 per cent for the majority of these countries. Erosion of preferential margins, which offer them a competitive edge in the market, has a greater impact on their overall export earnings due to their narrow export base, limiting their gains in improved access in other categories of products.

The impact of the reform programme envisaged in the Agreement on Agriculture would seem to be of much greater concern to African countries as the great majority of these are both net food-importing countries and least developed countries. A reduction or elimination of agricultural support and protection in the industrialized countries could have a dynamic impact on the development of agricultural production in African countries, and could provide the latter with an opportunity to expand their foreign exchange earnings from their agricultural exports in the longer run. However, in the short to medium term, because of reduced production in developed countries and lags in expanding agricultural production in developing countries, world food prices can be expected to rise. While such a rise could be beneficial in the long run, by making food production in food-deficit African countries more attractive, in the short run it would bring hardship to many African countries that are net importers of food. High food prices would increase pressure on the balance of payments of many food-deficit countries, with serious consequences not only for their debt repayment capacity and their ability to maintain essential imports at adequate levels but also for the well-being of the poor, whose food intake is already inadequate.

The challenge that African countries are likely to face in adjusting to the new competitive global market environment and sustaining a reasonable level of export income makes an even stronger case for technical and financial assistance from donor countries and international agencies for the short-term financing of commercial food imports and for the improvement of agricultural productivity and infrastructure in these countries.

In measuring the impact of the Round, and in order to keep the potential benefits of trade liberalization, African countries have to look beyond the short term. Africa, with the largest concentration of LDCs in the world, will need to transform its production and trade structures in order to face the challenge from an increasingly competitive global market environment as a result of trade liberalization. Competitive advantage in major export markets of African countries cannot be shielded permanently by preferential tariff margins, as has become evident from the

**Box 1 (concluded)**

market access outcome of the Uruguay Round. While intensifying the use of the existing preferences and seeking to deepen them where there is scope to do so, deliberate domestic policy actions will nevertheless have to be geared to improving the long-term international competitiveness of these countries' exports of goods and services. A set of policy actions could be focused on a number of priority areas: services infrastructure; development to support production and trade; technological capacity-building to improve quality and supply capabilities; diversification to higher value-added production through processing; improvement of investment conditions and the strengthening of regional and subregional markets. The support of the international community to complement domestic efforts in all these and related areas will be essential.

International efforts to enlarge the economic space for African countries will be determined to a large extent by the success of measures to integrate them into the international trading system and in no small measure by the success of trade and economic reforms now under way in those countries. This would require measures that go beyond those contained in the provisions on differential and more favourable treatment in the Final Act Embodying the Results of the Uruguay Round.

requirements in the multilateral trading system, including the new market access conditions resulting from erosion of the margin of preferences (see box 1).

In this context, the following measures could be envisaged by the international community:

- improvement of the GSP schemes through the widening of product coverage to include all products of export interest to the least developed countries, provision being made for deeper tariff cuts where tariff peaks remain in such areas as in textiles, processed food and beverages (where the problem of tariff escalation prevails), leather, wood and fisheries products;
- further liberalization of the rules of origin and elimination of the remaining non-tariff barriers to their imports;
- increased technical and financial assistance to improve their agricultural productivity and infrastructure;
- concrete action in the relevant international forums towards more vigorous debt relief measures;
- consideration to be given by aid donors and international financial institutions in their aid programmes to the special development, financial and trade needs of the least developed countries, with a view to ensuring that the economic and trade policy reforms of the latter are socially and economically sustainable through an appropriate blend of adjustment and external financing.

In implementing the results of the Uruguay Round, the least developed countries face a dual challenge. On the one hand, they need to strengthen their institutional and human resources capacities so as to be able to prepare implementing legislation to manage the complex set of agreements while, on the other, they need to maximize the opportunities offered by the various provisions of the Uruguay Round agreements.

## **E. The case of economies in transition**

Certain of the WTO Agreements embody provisions to take specific account of the special situation of economies in transition. Thus, the Agreement on Subsidies and Countervailing Measures contains, in Article 29, positive and flexible provisions for signatories "in the process of transformation from a centrally-planned

into a market, free enterprise economy" to apply programmes and measures necessary for such a transformation during a transitional period (including, in principle, prohibitive types of subsidies).

In addition, Article 65:3 of the Agreement on TRIPs provides that economies in transi-



tion, in addition to developing countries, may benefit from a period of delay of five years in all in the implementation of this Agreement, with certain exceptions.

In GATS, Article XII on restrictions to safeguard the balance of payments recognized

that a member in the process of economic development or economic transition may necessitate the use of restrictions to ensure, *inter alia*, the maintenance of a level of financial reserves adequate for the implementation of its programme of economic development or economic transition. ■

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## Annex 2 to chapter I

## THE URUGUAY ROUND AND REGIONAL FREE TRADE AGREEMENTS

In parallel to the GATT negotiations, many countries entered into negotiations aimed at the establishment or extension of regional trading arrangements. While the process of regional integration continued in Western Europe, the most significant development was the formation of the Canada/United States Free Trade Area (FTA) (later, with the inclusion of Mexico, to become the North American Free Trade Agreement (NAFTA)), given that the first two countries had traditionally been the main proponents of multilateral approaches. The Agreement on the European Economic Area (EEA) extended the scope of most of the integration instruments of the European Community to cover relations with those EFTA countries which chose to join the Area. The Canada/United States Free Trade Area Agreement (FTA) set out a detailed contractual framework for trade relations between the two countries, previously governed by GATT, which, in addition to tariff reductions, established provisions on the liberalization of trade in agricultural products and on services and investment, and set up special conciliation and judicial review procedures. The enlargement of this agreement in NAFTA resulted in the inclusion of provisions on intellectual property, labour rights and environment, health and sanitary regulations and additional provisions on services.

At the same time, regional agreements among developing countries have expanded and intensified. Impetus has been provided by the structural adjustment programmes applied by the majority of these countries which have led to the dramatic liberalization of import regimes. In this context, many developing countries have adopted the strategy of proceeding as far as possible with the liberalization process within the existing regional agreements, breathing new life into those that had become

moribund by including new issues on the multilateral negotiating agenda such as services. As a result, since 1990 most economic integration groupings of developing countries have revised their integration strategies, programmes and instruments, and new agreements have been negotiated so that the majority of developing countries are now members of at least one regional/subregional integration arrangement. One of the principal aims of such revisions has been the strengthening of market integration processes, albeit as part of an all-embracing approach which includes the strengthening of monetary and financial cooperation, functional cooperation such as infrastructure development, production development and social and political cooperation. This trend is quite pronounced in Latin America and the Caribbean where bilateral and plurilateral integration arrangements are being developed (see box 2).<sup>24</sup>

The countries in transition in Central and Eastern Europe have also adopted an active approach to regional cooperation. This approach has two dimensions: integration with Western European countries and integration among those countries themselves. The former category includes the association agreements with the EU, the free trade agreements between those countries and the members of EFTA, and the free trade agreements-between the Baltic and Nordic countries. The Central European Free Trade Agreement (CEFTA) and the Free Trade Agreement among the Baltic countries represent the intraregional integration. The members of the Commonwealth of Independent States (CIS) have also been in negotiations to establish a free trade area, and a model agreement has been elaborated in this regard.

The tendency toward the acceleration and intensification of regional agreements in the

<sup>24</sup> See, e.g. the report by the UNCTAD secretariat, "Follow-up to the recommendations adopted by the Conference at its eighth session: Evolution and consequences of economic spaces and regional integration processes" (TD/B/40(1)/7), 23 July 1993, chaps. III and IV.

## Box 2

## REGIONAL TRADING ARRANGEMENTS AMONG DEVELOPING COUNTRIES

Regional preferential trading arrangements among developing countries were examined in the GATT Committee on Trade and Development, in the light of the relevant provisions of the Enabling Clause agreed in the Tokyo Round.<sup>1</sup> The criteria for regional or global arrangements among developing countries for mutual reduction or elimination of tariffs, and under the conditions that may be prescribed by the participants for the mutual reduction or elimination of non-tariff measures on products imported from one another are that these arrangements:

- shall be designed to facilitate and promote the trade of developing countries and not raise barriers to or create undue difficulties for the trade of any other contracting parties;
- shall not constitute an impediment to the reduction or elimination of tariffs and other restrictions to trade on a most-favoured-nation basis;
- shall in the case of such treatment accorded by developing contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries.

These provisions clearly offer more flexibility than the provisions of Article XXIV and, in particular, those of the Understanding on the Interpretation of that Article.

There has, however, already been one exception to this procedure. It was agreed, after an extensive exchange of differing opinions in GATT, that the MERCOSUR Agreement<sup>2</sup> will be examined in a working party established by the GATT Committee on Trade and Development, but with the following terms of reference: "To examine the Southern Common Market Agreement (MERCOSUR) in the light of the relevant provisions of the Enabling Clause of the General Agreement, including Article XXIV, and to transmit a report and recommendations to the Committee for submission to the contracting parties, with a copy of the report transmitted as well to the Council". The examination under Article XXIV as well was insisted upon by a number of developed contracting parties in view of MERCOSUR's size and potential impact. In this context, many developing countries stated that this kind of procedure should not constitute a precedent for the examination of free trade arrangements among developing countries.

1 Decision of 28 November on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries.

2 The Treaty of Asuncion for the Formation of a Southern Common Market, signed in March 1991 between Argentina, Brazil, Paraguay and Uruguay.

1980s was provoked, to a certain extent, by frustration with the apparent difficulties of achieving multilateral liberalization in such sectors as agriculture, as well as with inefficiencies in the GATT dispute settlement mechanism, and the perceived need to establish rules and effective procedures to deal with the problems that would arise in the context of their extensive trade and economic relations. This resulted in the negotiation, in NAFTA and agreements among developing countries, of provisions which anticipated the results of the Uruguay Round in areas such as trade in services, TRIMs and TRIPs. The expansion and extension of regional arrangements created an impetus to form competing agreements. Regional "economic spaces" were seen as a way of providing firms with incentives to adjust to more competitive environments and prepare themselves to compete more effectively in the

world market. Some contained provisions on safeguards, rules of origin, etc., which led to increased discrimination against non-members' trade and investment. Smaller countries viewed regional agreements as an insurance policy against a breakdown of the multilateral system. Important differences with respect to the political basis for these agreements, the EEA for example, reflected a commitment to intensified political integration, while NAFTA was intended to have a strictly economic character. Other initiatives, such as APEC, did not contain trade commitments but established mechanisms for intensive technical cooperation at a regional level on trade-related matters.

This tendency gave rise to conflicting views about the interrelationships and implications of regional trading arrangements with and for the multilateral trading systems as a whole, i.e. as to whether regional agreements

constituted "building blocks" or "stumbling blocks" in the process of strengthening the multilateral trading system. The positive thesis, postulated by the proponents of these agreements, is that regional trading arrangements are essentially trade creating and would enable the participants to move more closely and quickly to free trade than could be expected at the multilateral level. Firms will become more competitive and thus inclined to promote further liberalization at the multilateral level. In addition, the intensive trade flows and economic relations among the partners in many of these agreements called for stronger disciplines over a wider range of subjects than were available in GATT, in order to provide for more secure access to markets and a less cumbersome mechanism for defusing trade tensions and for the conciliation of trade disputes. The results of the Uruguay Round show that many issues solved at the regional level have also become subject to liberalization and trade rules in the new multilateral agreements (Agriculture, Services, TRIPs), thus giving credence to the "building blocks" agreement.

However, an opposing view also emerged which considered regionalism to be a serious threat to the GATT system. According to this belief, regionalism will result in inward-looking, discriminatory and protectionist trading "blocs", centred around major powers competing for "spheres of influence"; it could seriously undermine the MFN principle of GATT and result in trade diversion instead of trade creation. Proponents of this view sought a substantial result from the Uruguay Round in terms of trade liberalization and the strengthening and extension of multilateral disciplines. The proliferation of regional agreements with certain countries that are members of several at once, and the extension of the scope of the agreements to areas not covered by GATT also gave rise to concerns with respect to the adequacy of the provisions of GATT Article XXIV to address the issue raised in these agreements. This led to the negotiation of the Understanding on the Interpretation of Article XXIV (see box 3).

In parallel, the results of the negotiations on services have been that the General Agreement on Trade in Services (GATS) allows its members to participate in economic integration arrangements aiming at liberalizing the trade in services provided that such arrangements are compatible with conditions analogous to those in Article XXIV. Members may also be a party to an agreement establishing full integration of the labour market, provided that such an arrangement exempts citizens of parties to the agreement from requirements concerning the residency and work permits of persons supply-

ing services. By the same token, however, discrimination in favour of regional partners will be reduced or removed for service sectors and subsectors included in their Schedules of Commitments annexed to GATS.

The concern of the international community with regional trends was reflected in paragraph 146 of the Cartagena Commitment which requested the Trade and Development Board to review, *inter alia*, the implications of the regional free trade areas and integration agreements for the international trading system. In this context, the UNCTAD secretariat has made a comparative analysis of the provisions with respect to key trade issues and sectors in the Final Act of the Uruguay Round, the North American Free Trade Agreement (NAFTA) and the Agreement on the European Economic Area (EEA). This comparison assessed the extent to which the rules and mechanisms in the two regional agreements were consistent with the Uruguay Round Agreements, the thesis being that to the extent they are consistent they can be "dissolved" in the multinational trading system and, hence, can be considered as building blocks of the system. On the contrary, when they introduce conflicting approaches and mechanisms, progress in strengthening the international trading system could be hampered. The analysis also pointed out direct interrelationships between the Uruguay Round results and the provisions and rules of these regional agreements, and the implications of the results for such agreements.

In general, the three agreements establish rights and obligations and procedures that are much more precise and detailed than those in GATT 1947 or in previous free trade agreements. They also extend to areas which go beyond traditional trade policy measures and mechanisms, and are designed to provide more discipline and security in the spectrum of issues in trade and economic cooperation relations among the participating countries.

One important distinction between the EEA Agreement, on the one hand, and NAFTA and the Uruguay Round Agreements, on the other, is that they are based upon different political and institutional characteristics, which have implications for their relationships with the multilateral trading system. Both the former have established a free trade area and cover roughly the same trade issues, although the EEA Agreement goes even further by establishing the free movement of goods, services, capital and labour. But the EEA Agreement and its operation have been largely designed to harmonize with the laws, rules, mechanisms and institutions of the European Union. The

## Box 3

## UNDERSTANDING ON THE INTERPRETATION OF ARTICLE XXIV OF GATT 1994

"GATT consistency" basically implies that regional agreements must be bona fide customs unions or free trade areas covering substantially all trade among the parties concerned, and not merely loose preferential arrangements. Although Article XXIV:5 of GATT provides that the duties and regulations of commerce shall not be made higher or more restrictive,<sup>1</sup> the economic (e.g. trade-diverting) impact of the regional agreements is not examined. Article XXIV also provides a negotiating framework for compensating countries whose contractual rights are affected by customs unions. These criteria have proved less adequate today when both the regional agreements and the multilateral system itself are extensively covering many more trade and economic policy instruments than the traditional trade policy mechanisms of customs tariffs and other frontier measures. For that reason, consistency with Article XXIV of the GATT would seem to be less of an issue than the "compatibility" of regional arrangements with the emerging multilateral trading system as reflected in the Uruguay Round agreements.

The Understanding on the Interpretation of Article XXIV of GATT 1994 recognizes, *inter alia*, that the contribution of free trade areas and customs unions to the expansion of world trade is increased if the elimination between the constituent territories of duties and other restrictive regulations of commerce extends to all trade, and diminished if any major sector of trade is excluded. Further, it is reaffirmed that the purpose of these arrangements is to facilitate trade between the constituent territories and not to raise barriers to the trade of other members with such territories, and that in their formation or enlargement the parties to them should to the greatest possible extent avoid creating adverse effects on the trade of other members.

This Understanding introduces for the first time an examination of the economic impact of regional agreements. As in other areas of the Uruguay Round, links between multilateral obligations and measurable economic criteria have been established.

The most important provisions are: (a) the evaluation under Article XXIV:5(a) of the general incidence of the duties and regulations of commerce applicable before and after a formation of a customs union shall be based upon an overall assessment of weighted average tariff rates and of customs duties collected; (b) the "reasonable length of time" referred to in Article XXIV:5(c) should exceed 10 years only in exceptional cases; (c) tariff negotiations under Article XXIV:6 and Article XXVIII concerning increases of bound rates involving a member forming a customs union have to start before tariff concessions under the customs union enter into force. These negotiations will take place with a view to achieving mutually satisfactory compensation from the customs union through reductions of duties on the same or other tariff lines.

The Understanding imposes no obligations to provide compensatory adjustment to the constituents of a customs union. Notification procedures under Article XXIV:7(a) as well as periodical reporting as provided for in GATT 1947 are reaffirmed. The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Understanding on Rules and Procedures Governing the Settlement of Disputes may be invoked with respect to any matters arising from the application of those provisions of Article XXIV relating to customs unions, free trade areas or interim agreements leading to the formation of a customs union or free trade area.

1. For customs unions, the "general incidence" of such duties and regulations shall not be more restrictive.

EU institutions have supranational character and powers in both political and economic matters. The EEA legal framework and the bodies established under the Agreement will follow the same pattern operating closely with the EU institutions and courts.

NAFTA and the North American Agreements on Environmental and Labour Cooperation (side agreements) have no political or economic institutions with a supranational character and decision-making power.

NAFTA's procedures for the enforcement of its provisions and the settlement of disputes will be similar to those provided for in the multilateral trading system embodied in the WTO, which do not imply any supranational decision-making powers either. This means that NAFTA is enforced through consultations or dispute settlement mechanisms, based on recourse to panels, which operate under its provisions and the national laws of the countries concerned. The elements and basic procedures of the GATT Understanding on Rules

and Procedures Governing the Settlement of Disputes are thus comparable with those in NAFTA as, apart from differences in scope, and in certain areas and approaches, the main elements in both cases are consultations and settlement of disputes through panels and arbitration.

The most important principles underpinning the Uruguay Round agreements are MFN treatment and non-discrimination. However, differential and more favourable treatment for developing countries is granted in the majority of these agreements. NAFTA, and in particular the EEA Agreement, treat their members as equals and require reciprocity with very few (scheduled) exceptions. In the field of services, GATS emphasized balanced obligations among countries, while giving due respect to national policy objectives. The EEA Agreement, while based on the "acquis communautaire" and requiring harmonization of laws, rules and regulations and homogeneous surveillance, implementation and interpretation of the provisions in most areas of the Agreement, allows its members, in many cases, to maintain higher objectives and standards than GATS establishes in general.

In assessing whether regional agreements can constitute "building blocks" for a strengthened multilateral trading system, an essential consideration is the ease with which their provisions can be given a multilateral basis. Acceptance of the different instruments annexed to the WTO Agreement by over 100 members would seem to entail such multilateralization. The TRIPs Agreement, for example, would endow all the member countries with roughly the same degree of intellectual property protection. In the area of financial services, the acceptance of the Understanding annexed to GATS would significantly reduce the "regional" aspects of the agreements in question as would many of the offers in various service sectors included in the Schedule of Commitments.

The Uruguay Round has served to mitigate the forces of regionalism by significantly diluting the preferential aspects of regional agreements. The obligations of the Agreement on Agriculture go well beyond those provided in the EEA Agreement, which practically excludes the liberalization of trade in agriculture, and in NAFTA where certain scheduled quantitative restrictions are still permitted. However, NAFTA has a "GATT acquis" with regard to these restrictions. The results of the Uruguay Round in agriculture also have to be

taken into account in further efforts to liberalize trade in agriculture within the EEA. Both the Agreement on Agriculture and NAFTA have tariffication as a basis for the liberalization of this trade and provide for the gradual reduction of tariffs (Uruguay Round) or their total removal, in accordance with an agreed timetable (NAFTA).

Furthermore, the multilateral MFN tariff reductions, which average around 38 per cent, including in the countries which are members of NAFTA and the EEA, and their acceptance of the "zero-zero" option in sectors of considerable importance in their interregional trade (e.g. construction, medical and agricultural equipment, steel, beer, distilled spirits, paper, furniture) reduce or eliminate the margins of preference. Discrimination in favour of regional partners will also be reduced or removed for those sectors and subsectors that are included in the schedules of commitments annexed to GATS.

In view of the problems of calculating precise figures for the effective tariff reductions, the observations that can be made in this regard on the basis of the GATT secretariat's preliminary evaluation will be rather general.<sup>25</sup> In the case of the parties to NAFTA and to the EEA, the trade-weighted tariff averages for imports of MFN origin prior to the Uruguay Round were 9.0 per cent (Canada), 5.4 per cent (USA), 46.1 per cent (Mexico) and 5.7 per cent (EC), and an average of 6.1 per cent (the four EFTA members of the EEA).<sup>26</sup> After the implementation of the WTO Agreement, the respective trade-weighted average tariffs will be 7.1 per cent (Canada), 3.5 per cent (USA) and 33.7 per cent (Mexico); and 3.6 per cent (EC) and 4.0 per cent (EFTA members). The average reduction in the NAFTA region will thus be 36 per cent, and, in the EEA region, 35 per cent.

In addition, the average share of duty-free imports of MFN origin in the pre-Uruguay Round period was 16 per cent (Mexico, 0 per cent) in the NAFTA region and 32 per cent in the EEA. The post-Uruguay Round shares of duty-free imports will be 28 per cent (Mexico, 1 per cent) and 42 per cent, respectively. Thus, access for duty-free imports to Canada and the United States will double, and increase by three quarters in the EEA region. When the reduction in the tariff rate and the extension in duty-free access are added together, this will undoubtedly mean a significant reduction of preferential margins in these two free trade

<sup>25</sup> Source: GATT.

<sup>26</sup> Austria, Finland, Norway and Sweden. Iceland and Liechtenstein were left out of these figures because of the much higher average tariff for Iceland compared with the other four countries and the small share of both countries in trade.

areas. It has to be taken into account, however, that the four EFTA countries of the EEA may join the EU from the beginning of 1995, which can change the picture slightly when they have to adopt the common external EU tariff rates which are generally somewhat higher than the rates in force in these four countries.

The areas where the obligations are roughly the same in all three agreements are the protection of intellectual property rights and the provisions for sanitary and phytosanitary measures. The MFN clause in the TRIPS Agreement effectively multilateralizes the corresponding provisions in NAFTA and the EEA Agreement, as does the Agreement on Sanitary and Phytosanitary Measures (as well as certain provisions of the Agreement on Technical Barriers to Trade). There are also many references in both NAFTA and the EEA Agreement in these fields as to whether the whole regime or specific provisions could or should be modified in the light of the final results of the Uruguay Round. The TRIMs Agreement provides for a shorter transition period than NAFTA for the phase-out of local content requirements in the automobile sector.

As regards subsidies, both the EEA Agreement and the Agreement on Subsidies and Countervailing Measures introduce stringent provisions concerning the subsidization of industrial products. Definitions of prohibited and allowed subsidies are very detailed and similar in both cases. NAFTA makes little provision for subsidization as such, but countervailing duty measures can be applied in this context. The Uruguay Round Agreement, in those parts that are related to countervailing measures, will be the instrument for dealing with these issues in the context of NAFTA. The Agreement on Anti-Dumping will also provide a basis for action against regional partners in NAFTA. This will have implications for the relevant NAFTA provisions, which have the GATT "acquis" and which in certain cases allow the choice between NAFTA procedures and those provided for in the Uruguay Round Agreement to be settled through disputes arising from these measures. On the other hand, the latter provisions have little or no effect in the intra-EEA system which is based on competition policy regulations.

Although both NAFTA and, in particular, the EEA Agreement establish their own mechanisms to review the functioning of the agreements, and to evaluate and amend them, as well as to deal with trade problems and disputes, the references to the Uruguay Round

agreements and the possibilities in certain cases of applying the procedures provided therein will make for greater coherence between these regional agreements and the multilateral trading system.

The regional agreements examined here include provisions on areas that were not dealt with in the Uruguay Round. Environment-related trade measures are one example, and so are investment and competition policies. The EEA Agreement establishes fairly extensive disciplines in environment-related trade issues and measures. The North American Agreement on Environmental Cooperation, a "side agreement" to NAFTA, brings environment-related trade matters under rather stringent scrutiny and rules. Nevertheless, the growing consciousness concerning the interactions between trade and environmental measures, and the incidental inclusion of these issues in the two major regional agreements have resulted in specific preference being given to environmental concerns in a number of multilateral agreements embodied in the Final Act of the Uruguay Round.

In view of the increasing importance of the linkages between trade, environment and competition issues and policies, and the amount of attention that these matters now attract in various international forums, it seems obvious that the post-Uruguay Round agenda has to address such issues more profoundly at the multilateral level. In particular, the experiences of regional groupings in these fields should be taken into account since these issues are already linked to NAFTA and the EEA Agreement.

To sum up, it can safely be said that there is little in these regional agreements in question that would directly impede action at the multilateral level. On the contrary, the implementation of the Uruguay Round agreements would effectively multilateralize certain elements of the regional agreements and even go beyond them by diluting the rate of preferences granted within these arrangements. Several countries have proposed that UNCTAD should continue to examine the implications of regional agreements for the international trading system as a whole as a priority issue. In this context, at the Mid-Term Review of UNCTAD's work programme, conducted by the Trade and Development Board in May 1994, agreement was reached on the holding of a seminar on regional economic arrangements and their relationship with the multilateral trading system. ■



## PROBLEMS FACED BY THE COUNTRIES NOT CONTRACTING PARTIES TO GATT 1947: MAIN ISSUES INVOLVED

There were 125 participants in the final leg of the Uruguay Round, a large number of which had become contracting parties to GATT in the period since the Round was launched in 1986. Unlike the Tokyo Round, the Uruguay Round was open only to GATT contracting parties or those developing countries committing themselves to become so. Over 20 developing countries met the participation criteria for the Round by applying for GATT membership, and becoming GATT contracting parties during the Uruguay Round (see box 4 below). In the final phase of the Round, given that *de facto* GATT status could not be carried through into the WTO, a number of developing countries and territories became GATT contracting parties under Article XXVI:5(c) of GATT 1947, bringing the overall GATT membership to 123 contracting parties. Thus, the Uruguay Round has also contributed to the achievement of more universal GATT membership.

In addition, the Trade Negotiations Committee agreed in July 1993 that countries and territories that were negotiating their accession to GATT, but did not have the status of participant in the Uruguay Round, could associate themselves with the activities of the Round. By the end of the Round there were 19 acceding countries and territories in this category. As of 1 June 1994, 19 working parties on accession had been established, involving accession negotiations of such countries and customs territories as Bulgaria, Mongolia, Croatia, Panama, Slovenia, Taiwan province of China,<sup>27</sup> Saudi Arabia, Jordan, Nepal, the Baltic States and several CIS member States (Armenia, Belarus, Moldova, the Russian Federation and Ukraine).

Some of these countries would seem to be motivated to become original members of the WTO according to Article XI of the WTO Agreement, which stipulates that "the contracting parties to GATT 1947 as of the date of entry into force of this Agreement, and the European Communities, which accept this Agreement and the Multilateral Trade Agreements and for which Schedules of Concessions and Commitments are annexed to GATT 1994 and for which Schedules of Specific Commitments are annexed to GATS shall become original Members of the WTO". In this context, it should be noted that the WTO Agreement does not distinguish in any way between the WTO original members and those WTO members which would accede to it in accordance with the accession procedure in Article XII (see box 5).

Under the Marrakesh Ministerial Decision on Acceptance of and Accession to the WTO Agreement, the acceding countries are divided into four groups:

- (1) Any Signatory of the Final Act
  - to which paragraph 5 of the Final Act applies, or
  - to which paragraph 1 of the Decision on Measures in Favour of Least-Developed Countries applies, or
  - which became a contracting party under Article XXVI:5(c) of GATT 1947<sup>28</sup> before 15 April 1994 but was not in a position to establish a schedule to GATT 1994 and GATS for inclusion in the Final Act, and
- (2) any State or separate customs territory

<sup>27</sup> Designated in its application as Chinese Taipei, to be known in full as the "Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu", see *Focus, GATT Newsletter*, No. 94, October 1992.

<sup>28</sup> Countries which maintain a *de facto* application of GATT.

## Box 4

## CRITERIA FOR PARTICIPATION IN THE URUGUAY ROUND

The Punta del Este Declaration set the following criteria for countries to participate in the Round: Negotiations will be open to: "all contracting parties; countries having acceded provisionally; countries applying the GATT on a de facto basis having announced, not later than 30 April 1987, their intention to accede to the GATT and to participate in the negotiations; countries that have already informed the CONTRACTING PARTIES, at a regular meeting of the Council of Representatives, of their intention to negotiate the terms of their membership as a contracting party; and developing countries that have, by 30 April 1987, initiated procedures for accession to the GATT, with the intention of negotiating the terms of their accession during the course of the negotiations".

Source: GATT, *Multilateral Trade Negotiations of the Uruguay Round* (MIN.DEC), 20 September 1986.

- which becomes a contracting party to GATT 1947 between 15 April 1994 and the date of entry into force of the WTO Agreement may submit to the Preparatory Committee for its examination and approval a Schedule of Concessions and Commitments to GATT 1994 and a Schedule of Specific Commitments to GATS.

(3) The WTO Agreement shall be open for acceptance in accordance with Article XIV of this Agreement by contracting parties to GATT 1947, the schedules of which have been submitted and approved before the entry into force of the WTO Agreement.

(4) The above provisions of subparagraphs (1) (2) and (3) shall be without prejudice to the right of the least developed countries to submit their schedules within one year from 15 April 1994.

As compared to accession to GATT 1947, membership in the WTO requires the acceptance of all Multilateral Trade Agreements annexed to the WTO Agreement and of the schedules of concessions in the areas of goods and services. Thus, subsequent accession to the WTO is likely to be more complicated and demanding process given the wider scope and greater complexity of the obligations. Decisions on accession are taken by the Ministerial Conference which approves the respective agreements on the terms of accession by a two thirds majority of the members of the WTO. Accession to a Plurilateral Trade Agreement is governed by the provisions of that Agreement.

Paragraph 5 of the Final Act of the Uruguay Round provides that, for countries which participated in the Uruguay Round but are still negotiating their accession to GATT 1947, the Schedules of Concessions are not definitive, and will be subsequently completed for the purpose of the accession of these countries to GATT 1947 and their acceptance of the WTO Agreement. Further, those States or separate customs territories which were not participants in the Uruguay Round, but may become contracting parties to GATT 1947 before the entry into force of the WTO Agreement, will be given the opportunity to negotiate schedules to GATT 1994 and GATS to enable them to accept the WTO Agreement. There is also the case of countries or separate customs territories which would not complete the process of accession to GATT 1947 before the entry into force of the WTO Agreement or which do not intend to become contracting parties to GATT 1947. These will be able to initiate the process of their accession to the WTO before the entry into force of the WTO Agreement in accordance with the Marrakesh Ministerial Decision on Acceptance of and Accession to the WTO Agreement.

In addition, certain participants in the Uruguay Round, which had applied GATT 1947 on a de facto basis and became contracting parties under Article XXVI:5(c) of the GATT 1947 but were not in the position to submit schedules to GATT 1994 and GATS before 15 April 1994, may submit them to the WTO Preparatory Committee for its examination and approval.

The WTO Preparatory Committee will have an active role to play regarding those

## CHINA

China, which was participating in the Uruguay Round, was one of the 23 original contracting parties to the General Agreement, but withdrew from GATT in contentious circumstances in 1950. In 1982, China became an observer in GATT, and two years later became a party to the Multi-Fibre Agreement. In June 1986, China submitted a request to GATT to resume its status as a contracting party. This request has been under consideration by a Working Party since March 1987. In parallel, China has fully participated in the Uruguay Round.

The interest taken by GATT contracting parties in China's membership is apparent in the thousands of questions that participants in the Working Party have put to the Chinese authorities. Among the various concerns that have come to light in the course of the deliberations are concerns about transparency in China's trade regime, uniform administration of the trade regime, certainty as regards the treatment of imports (including the application of quotas, licences and standards), and the role of state-trading enterprises. On the other hand, China has resisted attempts to include, in its Protocol of Resumption, special provisions such as selective safeguard clauses that would impair its ability to enjoy full rights under GATT and the WTO, as well as those which would impose additional obligations, more onerous than those accepted by WTO members.

China has recently announced significant programmes of liberalization and reform, particularly those relating to the exchange regime, taxation, state trading, licensing, tariffs and non-tariff measures. These include, *inter alia*, the elimination of mandatory import and export plans, major tariff reductions on items of export interest to trading partners, increased transparency in its standards and inspection regime, and the phasing out by 1997 of quotas and licensing requirements on most categories of imports.

If the negotiations on resumption of China's contracting party status and verification of its Uruguay Round commitments, including those on market access in goods and services, are completed before the entry into force of the WTO, planned for early 1995, China would be eligible to become an original member of the new Organization at that time.

*Source: GATT Press Release (GATT/1633), 10 May 1994; Financial Times, 27 and 30 May 1994.*

countries for which working parties have already been established to examine their applications for accession to GATT 1947, in considering such cases jointly with the existing working parties. In particular, the Preparatory Committee will, upon a request from an acceding country or customs territory, initiate the process of accession to the WTO, and the relevant GATT Working Party will be requested to examine such cases of accession on behalf of the Preparatory Committee and to report to it.

### 1. WTO provisions on non-application

As in GATT 1947, the WTO Agreement provides for non-application between any member and any other member of the Agreement itself and MTAs in Annexes 1 and 2. However, this provision could be applied to

original WTO members only if Article XXXV of GATT 1947 had been invoked earlier and was effective at the date of entry into force of the WTO Agreement for the members concerned. It can be applied against a new WTO member only if the member not consenting to the application has so notified the Ministerial Conference before the approval of the terms of accession of the former. The Ministerial Conference may review the operation of the non-application provisions and make appropriate recommendations. Non-application of PTAs will be governed by their own provisions.

The non-application provision of the WTO Agreement does not permit sectoral non-application, and only "global" non-application may be invoked with regard to all Multilateral Trade Agreements, including dispute settlement rules and procedures. On the other hand, the WTO non-application clause is more flexible than Article XXXV of GATT 1947 in that it permits members to invoke the non-application provision even after engaging

## Box 6

## SLOVENIA'S ACCESSION TO GATT 1947/WTO

Slovenia, which started its accession process to GATT 1947 in 1992, is the first country that, having formally finalized these negotiations in June 1994, will apply immediately for accession to the WTO as an original member. There are also other particular provisions in the Report of the Working Party (WP) on the accession of Slovenia which could be illustrative for the accession negotiations of other countries.<sup>1</sup>

For example, the Report of the Working Party includes Slovenia's assurances that its trade policies, measures and relevant laws and regulations in such fields as state trading, non-tariff measures and quantitative restrictions, subsidies, anti-dumping and countervailing duties and safeguards, and preferential trading arrangements, are in conformity, or will be brought into conformity within specified timetables, with the respective GATT provisions. In addition, there is a large number of more specific commitments made by Slovenia concerning, *inter alia*, tariff levels and bindings, taxes, variable levies and tariff surcharges, application of various relevant technical regulations and measures, balance-of-payments restrictions, and adoption of MTN Codes. Thus, Slovenia agreed to bind its tariff for industrial products at an across the board ceiling level of 27 per cent. The same level of bindings, with some exceptions, will apply to tariffs on agricultural products.

Other matters which have become relatively dominant in Slovenia's accession negotiations are the issues of state trading, state participation and ownership, and privatization. Some members of the WP stated that the commitments and assurances reflected in the Report of the Working Party and in the Protocol of Accession should be restricted to the obligations embodied in GATT 1947. The Working Party noted the statements made by those countries that any assurances or commitments given by the Government of Slovenia which constituted obligations additional to those required by the General Agreement or relevant instruments under its auspices, did not constitute a precedent, either for future accessions or for other GATT negotiations or procedures. On the other hand, some other members of the WP stated that working parties on accession had a mandate to examine the foreign trade regime of an acceding government and define the conditions for accession; therefore, the working parties had to address all issues that appeared to be relevant to international trade relations. These countries noted that if a government pursued policies that would have an immediate effect on market conditions, including access thereto, it seemed reasonable for a working party on accession to seek a high degree of transparency in the implementation of these policies.

In connection with state-owned enterprises and privatization, Slovenia made specific commitments to submit an intended timetable for privatization under the relevant law, to provide detailed annual information on the implementation and completion of the privatization and ownership transformation processes, including details on the status of the international trade operations of state- and socially-owned enterprises that remain unprivatized. In this regard, some members of the WP reiterated that accession of any applicant country should not be made contingent upon undertakings relating to areas not covered by any provisions of the General Agreement, such as transformation of the economy, including ownership structure or privatization. The same kind of discussion is being held in the WP on the accession of Bulgaria and Mongolia, and is very likely to recur in other accession cases.

Finally, in accordance with paragraph 8(b)(i) of the Ministerial Decision of 14 April 1994 on Acceptance of and Accession to the Agreement Establishing the World Trade Organization (WTO), the Government of Slovenia indicated its wish to follow the procedures for membership in the WTO set out by the Preparatory Committee on 31 May 1994. The Working Party agreed that it would reconvene, under the terms of the Preparatory Committee mandate, to examine on its behalf the application of Slovenia and to initiate the required negotiations without delay. For these purposes, Slovenia would prepare a report on its trade regime in services, its initial offer as the basis on which to negotiate commitments concerning trade in services with a view to preparing its schedule to be annexed to GATS, and provide information on laws, regulations and procedures related to TRIPs. Other countries currently negotiating their accession to GATT 1947 are likely to follow the same kind of procedure.

<sup>1</sup> See, Report of the Working Party on the Accession of Slovenia, GATT document L/7492, 1 July 1994.

in full negotiations, including the conduct of negotiations on tariff concessions, with the acceding country. This gives rise to concern that the threat of non-application could be used by WTO members as additional leverage, to obtain greater concessions from acceding countries.

## 2. *The case of acceding economies in transition*

Countries in transition which are not yet contracting parties to the GATT face a complex internal and external situation which may complicate their accession procedures to the WTO. Thus, both the CIS member countries and the Baltic States are undergoing a fundamental transformation of their economies and societies into market-based systems in which integration into the international trading system plays an important role in overall economic strategies. These countries will undoubtedly require a certain degree of understanding from their trading partners in the accession negotiations in that they may need to be accorded some flexibility before their trade regimes take shape as a result of economic reforms and trade liberalization policies. For example, these countries' tariff regimes have only begun to develop compared to the tariffs of GATT contracting parties, and the approaches applied in the Uruguay Round to maximize tariff cuts and tariff bindings of all participants may not necessarily be applicable in such a case. The same considerations, although to varying degrees, may be relevant to accession by other countries (for example, Albania, Bulgaria, Croatia, and developing countries such as Mongolia and Vietnam).

On the other hand, when countries in transition began the transformation of their economies, their trade faced highly restrictive import and export regimes in major developed countries. These regimes discriminated against the trade of countries in transition in various ways, including the denial by certain countries of unconditional most-favoured-nation treatment, even to some Central and Eastern European countries which had become contracting parties to GATT. As a result of a substantial improvement in trade regimes, most countries in transition are now granted MFN treatment by major trading countries. Developed countries have also taken measures to further open their markets in favour of countries in transition, for example, within "Europe"

Agreements and EFTA Free Trade Agreements, and this has resulted in tariff reductions and liberalization of quantitative restrictions. Many of the economies in transition are receiving GSP treatment from some developed countries.

However, in spite of the progress achieved, economies in transition still face a number of non-tariff measures, including levies and quantitative restrictions, in major markets for agricultural products, textiles, clothing and other industrial exports. Some quantitative restrictions and import procedures are especially targeted at them. Furthermore, other residual elements of trade regimes previously applied to imports from these countries are still in force and remain an important obstacle to their integration into the international trading system:

- Selective (bilateral) safeguard clauses, which provide for emergency safeguard action to prevent injury to domestic producers, to be applied only against imports from only the country concerned and not all other suppliers as required by Article XIX of GATT. In addition, these clauses contain criteria for weaker action of that kind than the measures required by Article XIX of GATT and applied with respect to market-economy countries. In this context, the new Agreement on Safeguards represents a balanced instrument to deal with the situations that might arise in cases of imports from economies in transition.
- Special criteria for the imposition of anti-dumping and countervailing measures, based on prices in third countries with market economies or constructed values or even on domestic prices in the importing country of like products. Anti-dumping measures in particular are among the most frequent access barriers encountered by exporters from economies in transition in their major markets.

The efforts of these countries to become integrated into the international trading system on the basis of the Uruguay Round agreements through early accession to the WTO merit the full support of the international community. This process can be viewed as a major challenge for this new organization. In the WTO accession negotiations, economies in transition should be treated as normal trading partners, and trade relations with them should be based effectively on unconditional MFN treatment and the elimination of all residual elements of past discriminatory trade regimes applied against them (see box 6).■

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## AGREEMENT ON SAFEGUARDS

### A. Background

#### 1. Origin of the safeguard provision

The safeguard provision (Article XIX of GATT 1947) has its origins in proposals made at preparatory meetings convened in London and New York in 1946 and 1947 for the purpose of drafting a Charter for an International Trade Organization (ITO).

The first proposal to include such a provision in GATT was made by the United States in London in 1946.<sup>29</sup> The negotiators at those meetings agreed in principle on the need for a safeguard provision but their views diverged as to its proper scope. At the New York Meeting it was decided to include the proposed safeguard provision in the draft Charter for an ITO. Since the adoption in early 1948 of the Final Act of the Havana Conference, which was convened late in 1947 to establish the ITO, Article XIX of GATT has been amended only once, and then in a very minor way.<sup>30</sup>

#### 2. Conditions for invoking the safeguard provision

Under Article XIX of GATT, action can be taken "to suspend the obligation in whole or in part or to withdraw or modify the con-

cession" when the following criteria and conditions are met: as a result of "unforeseen" developments, the product in question is imported in such increased quantities and under such conditions as to cause or threaten "serious injury" to domestic producers of like or directly competitive products. The suspension of an obligation or the withdrawal or modification of a concession must be limited to the extent and the time necessary to prevent or remedy the injury caused or threatened. There are also important reporting, review and consultation requirements.<sup>31</sup>

#### 3. Problems of the safeguard provision

Article XIX is one of a number of so-called "safeguard" provisions of the General Agreement which enables contracting parties, subject to specific requirements, to impose trade restrictions that are otherwise prohibited.<sup>32</sup> It permits the imposition of higher tariff duties above bound rates or of quantitative restrictions, which are prohibited under Articles II and XI, against imports that "... cause or threaten serious injury to domestic producers". However, the use of Article XIX has been declining as more "safeguard" actions have been taken without reference to GATT

<sup>29</sup> See United States submission of a working proposal for a Charter, U.S. Department of State Pub. No. 2598, Article 29, at 22 (1946). Its proposal was modelled on the safeguard provision contained in its Reciprocal Trade Agreement with Mexico of 1942, which reads as follows: If, as a result of unforeseen developments and of the concession granted on any article enumerated and described in the Schedules annexed to this Agreement, such article is being imported in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers of like or similar articles, the Government of either country shall be free to withdraw the concession, in whole or in part, or to modify it to the extent and for such time as may be necessary to prevent such injury.

<sup>30</sup> GATT, *Analytical Index*, Sixth edition, 1993, p. 414.

<sup>31</sup> *Report on the Withdrawal by the United States of a Tariff Concession under Article XIX*, Geneva, November 1951 (Sales No. GATT/1951-3); see also GATT, *Analytical Index*, Sixth edition, 1993.

<sup>32</sup> Other GATT provisions for restricting imports are to be found in: Article VI, which provides for the imposition of anti-dumping and countervailing duties; Article XII, which permits the imposition of import restrictions for balance-

rules, and frequently in contravention of these, or under other GATT provisions such as Article VI which, unlike Article XIX, are intended to protect domestic producers from "unfair" practices such as dumping and subsidization. One of the principal means of avoiding the disciplines of Article XIX has been to negotiate bilateral export restraint arrangements (e.g. voluntary export restraints, orderly marketing arrangements, and price monitoring systems).<sup>33</sup> The danger for developing countries and other weaker trading partners in such arrangements is twofold. First, the fact that such measures have no legal status in GATT and have not been effectively challenged in it increases the temptation of the importing countries to achieve their goals of restraining imports in this extra-GATT fashion. Secondly, the bilateral nature of such arrangements clears the way for arbitrary solutions and the exertion of pressure on weaker trading partners, as imports of the major trading partners can be omitted from GATT actions. The proliferation of these so-called "grey area" measures has been one of the major factors undermining the credibility of GATT.

There are a number of motives for countries to avoid recourse to Article XIX. The first is that the application of Article XIX complied with the most-favoured-nation obligation laid down in Article I of GATT, precluding discrimination between different sources of imports. The argument most commonly used by the proponents of a "selective", i.e. discriminatory, application of safeguard measures is that Article XIX should allow governments to prevent disruption of the market by the increase of exports from particular sources,<sup>34</sup> that is, the right to limit the impact of new competitors. These arguments have been opposed on the ground that action against one or a few sources may divert import competition to non-restricted suppliers. But the proponents of selectivity argued that in fact "injury" often occurred because of the rapid expansion of imports from only one or a few sources, and that only those imports should be

restrained, whereas there was no need to restrain the exports of other, traditional suppliers.

A second reason is the possible need to offer "compensation" for restrictive action or else face compensatory withdrawal of concessions on a discriminatory basis. In terms of domestic political considerations, the possibility, as provided for in Article XIX, of the withdrawal by the exporting country of substantially equivalent concessions, or of the offer by the importing country of compensatory concessions, as an alternative, may well have been an important discipline limiting recourse to Article XIX, particularly given the MFN obligation.<sup>35</sup> Protection granted to one domestic industry would thus be balanced by the cost imposed on other domestic industries, with the likelihood of political implications. There is a vast difference, therefore, in domestic political terms, between seeking to impose a restraint on imports under Article XIX with compensation, and dealing with such imports by negotiating a restraint outside GATT where no compensation or retaliation would be involved.<sup>36</sup>

Most importantly, many industries which have sought and obtained protection under extra-GATT measures could not have demonstrated that they were suffering "serious injury" in the sense of Article XIX.

#### **4. Attempts to introduce "selectivity" into GATT Article XIX actions before the Tokyo Round**

Throughout the history of GATT, various attempts have been made to introduce discrimination into the application of safeguard measures. The first case occurred in the early 1950s when Japan's accession to GATT was under consideration. Some contracting parties wished to retain the right to apply dis-

of-payments reasons; Article XVIII, providing for the less-developed contracting parties rights' to impose tariff and import restrictions; Article XX, which permits action to safeguard public health and safety; Article XXI, which may be invoked to safeguard security interests; Article XXIII, which permits contracting parties to renegotiate concessions in GATT schedules; and Article XXXV, which permits the non-application of the General Agreement between particular contracting parties in certain circumstances.

<sup>33</sup> According to GATT sources, in the period 1980-1987, 35 Article XIX actions were resorted to in all (19 involving tariff increases and 16 non-tariff measures). By contrast, as of April 1988, 191 restraint arrangements were in force covering such sectors as automobiles and transport equipment, steel and steel products, electronics, temperate-zone agricultural products, textiles (outside MFA), footwear, and machine tools. Nearly 80 per cent of those actions were taken by the EC, the United States and Canada.

<sup>34</sup> GATT document L/4679, para. 22.

<sup>35</sup> Paragraph 3(a) of Article XIX provides for the affected party's right to "suspend ... the application ... of ... substantially equivalent concessions or other obligations under this Agreement ...".

<sup>36</sup> In practice, there have been few cases of retaliation or requests for compensation as countries preferred to continue to press for removal of the safeguard measures themselves.



criminary quantitative restrictions on imports from Japan<sup>37</sup> and sought to include a "selective" safeguard provision in Japan's Protocol of Accession (which would allow them to impose safeguard measures only upon imports from Japan). They also suggested that an additional safeguard provision should be introduced into the General Agreement, arguing that a large number of Article XIX actions, which would have to be applied on a most-favoured-nation basis, might lead to a general raising of barriers to world trade. The suggestion was made that, in order to avoid a higher general level of barriers to world trade, contracting parties might bring cases to GATT under Article XXIII:2, under which GATT contracting parties are entitled to authorize the application of safeguard actions on a discriminatory basis. However, some delegations pointed out that there might be circumstances in which the procedures of Article XXIII would be too slow in operating to provide adequate safeguards, and suggested that if the contracting parties failed to reach a decision within 30 days, provisional safeguard measures might be taken pending such a decision. In the end there was no agreement on the application of Article XXIII along these lines.<sup>38</sup>

Japan successfully resisted this attempt and became a GATT contracting party in September 1955 although no new general safeguard provision was added to GATT or any "selective" safeguard provision in its Protocol of Accession. However, many contracting parties invoked Article XXXV against Japan's accession (disinvoked in most cases within a 10-year period), and then negotiated bilateral understandings with Japan envisaging special bilateral safeguard measures outside GATT.<sup>39</sup>

The failure to add a new general safeguard provision to GATT and to include a selective safeguard provision in Japan's Protocol of Accession, combined with the growing competitiveness of some other Asian countries, provoked efforts to introduce the possibility of discrimination into the multilateral safeguard system through the concept of "market disruption".<sup>40</sup> This was defined as serious damage to domestic producers caused by "a sharp and substantial increase or potential increase of imports of particular products from particular sources", and if "these products are offered at prices which are substantially below those prevailing for similar goods of comparable quality in the market of the importing country".<sup>41</sup>

While attempts to legitimize the general application of discrimination based on "market disruption" at the multilateral level were not successful, this concept was introduced into the cotton textiles sector and incorporated into the Short-Term Arrangement Regarding International Trade in Cotton Textiles (STA) in the early 1960s.<sup>42</sup> It permitted the application of what were, in practice, selective safeguards against the so-called "low cost suppliers", normally in the form of "voluntary" export restraints. This led to an extension in 1974 to other supplying countries and to a wider range of products in the Arrangement Regarding International Trade in Textiles, commonly known as the Multi-Fibre Arrangement or the MFA. The MFA now covers almost all textile and clothing products and has subjected nearly 40 developing countries and economies in transition to export restraints in most major developed countries.<sup>43</sup> This Arrangement influenced governments to make broader use of voluntary restraints as a mechanism to restrict trade on a discriminatory basis in other sectors where such

<sup>37</sup> See GATT document L/76.

<sup>38</sup> GATT document MTN.GNG/NG9/W.1, 7 April 1987. See also Gardner Patterson, *Discrimination in International Trade - The Policy Issues 1945-1965* (Princeton, N.J.: Princeton University Press, 1966), pp. 285-317.

<sup>39</sup> *Ibid.*

<sup>40</sup> In June 1960 a GATT Working Party on Avoidance of Market Disruption was established to develop a way to deal with the problems of imports of textiles from the so-called "low cost" suppliers other than dumped or subsidized imports. In November 1960, through a Decision, the concept of discrimination based on market disruption was accepted by GATT to describe a situation in which, *inter alia*, there should be a combination of the following elements: "(i) a sharp and substantial increase or potential increase of imports of particular products from particular sources; (ii) these products are offered at prices which are substantially below those prevailing for similar goods of comparable quality in the market of the importing country; (iii) there is serious damage to domestic producers or threat thereof; and (iv) the price differentials referred to in paragraph (ii) above do not arise from governmental intervention in the fixing or formation of prices or from dumping practices". Since then, this concept has been one of the basic premises of the MFA.

<sup>41</sup> GATT, *Basic Instruments and Selected Documents (BISD)*, Ninth Supplement, February 1961, p. 26.

<sup>42</sup> Later on the STA was superseded by the Long-Term Arrangement Regarding International Trade in Cotton Textiles (LTA).

<sup>43</sup> As of 24 November 1993, the status of MFA acceptances was as follows: Argentina, Austria, Bangladesh, Brazil, Canada, China, Colombia, Costa Rica, Czech Republic, Dominican Republic, EC, Egypt, El Salvador, Fiji, Finland, Guatemala, Honduras, Hong Kong, Hungary, India, Indonesia, Jamaica, Japan, Lesotho, Macau, Malaysia, Mexico, Norway, Pakistan, Panama, Paraguay, Peru, Philippines, Poland, Republic of Korea, Romania, Singapore, Slovak Republic, Sri Lanka, Switzerland, Thailand, Turkey, United States and Uruguay. GATT document COM.TEX/75/Rev. 1, 26 November 1993.

a multilateral instrument exists to legitimize actions such as "grey area" measures.<sup>44</sup>

Although the concept of "market disruption" was ostensibly applied to deal with a temporary situation, the discriminatory regime on textiles has remained in existence for more than 30 years, and has been continually extended in its product and country coverage against developing countries.<sup>45</sup>

### 5. Attempts to introduce "selectivity" into GATT Article XIX actions during the Tokyo Round

At the preparatory stage of the Tokyo Round, the question of the adequacy of the existing multilateral safeguard system emerged as a high priority issue. In accordance with the Tokyo Declaration adopted in September 1973, a negotiating group on safeguards was established to examine "the adequacy of the multilateral safeguard system, considering particularly the modalities of application of Article XIX". However, the group progressed very slowly and intensive negotiations on substantive issues did not take place until 1978. A draft integrated text on safeguards was put forward by a number of developed countries as a basis for further discussion.<sup>46</sup> Intensive bilateral and plurilateral negotiations also took place, but positions on the major problems and in particular on the question of selectivity remained far apart. Some countries favoured an approach that permitted unilateral, selective action with *ex post facto* review by a Committee on Safeguard Measures. One of their arguments was that countries were far more likely to move toward further trade liberalization if there were adequate provisions for safeguard action against imports when these became disruptive and created unacceptable social costs. Some other countries were insistent that any selective action be preceded by an agreement on the part of the exporting

country, or approval by the Committee. In this connection, there was also considerable discussion on the criteria under which there might be a selective application of the safeguard clause.<sup>47</sup>

At the early stage of the negotiations, views among developing countries as to the advantages of "selectivity" diverged to a certain extent. While many of these countries steadfastly supported the non-discrimination rule coupled with special and differentiated treatment for developing countries, others tended to favour the idea of selective application in the belief that this would facilitate exemption of their exports from safeguard action taken by countries desirous of limiting more dynamic exporters than themselves. However, there was a noticeable shift in the position of this latter group of developing countries at a late stage of the negotiations. Their thinking was significantly influenced by the experience of the bilateral negotiations under the MFA in which the EC negotiated restraint agreements with even those developing countries which supplied extremely small percentages of the EC market for a given textile product.<sup>48</sup> This revelation made it clear to most developing countries that "selectivity" provided no guaranteed immunity even for relatively small exporters, and in fact considerably strengthened the hand of the economically strong in their dealings with poorer and weaker countries. They strongly favoured the continued MFN application of Article XIX, and maintained that safeguard measures should be applied on a global basis without discrimination and in conformity with Articles I and XIII of GATT. They believed that pressures in developed countries for protection against so-called low-cost imports in sectors other than textiles made it highly likely that a modified safeguard clause would be principally used against them.

In the event, in spite of intensive efforts made at the final stage of the Tokyo Round, and a narrowing of differences, it was not possible to reach agreement within the framework of the Round as the EC insisted on the inclusion of selectivity in the final text. Apart from

<sup>44</sup> While Article 1 of the MFA recognizes that the provisions of the MFA do not affect the rights and obligations of participating countries under the GATT, Article 3 of the MFA permits importing countries to impose discriminatory quantitative restrictions when they consider that imports cause or threaten to cause "market disruption", as defined by its Annex A. Consultations between the importing and exporting countries are provided for, but the MFA, unlike Article XIX, does not specify that affected exporting countries may retaliate if agreement is not reached in the consultations. Instead, they may bring the matter for immediate attention to the Textiles Surveillance Body, which is responsible for making recommendations with regard to all disputes brought before it. Article 4 of the MFA permits participating countries to conclude bilateral agreements on mutually acceptable terms in order to eliminate "real risks of market disruption". It is under this Article that a great number of "grey area" measures are legitimized.

<sup>45</sup> See discussion in chapter V.

<sup>46</sup> GATT document MTN/SG/W/39, 22 June 1978.

<sup>47</sup> GATT document MTN.GNG/NG9/W/1, 7 April 1987.

<sup>48</sup> See UNCTAD/MTN/CB.18/Rev. 1/PART II, September 1979, pp. 36-42.

the question of selectivity, the key areas of disagreement, as identified by the Director-General of GATT, also included surveillance and dispute settlement, determination of serious injury, and structural adjustment.<sup>49</sup> The lack of an agreement on safeguards was considered by some to be a major failure of the Tokyo Round; others thought that it was of no great relevance because "selectivity" could be secured by more widespread recourse to Article VI measures, that is, to anti-dumping duties and to "undertakings" in anti-dumping cases.

## 6. The 1982 Ministerial Declaration

In the 1982 GATT Ministerial Meeting, contracting parties undertook individually and jointly, "to bring into effect expeditiously a comprehensive understanding on safeguards to be based on the principles of the General Agreement".<sup>50</sup> The 1982 Ministerial Declaration called for an "improved and more efficient safeguard system which provides for greater predictability and clarity and also greater security and equity for both importing and exporting countries, so as to preserve the results of trade liberalization and avoid the proliferation of restrictive measures".<sup>51</sup>

But, again due to the difference of opinion on the question of "selectivity", it was not possible to reach a clear understanding providing for the elimination of "grey area" measures, and the suggestion to implement any partial agreements that might be reached in the absence of a comprehensive understanding was also found to be unacceptable to certain participants.

## 7. Discussions in the Preparatory Committee of the Uruguay Round

During the preparatory process of the Uruguay Round, almost all GATT contracting parties recognized the importance of a workable comprehensive agreement on safeguards for the multilateral trading system and agreed to include safeguards as a key issue in the programme of negotiations. However, the po-

sitions of the contracting parties as to how to approach the negotiations on safeguards remained far apart. Developing countries, in particular Brazil, were of the view that, as the new round was intended to further liberalize world trade, commitments should be made not "to introduce new restrictive measures outside GATT and to phase out any such measures already in existence". They proposed that safeguard actions should be based on the MFN principle.

In July 1986, a draft Ministerial Declaration representing a broad consensus among both developed and developing countries was circulated by the delegations of Colombia and Switzerland. On the issue of safeguards, the draft was clearly a compromise. It emphasized the importance of reaching a comprehensive agreement on safeguards based on the principles of GATT and clarified and reinforced the disciplines contained therein.

## 8. The Ministerial Declaration of the Uruguay Round

In view of the renewed determination of the GATT contracting parties to achieve the objective of strengthening the multilateral trading system, the Uruguay Round offered another opportunity to negotiate a comprehensive agreement on safeguards. The decision taken on safeguards by the Ministerial Declaration adopted at Punta del Este in September 1986 stated that: "A comprehensive agreement on safeguards is of particular importance to the strengthening of the GATT system and to progress in the Multilateral Trade Negotiations", and specified that such an agreement "shall be based on the basic principles of the General Agreement; shall contain, *inter alia*, the following elements: transparency, coverage, objective criteria for action including the concept of serious injury or threat thereof, temporary nature, degressivity and structural adjustment, compensation and retaliation, notifications, consultation, multilateral surveillance and dispute settlement; and shall clarify and reinforce the disciplines of the General Agreement and should apply to all contracting parties".

<sup>49</sup> For details see *Tokyo Round of Multilateral Trade Negotiations: Report by the Director-General of GATT*, April 1979, pp. 94-95.

<sup>50</sup> Ministerial Declaration of 29 November 1982, GATT, *BISD*, Twenty-ninth Supplement, March 1983, p. 12.

<sup>51</sup> *Ibid.*

## 9. Mid-Term Review

The question of "selectivity", referred to earlier, had prevented the achievement in the Tokyo Round of an agreement on safeguards. Observance of the MFN principle when resorting to Article XIX actions has been viewed by many participants, particularly weak, small and medium-sized countries, as the main element in an equitable solution to the problem of safeguards for the success of both the Uruguay Round and the multilateral trading system.<sup>52</sup> They considered that it was the non-discriminatory application of Article XIX which protected their interests since a government taking discriminatory action would come under pressure to desist from all countries affected. However, the EC, as in the Tokyo Round, argued that the selective application of Article XIX actions would allow countries to deal with problems created by a few exporting countries in such a way as to cause the minimum disturbance of trade.<sup>53</sup>

At the Mid-Term Review in late 1988, a text setting out principles to govern the safeguard negotiations was submitted by the Chairman of the Negotiating Group on Safeguards. It emphasized that safeguard measures should be of limited duration and non-discriminatory, and that "grey area" measures that resulted in selective application should be proscribed. However, the text was not approved by the Ministers at the Mid-Term Review because of the lack of consensus on this last principle, and their disagreement left the negotiations in an impasse. However, at the

resumed session of the Mid-Term Review in April 1989, participants agreed to put forward texts and proposals, and requested the Chairman of the Group to submit a draft text on a comprehensive agreement with a deadline, founded on the basic GATT principles, and stressed the importance of re-establishing multilateral control over safeguards by, *inter alia*, eliminating measures that escape such control. They also recognized that safeguard measures should, by definition, be of limited duration.<sup>54</sup>

In June 1989, a draft text of an agreement on safeguards was submitted by the Chairman for consideration by the Group.<sup>55</sup> However, the draft proposal was exposed to criticism from both developed and developing countries. The EC maintained its position that Article XIX should allow safeguards to be applied selectively. In January 1990, the EC submitted a comprehensive proposal on a selective safeguard system,<sup>56</sup> which set out in specified terms its views on when selectivity should be permitted.<sup>57</sup>

## 10. The Brussels Meeting and its aftermath

Though most of the technical work had been accomplished prior to the Brussels Meeting, divergent views on the key questions remained.<sup>58</sup> When trade ministers met at Brussels in December 1990 the gap between the various

<sup>52</sup> See, for example, the Communication from Australia, Hong Kong, Korea, New Zealand and Singapore, GATT document MTN.GNG/NG9/W/4, 25 May 1987; Communication from Brazil, GATT document MTN.GNG/NG9/W/5, 2 July 1987; Communication from Mexico, GATT document MTN.GNG/NG9/W/18, 10 June 1988; Communication from Switzerland, GATT document MTN.GNG/NG9/W/26, 2 November 1989 and Submission by Switzerland, GATT document MTN.GNG/NG9/W/20, 14 July 1988; and Submission by Japan, GATT document MTN.GNG/NG9/W/11, 13 October 1987.

<sup>53</sup> Submission by the European Communities, GATT document MTN.GNG/NG9/W/24/Rev. 1, 26 June 1989.

<sup>54</sup> GATT document MTN.TNC/11, 21 April 1989.

<sup>55</sup> GATT document MTN.GNG/NG9/W/25, 27 June 1989.

<sup>56</sup> See Communication by the European Communities, "Safeguards regime applicable in special circumstances", GATT document MTN.GNG/NG9/W/29, 31 January 1990.

<sup>57</sup> The EC proposal permitted interim precautionary action against one supplier or a group of suppliers of products found by the importing country to be causing injury to domestic producers as a result of a large increase in imports. Action to restrict imports from the supplier or suppliers concerned would follow consultations, would be proportional to the injury suffered and would be removed after a maximum of eight months or at the end of the full injury investigation. Where serious injury was finally established, the importing country would be able, following consultations, to apply safeguard measures selectively for a maximum period to be the subject of negotiations in the Round. Countries affected by the interim or final measures would be free to withdraw equivalent concessions or other obligations from the importing country. During the period the selective measures were in place, imports from unaffected suppliers would be monitored in the importing country. If such imports increased significantly, the countries covered by the safeguard measure could request the extension of the restrictions to other suppliers. The period of application of selective measures would be fully taken into account in the maximum period for safeguard measures authorized under the general provision of the agreement (i.e. non-selective provisions).

<sup>58</sup> These included such questions as: "Should selective exceptions to normal application of Article XIX be permitted in exceptional circumstances and subject to specific conditions or should it be confirmed that Article XIX action can only be taken on an MFN basis?" "Should incentives be provided for governments to act within the rules of Article

contracting parties narrowed significantly. Progress was made in establishing time-limits for the measures, ensuring degressivity, improving notification and consultation procedures, establishing greater transparency in domestic procedures, and creating a standing Safeguards Committee. Even on the issue of selectivity, which had long been a source of disagreement, the EC indicated its readiness to drop their support for selectivity if greater flexibility was allowed in allocating MFN quotas (the so-called "quota modulation" i.e. an importing country would be allowed, in allocating quota shares, to restrict some suppliers more than others). Furthermore, improved consensus on a number of core issues rendered the question of structural adjustment measures less important or controversial. For example, the time-limit for safeguard measures would force the industries to come to grips with adjustment programmes.<sup>59</sup>

By the end of the Brussels Meeting, most of the technical work had been completed, although the negotiating group still faced a number of substantive decisions. A new draft text was prepared which called for definitive elimination of all measures taken outside the purview of Article XIX, but no timetable for phasing out these measures was set. On the question of whether selectivity should be permitted, the language used in the draft was al-

tered, but it was agreed that an importing country, in allocating quota shares, might restrict some suppliers more than others, subject to certain limitations. However, difficulties arose over the details of the limitations, such as how to preclude the use for safeguard purposes of measures other than those provided for in the agreement. The negotiators also had to decide on whether to suspend compensatory action for an initial period of time, whether to permit internal measures such as subsidies as a form of safeguard action, and how to define in quantifiable terms the proportion of domestic industry which should suffer injury before safeguard measures could justifiably be taken. Questions related to the minimum and maximum durations of a safeguard measure and the criteria governing the provision for differential and more favourable treatment for developing countries also had to be resolved.<sup>60</sup>

In December 1991, Mr. Arthur Dunkel, the Director-General of GATT, presented what he described as the "concrete and comprehensive representation of the final global package of the results of the Uruguay Round". The final text of the Agreement on Safeguards included in this package is not markedly different in substance from a draft text of the Chairman of the Negotiating Group on Safeguards prepared in June 1991.

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## B. Content

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### 1. *Brief description of the Agreement on Safeguards*

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The final text of the Agreement on Safeguards, as verified after 15 December 1993 for signature by Ministers at the Marrakesh Meeting of 12-15 April 1994, consists of a preamble, 14 articles and an annex. The preamble recognizes the need to clarify and reinforce the disciplines of GATT and specifically those of its Article XIX, to re-establish multilateral control over safeguards and eliminate measures that escape such control. It also recognizes the importance of structural adjustment and the need

to enhance rather than limit competition in international markets. Articles 1, 2, 3, 5, 6 and 10 establish basic principles, rules, conditions and scope for the application of the safeguard measures provided for in Article XIX. Article 4 defines the criteria of serious injury or threat thereof. Article 7 establishes time-limits for the application of safeguard measures. Article 8 relates to the waiver on compensation requirements. Article 9 provides for differential and favourable treatment for the developing country members. Article 11 prohibits and phases out "grey area" measures. Articles 12, 13 and 14 establish the procedures for monitoring and review of the operation of the Agreement and the requirements for notification, consultation

XIX e.g. by waiving retaliation in specific circumstances, and, if so, what are those circumstances?" "Should "grey area" measures be phased out or brought into conformity with this agreement?" "If so, what are the conditions and timetables for such actions?"

<sup>59</sup> Terence P. Stewart (ed.), *The GATT Uruguay Round: A Negotiating History (1986-1992)*, Vol. II (Deventer (Netherlands), Boston: Kluwer Law and Taxation Publishers, 1993), pp. 1788-1790.

<sup>60</sup> *Ibid.*, pp. 1790-1794.

and dispute settlement. The Annex gives an example of a "grey area" measure that constitutes an exception under Article 11, and that may be maintained by an importing member until 31 December 1999.<sup>61</sup>

## 2. *Selectivity vs. most-favoured-nation treatment (MFN)*

At the later stage of the negotiations, compromises were inevitable. As mentioned above, the EC finally dropped its demand for selectivity, provided that flexibility in allocating MFN quotas would be permitted under the so-called "quota modulation" provision. Nevertheless, some conditions were attached to that flexibility, such as evidence of serious injury, prior consultation, surveillance, examination and review, and in particular the establishment of a mechanism to ensure that these conditions were met. Whether this proves to be anything other than selectivity in disguise remains to be shown by the actions of governments after the agreement comes into effect (see box 7).

The nature of the "special factors which may have affected or may be affecting trade in the product" is not clearly specified, and could be interpreted to mean prices. Neither are the terms in which a departure from the general rule may be "justified", nor the criteria of equity under which a departure from the rule in Article 5:2(a) might be "equitable to all suppliers".<sup>62</sup> Problems may arise as to how to define that "imports from certain members have increased in disproportionate percentage in relation to the total increase of imports of the product concerned in the representative period" and how to justify that "the conditions of such departure are equitable to all suppliers of the product concerned".

During the course of the negotiations, certain attempts were also made by some developed countries to introduce the concept of including "low-prices" in the Agreement among the criteria for safeguard action<sup>63</sup> (as when determining "market disruption"), which was

aimed at low-cost suppliers in developing countries. Owing to the opposition of developing countries, any such reference to price was finally dropped from the Chairman's draft text of June 1991.

On the related issue of "grey area" measures, a possible clue appears as a footnote to Article 11:1(b), which states that "An import quota applied as a safeguard measure in conformity with the relevant provisions of GATT 1994 and this Agreement may, by mutual agreement, be administered by the exporting member." An import quota administered by an exporting-member government, however, has many of the characteristics of a VER. An importing-member government may therefore be able to persuade an exporting-member government to accept an unduly small Article XIX quota allotment (less than the exporting-member entitlement under the GATT Article XIII), in the same way that it might have currently persuaded that government to accept a VER.

## 3. *"Grey area" measures*

Article 11 addresses the key issue of the proliferation of the "grey area" measures. Paragraph 1 (a) states that a member shall not take or seek any emergency action on imports of particular products as set forth in Article XIX of GATT 1994 unless such action conforms "with the provisions of that Article applied in accordance with this Agreement." In other words, the Agreement prohibits the future use of "grey area" measures for the purpose of evading multilateral control.

Paragraph 1 (b) of Article 11 calls for the existing "grey area" measures to be phased out. In this respect, paragraph 2 of the same Article requests the members concerned to present timetables to the Committee on Safeguards within 180 days after the date of entry into force of the WTO Agreement. These timetables will provide for all measures (except those covered by other provisions and agreements

<sup>61</sup> As indicated in the Annex, the EC/Japan agreement on certain automobiles is one of these measures agreed as following under this exception to which the EC is entitled.

<sup>62</sup> In the history of GATT, there have been several cases in which Article XIX actions have been taken unilaterally on a discriminatory basis. For example, the 1978 case of the United Kingdom's restrictions on imports of television sets from the Republic of Korea; the 1980 case of Norway's restrictions on imports of certain textile products from Hong Kong; the 1993 case of Austria's restrictions on imports of certain types of cement and certain preparations containing cement from Poland, Romania, the Czech Republic and the Slovak Republic; and, most recently, the case of Canada's restrictions on imports of boneless beef from Australia and New Zealand, imports of which from the United States have been excluded from the restrictions.

<sup>63</sup> See the Brussels text of the draft Final Act, GATT document MTN.TNC/W/35, 26 November 1990, p. 187.

## QUOTA MODULATION

One of the main issues under discussion in the negotiations on safeguards in the Uruguay Round was whether selective exceptions to the normal application of GATT Article XIX should be permitted in exceptional circumstances and subject to specific conditions or whether it should be confirmed that Article XIX action could only be taken on an MFN basis.

Despite Article 2:2, which states that "Safeguard measures shall be applied to a product being imported irrespective of its source", the Agreement on Safeguards, in Article 5:2(b), permits flexibility in allocating MFN quotas among suppliers in certain circumstances. This is the so-called "Quota modulation" provision under which WTO members may deviate from the MFN provisions when an overall import quota is imposed by an importing country against all sources of suppliers, in that the share allocated to countries found to be contributing more to global injury could be lower than the share allocated to them on the basis of recent trade patterns.

Article 5:2(a) states that an importing member applying a quota under Article XIX may seek agreement among the exporters as to their respective shares of the quota. In the event that "this method is not reasonably practicable", however, it allows the importing member to allot shares in the quota on the basis of import shares "during a previous representative period", "due account being taken of any special factors which may have affected or may be affecting the trade in the product."

Article 5:2(b) details the conditions under which a WTO member may depart from allocating quotas among supplier parties on a strict MFN basis and from the traditional practice of GATT.<sup>1</sup> Such departure from the MFN provisions is permissible provided that (i) "imports from certain Members have increased in disproportionate percentage in relation to the total increase of imports of the product concerned in the representative period", (ii) the reasons for the departure are justified and consultations are conducted, in advance, with affected parties, and (iii) "the conditions of such departure are equitable to all suppliers of the product concerned". Furthermore, such departure is only allowed to remedy serious injury for a period of four years and is not permitted in the case of threat of serious injury.

In order to seek a departure, the importing country needs:

- to provide the Committee on Safeguards with all pertinent information, which includes evidence of serious injury, a precise description of the product and the proposed measure (which, in this case, may only be in the form of a quota), proposed date of introduction, etc.; and
- to provide adequate opportunity for prior consultation with the affected exporting country with a view to reviewing the above-mentioned information.

The reasons for the departure must be justified to the Committee on Safeguards.

As referred to above, a departure from the non-discrimination rule shall only be permitted in the case of serious injury, which, as provided for in paragraph 1 (a) of Article 4, "shall be understood to mean a significant overall impairment in the position of a domestic industry".

Furthermore, such departure would not apply to a developing country whose share of imports of the product concerned in the importing country does not exceed 3 per cent, on condition that developing countries with less than 3 per cent import share collectively account for not more than 9 per cent of total imports of the product concerned.

Although, some conditions were laid down with a view to limiting the scope for an importing country to make a departure, this may lead to some arbitrary applications of this provision and leaves the door open for selectivity or discriminatory applications in certain cases. In this regard, problems may arise as to how to define that "imports from certain Members have increased in disproportionate percentage in relation to the total increase of imports of the product concerned in the representative period" and that "the conditions of such departure are equitable to all suppliers of the product concerned".

At certain stages of the negotiations, attempts were made to establish some percentage points (or a ratio) of the proportion supplied during the representative period as a criterion for the importing country in reducing the individual quota allotments when it is necessary to remedy the serious injury. However, at a late stage of the negotiations participants dropped this idea.

**Box 7 (concluded)**

The nature of the "special factors which may have affected or may be affecting trade in the product", is not clear. The term "equitable" is also difficult to define as the criteria by which to judge "what would have been the case" are not precisely specified.

In this context, several cases in GATT history are relevant in respect of "quota modulation", for example, the dispute over "Norway - Restrictions on Imports of Certain Textile Products from Hong Kong". In 1980, a GATT panel was established to examine the Article XIX action by Norway, whereby global quotas were introduced on nine textile items. Imports from the EEC and EFTA countries were not subject to those quotas, nor were imports from six developing country textile-exporting countries with which Norway had concluded bilateral arrangements. The size of the global quotas was calculated on the basis of average imports in 1974-1976 from the countries included in the quotas, the quotas being allocated to importers but not by supplier country. The panel report was as follows: "The panel was of the view that the type of action chosen by Norway, i.e. the quantitative restrictions limiting the importation of the nine textile categories in question, as a form of emergency action under Article XIX, was subject to the provisions of Article XIII, which provides for non-discriminatory administration of quantitative restrictions... The panel was of the view that to the extent that Norway had acted with effect to allocate import quotas for these products to six countries but had failed to allocate a share to Hong Kong, its Article XIX action was not consistent with Article XIII".

Another example is the recent Article XIX action by Canada against imports of boneless beef from Australia and New Zealand. The United States has been excluded from such action.

However, under the quota modulation provisions, the actions taken by Norway and Canada may be justified and could be consistent. Therefore, quota modulation appears to move in the direction of allowing a certain selectivity and could have the effect of weakening the conditions of application of safeguard measures as provided for in Article XIX of GATT 1947.

1 GATT Article XIII:2 (d) provides that "In cases in which a quota is allocated among supplying countries, the contracting party applying the restrictions may seek agreement with respect to the allocation of shares in the quota with all other contracting parties having a substantial interest in supplying the product concerned. In cases in which this method is not reasonably practicable, the contracting party concerned shall allot to contracting parties having a substantial interest in supplying the product shares based upon the proportions, supplied by such contracting parties during a previous representative period, of the total quantity or value of imports of the product, due account being taken of any special factors which may have affected or may be affecting the trade in the product. No conditions or formalities shall be imposed which would prevent any contracting party from utilizing fully the share of any such total quantity or value which has been allotted to it, subject to importation being made within any prescribed period to which the quota may relate."

other than Article XIX and the Agreement on Safeguards) to be phased out or brought into conformity with this Agreement within a period of four years after the date of entry into force of this Agreement, with the exception that each importing member may maintain one specific measure for a period not extending beyond 31 December 1999. However, any such exception must be mutually agreed between the members directly concerned and notified to the Committee on Safeguards for its review and acceptance within 90 days after the entry into force of the WTO Agreement.

To enforce this Article on a technical level could be a central problem. One difficulty lies in identification. For example, VERs take many forms. Formal treaties or agreements are

not needed for a VER to be effective. In particular, VERs may appear as arrangements between industries, sometimes without apparent involvement on the part of governments. Consequently, it is difficult to prevent VERs from going underground.

In this regard, Article 11:3 refers to the obligation upon members not to encourage or support non-governmental measures adopted or maintained by public and private enterprises such as industry-to-industry agreements, which are equivalent to "grey area" measures maintained by governments. However, there is no commitment to ensure that such action does not occur. This has been a major argument by the proponents of multilateral rules on competition policy (see box 8).



### "GREY AREA" MEASURES

During the last three decades the international trading community has witnessed a growing use of the so-called "grey area" measures, which pose a serious threat to the multilateral trading system. "Grey area" measures are taking place in various forms of selective restraint arrangements whereby the exporting country, "voluntarily" or not, undertakes not to ship more than a certain amount of goods to the importing country. These arrangements, under different guises such as "voluntary export restraints" (VERs), "orderly marketing agreements" (OMAs), or other similar measures on the export or import side (e.g. export moderation, export-price or import-price monitoring systems, export or import surveillance, compulsory import cartels and discretionary export or import schemes, etc.), are direct substitutes for Article XIX actions and constitute a violation of basic provisions in GATT. The main characteristic of these arrangements is that they are generally bilateral and not very transparent, so they escape scrutiny in GATT.

According to the UNCTAD Data Base on Trade Control Measures, around 8 per cent of the imports (excluding fuels) of the developed countries from the developing countries and countries in transition has been subject to these measures. These measures have been taken in addition to tariffs, MFA restrictions, anti-dumping and countervailing measures. "Grey area" measures proliferate by accommodating bilateral demands from trading partners, by all possible means, with little regard for international rules and disciplines. The list of products subject to such measures is impressive, and includes agriculture, footwear, textiles and clothing, steel and steel products, machinery, electrical and electronic products, and motor vehicles.

Currently, there are over 200 such measures (or arrangements), and the most frequent users of these measures are the United States and the EC. For example, according to GATT, *Trade Policy Review - European Communities 1993* (for details see table 1), nearly 50 such measures were maintained by the EC during the period 1991-1992. The United States has also maintained more than 20 such measures as recorded by the recent GATT *Trade Policy Review - United States 1994* (for details see table 2).

#### 4. Serious injury

The criteria for "serious injury" have not been defined in GATT, and jurisprudence which has developed in particular circumstances has resulted in national decisions regarding the threat or existence of serious injury not being challenged. However, it is generally believed that the standard for "serious injury" (i.e. more serious than "material injury" or "serious damage" for example), is the most difficult to establish.

Article 4 of the Agreement on Safeguards clarifies and delineates more rigorously the basic concepts covered by Article XIX, including the need to specify the reasons for increased imports, and to demonstrate the existence of the causal link between increased imports of the product concerned and "serious injury" (see box 9).

#### 5. Investigation

For the first time, the Agreement establishes clear disciplines for the initiation of safeguard measures. Article 3:1 stipulates that a safeguard measure cannot be applied unless the competent authorities of the importing member have carried out an investigation. Such investigation "shall include reasonable public notice to all interested parties and public hearings or other appropriate means in which importers, exporters and other interested parties could present evidence and their views, including the opportunity to respond to the presentations of other parties and to submit their views, *inter alia*, as to whether or not the application of a safeguard measure would be in the public interest". With respect to the result of the investigation, the competent authorities of the importing member "shall publish a report setting forth their findings and reasoned

## Box 9

## SERIOUS INJURY AND MARKET DISRUPTION

The safeguard actions under Article XIX of GATT are often described as actions of a temporary nature taken to impede imports which are causing "serious injury" to competing domestic industries. Despite the vagueness of the description and the lack of jurisprudence in GATT, it is generally believed that the standard for "serious injury" should be the highest or most difficult to establish, since it is designed to respond to situations that do not involve any unfair action by foreign exporters. Anti-dumping and countervailing duty laws, by contrast, are designed to respond to actions deemed improper, and therefore a less rigorous standard of injury is thought appropriate. The concept of "serious injury" also differs considerably from the "market disruption" concept, which led indirectly to the negotiation of the special safeguard clause relating to the textiles and clothing sector.

Although, it is often difficult to establish what precisely should be the criteria for determining "serious injury", Article 4 of the Agreement on Safeguards reclarifies and redefines "serious injury", which "shall be understood to mean a *significant overall impairment* (emphasis added) in the position of a domestic industry", and a "domestic industry", which "shall be understood to mean the producers as a whole of the like or directly competitive products operating within the territory of a Member, or those whose collective output of the like or directly competitive products *constitutes a major proportion* (emphasis added) of the total domestic production of those products". Article 4:2 contains a detailed list of factors that can give some guidance in this respect (see the end of the Box).

In contrast to the concept of "serious injury", the concept of "market disruption" was introduced in GATT in 1960 as legitimizing the use of discriminatory restrictions against imports from specific countries - developing ones in particular.<sup>1</sup> It supposedly described a situation differing from that for which GATT Article XIX provisions were designed to provide a remedy; the inclusion of price levels in the definition of market disruption give the developed countries the justification they were seeking to restrict imports of "low cost" products from particular countries without similar imports from other sources being affected. The acceptance of the concept of "market disruption" by GATT opened the way for the establishment of a discriminatory regime - the MFA - against developing country exports of textiles and clothing, which has never ceased to expand in product and country coverage since then. (For details of the concept of "market disruption", see Annex A of the MFA below).

The concept of "market disruption" sets the dangerous precedent of introducing the price element into GATT. Such price-based discriminatory use of Article XIX (other than dumping and subsidy), and the discrimination between suppliers, either geographically or on the basis of prices, have been viewed by many countries as an infringement of GATT rules and principles and as aimed at low-cost suppliers in developing countries.

The main differences between "serious injury" and "market disruption" are as follows:

- "serious injury" refers to the totality of impairment of the industry while "market disruption" focuses on imports of particular products from particular sources;
- "serious injury" is designed to respond to situations which do not necessarily involve any price consideration. However, "market disruption" is targeted at similar products offered at prices which are substantially lower;
- "market disruption", unlike "material injury", is not aimed at unfair action but is rather a denial of the growing competitiveness of developing countries in international trade; and
- in actions taken in relation to the concept of "serious injury" the exporting country can withdraw substantially equivalent concessions, or the importing country, as an alternative, can make compensatory concessions. However, no compensation would be required for actions taken under "market disruption", as in the case of the MFA.

#### Market Disruption (Annex A of the MFA)

I. The determination of a situation of "market disruption", as referred to in this Arrangement, shall be based on the existence of serious damage to domestic producers or actual threat thereof. Such damage must demonstrably be caused by the factors set out in paragraph II below and not by factors such as technological changes or changes in consumer preference which are instrumental in switches to like and/or directly competitive products made by the same industry, or similar factors. The existence of damage shall be determined on the basis of an examination

## Box 9 (concluded)

of the appropriate factors having a bearing on the evolution of the state of the industry in questions such as: turnover, market share, profits, export performance, employment, volume of disruptive and other imports, production, utilization of capacity, productivity and investments. No one or several of these factors can necessarily give decisive guidance.

II. The factors causing market disruption referred to in paragraph I above and which generally appear in combination are as follows:

(i) a sharp and substantial increase or imminent increase of imports of particular products from particular sources. Such an imminent increase shall be a measurable one and shall not be determined to exist on the basis of allegation, conjecture or mere possibility arising, for example, from the existence of production capacity in the exporting countries;

(ii) these products are offered at prices which are substantially below those prevailing for similar goods of comparable quality in the market of the importing country. Such prices shall be compared both with the price for the domestic product at a comparable stage of commercial transaction, and with the prices which normally prevail for such products sold in the ordinary course of trade and under open market conditions by other exporting countries in the importing country.

III. In considering questions of "market disruption" account shall be taken of the interests of the exporting country, especially in regard to its stage of development, the importance of the textile sector to the economy, the employment situation, overall balance of trade in textiles, trade balance with the importing country concerned and overall balance of payments.

**Determination of Serious Injury or Threat Thereof**  
(Article 4 of the Agreement on Safeguards)

1. For the purposes of this Agreement:

- (a) "serious injury" shall be understood to mean a significant overall impairment in the position of a domestic industry;
- (b) "threat of serious injury" shall be understood to mean serious injury that is clearly imminent, in accordance with the provisions of paragraph 2. A determination of the existence of a threat of serious injury shall be based on facts and not merely on allegation, conjecture or remote possibility; and
- (c) in determining injury or threat thereof, a "domestic industry" shall be understood to mean the producers as a whole of the like or directly competitive products operating within the territory of a Member, or those whose collective output of the like or directly competitive products constitutes a major proportion of the total domestic production of these products.

2 (a) In the investigation to determine whether increased imports have caused or are threatening to cause serious injury to a domestic industry under the terms of this Agreement, the competent authorities shall evaluate all relevant factors of an objective and quantifiable nature having a bearing on the situation of that industry, in particular, the rate and amount of the increase in imports of the product concerned in absolute and relative terms, the share of the domestic market taken by increased imports, changes in the level of sales, production, capacity utilization, profits and losses, and employment.

1 In 1959, United States Under-Secretary of State Douglas Dillon launched in GATT the idea of permitting importing countries to take action to alleviate the adverse effects of an abrupt invasion of established markets and called for discussions and studies which, soon completed, led to the acceptance of the new concept of "market disruption". See Ying-Pik Choi, Hwa Soo Chung and Nicolas Marian, *op. cit.*, pp. 14-15. In November 1960, a Decision was adopted by the GATT contracting parties providing that "in a number of countries situations occur or threaten to occur which have been described as "market disruption" and that "these situations generally contain the following elements in combination: (i) a sharp and substantial increase or potential increase of imports of particular products from particular sources; (ii) these products are offered at prices which are substantially below those prevailing for similar goods of comparable quality in the market of the importing country; (iii) there is serious damage to domestic producers or threat thereof; (iv) the price differentials referred to in paragraph (ii) above do not arise from governmental intervention in the fixing or formation of prices or from dumping practices (emphasis added). See GATT, *BISD*, Ninth Supplement, p. 26, Decision of 19 November 1960 on "Avoidance of Market Disruption - Establishment of Committee".

conclusions reached on all pertinent issues of fact and law". Such disciplines could prevent arbitrary actions and provide security in international trade.

## 6. Coverage

While Article 1 states that "This Agreement establishes rules for the application of safeguard measures which shall be understood to mean those measures provided for in Article XIX of GATT 1994", Article 11:1(c) elaborates upon this in providing that "This Agreement does not apply to measures sought, taken or maintained by a member pursuant to provisions of GATT 1994 other than Article XIX, and Multilateral Trade Agreements in Annex IA other than this Agreement, or pursuant to protocols and agreements or arrangements concluded within the framework of GATT 1994".

Given that the Agreement on Textiles and Clothing contains a transitional safeguard clause allowing MFA-type discriminatory restrictions to be continuously imposed on textile products from developing countries over the 10-year transitional period, that the Agreement on Agriculture embodies a special safeguard provision, many products of key trade interest to developing countries will continue to be dealt with outside the scope of the Agreement on Safeguards (see tables 1 and 2). Furthermore, it leaves open the possibility for the inclusion of special safeguard clauses in future Protocols of Accession to the WTO.

## 7. Duration of safeguard measures

Safeguard actions are emergency actions and should therefore be temporary. Since 1950, GATT has been notified of 151 safeguard actions as of 15 April 1993, 34 of which were in force for less than a year. However, there were 54 cases of 1-4 years' duration, 43 cases of 4-8 years' duration, 9 cases of 8-12 years' duration, 6 cases of 12-16 years' duration and 5 cases of over 16 years' duration. Of the latter, 2 cases had a duration of more than 30 years (see tables 3, 4 and 5).

In order to ensure that the safeguard actions are temporary in nature, Article 7 provides that a safeguard measure may be taken for an initial period of four years. It can then

be extended if it is shown to be still necessary, if there is evidence that the industry is adjusting, and if the provisions regarding levels of concessions (Article 8) and notification and consultation (Article 12) are complied with. The total life of the measure, however, may not exceed eight years (ten years for developing countries).

## 8. Progressive liberalization

Apart from the time-limits on the duration of safeguard measures, Article 7:4 of the Agreement provides that when a safeguard measure applied has exceeded the initial period of application it should be progressively liberalized by the member applying it at regular intervals, and terminated when it is no longer necessary to remedy the "serious injury" or facilitate adjustment.

Article 7:5 stipulates that no safeguard measure shall be applied again to the import of a product which has been subject to such a measure, taken after the date of the entry into force of the WTO Agreement, for a period of time equal to the duration of the measure previously applied, provided that the non-application period is at least two years. However, paragraph 6 allows for a measure to be applied again if its duration was 180 days or less, on condition that at least one year has elapsed since the date of introduction of a safeguard measure on the import concerned, and such a measure has not been applied on the same product more than twice in the five-year period immediately preceding the date of introduction of the measure.

## 9. Waiver on compensation requirement

It is generally recognized that the obligations of Article XIX with regard to compensation and retaliation have encouraged countries to seek solutions outside GATT by using "grey area" measures. In order to strengthen the rules and disciplines in this regard, Article 8:3 waives the right of compensation within the first three years provided that the safeguard measure imposed has been taken as a result of an absolute rather than a relative increase in imports and that such a measure conforms to the provisions of the Agreement.

Table 1

## SOME OF THE SO-CALLED "GREY AREA" MEASURES AFFECTING EC IMPORTS (1991-1992)

<i>Exporter/Importer</i>	<i>Product</i>	<i>Measures</i>
<b>A. Agriculture</b>		
All suppliers/EC	Sheep meat and goat meat	Voluntary restraint/ duty-free access
Korea, Rep. of/EC (Italy)	Frozen squid	Reference prices
<b>B. Footwear</b>		
Korea, Rep. of, Taiwan/EC	Footwear (excluding slippers)	Prior Community surveillance/ export restraint
China/EC	Slippers and indoor footwear	Prior Community surveillance
(All third country imports of footwear are under retrospective Community surveillance.)		
<b>C. Textiles (outside MFA)</b>		
Bulgaria/EC	MFA Textiles and Clothing	MFA-type export restraints (1987-1992)
Egypt/EC	Cotton fabrics, cotton yarn	Export monitoring and moderation arrangement
Malta/EC	Certain textiles and clothing categories	Export monitoring and moderation arrangement
Morocco/EC	Certain textiles and clothing categories	Export monitoring and moderation arrangement
Tunisia/EC	Certain textiles and clothing categories	Export monitoring and moderation arrangement
Turkey/EC	Certain textiles and clothing categories	Arrangements with Turkish exporters
Japan/EC	Cotton fabrics	Export approval
Japan/United Kingdom	Clothing	Export approval
Chile, Bolivia, Paraguay, Honduras, Venezuela, Costa Rica, Cuba, Ecuador, El Salvador, Nicaragua/EC	Certain textiles and clothing categories	Exchange of letters in the GSP framework
Estonia, Latvia, Lithuania/EC	MFA Textiles and Clothing	Community surveillance
<b>D. Steel and steel products</b>		
Korea, Rep. of/EC	Steel, ferro-alloys, steel semi-manufactures	Export recommendation
All sources except EFTA/EC	All ECSC iron and steel products	Retrospective Community surveillance
All sources except EFTA/EC	Certain primary and semi- manufactured iron and steel products	Prior Community surveillance
<b>E. Machinery</b>		
Japan/EC	Forklift trucks	Retrospective Community surveillance/export constraints
Japan/EC	Machine tools for planing, gear cutting, etc.	Retrospective Community surveillance
Japan/EC	Machining centres	Retrospective Community surveillance
Japan/EC	Personal computers	Retrospective Community surveillance
Japan/EC	Electropneumatic drills	Retrospective Community surveillance
Japan/EC	Ball bearings	Export approval (no quantitative limits)

(For source and note see end of table.)

Table 1 (concluded)

SOME OF THE SO-CALLED "GREY AREA" MEASURES AFFECTING EC IMPORTS (1991-1992)		
Exporter/Importer	Product	Measures
<b>F. Electrical and electronic household equipment</b>		
Japan/EC	Colour TV sets	Retrospective Community surveillance
Japan/EC	Colour TV tubes	Retrospective Community surveillance
Japan/EC	Video tape recorders	Retrospective Community surveillance
Korea, Rep. of/EC	Video tape recorders	Retrospective Community surveillance/export performance
Korea, Rep. of/EC	Radio and TV receivers	Retrospective Community surveillance/export recommendation
Korea, Rep. of/EC	Microwave ovens	Export recommendation
Singapore/United Kingdom	Colour TV sets	Export restraints
<b>G. Road motor vehicles</b>		
Japan/EC	Passenger cars and light commercial vehicles	Retrospective Community surveillance/export monitoring
Japan/EC	Motorcycles	Retrospective Community surveillance (machines of more than 380 cc)
<b>H. Other products</b>		
Japan/World	Metal flatware	Export restraints
Japan/United Kingdom	Pottery and chinaware	Export restraints
Korea, Rep. of/EC	Spectacles and frames	Export recommendation
Korea, Rep. of/Belgium, France, Germany, Italy, Netherlands, United Kingdom	Travel goods (trunks, handbags)	Export recommendation

Source: Reproduced from GATT, *Trade Policy Review Report - European Communities 1993*, table IV.2, pp. 73-75.

Note: This table is an exact reproduction of the terminology used in table IV.2, which is that of GATT.

Otherwise, the right of an affected exporting member to suspend substantially equivalent concessions or other obligations is maintained.

Article 8:1 provides that, in applying a safeguard measure or seeking an extension of such a measure, the proposing member shall endeavour to maintain a substantially equivalent level of concessions and other obligations to that existing between it and the exporting members which would be affected by such a measure under GATT 1994. In order to achieve this, the members concerned may agree on an adequate means of trade compensation for the adverse effects of the measure on their trade. If no agreement is reached within 30 days in the consultations under the relevant provisions of the Agreement, the affected exporting members are free, not later than 90 days after the measure has been applied, to suspend, upon the expiration of 30 days from

the day on which written notice of such suspension is received by the Council for Trade in Goods, the application of substantially equivalent concessions or other obligations under GATT 1994 to the trade of the member applying the safeguard measure (Article 8:2).

## 10. Special and differential treatment for developing countries

Article 9:1 provides that safeguard measures shall not be applied to products originating in developing countries whose share of imports of the product concerned does not exceed 3 per cent, on condition that, in the case of developing country suppliers with a share of less than 3 per cent, their import share should collectively account for not more than 9 per

Table 2

**SOME OF THE SO-CALLED "GREY AREA" MEASURES AFFECTING UNITED STATES IMPORTS (AS OF OCTOBER 1993)**

<i>Exporter</i>	<i>Product</i>	<i>Measures</i>
<b>A. Agriculture</b>		
Australia	Beef and veal	VRA <sup>a</sup> on export volume
New Zealand	Beef and veal	VRA <sup>a</sup> on export volume
<b>B. Machinery</b>		
Chinese Taipei	Computer controlled machine tools	VRA <sup>a</sup> setting quotas for each machine tool category
Japan	Passenger cars and minivans	Company quotas allocated by MITI
Japan	Computer-controlled machine tools	VRA <sup>a</sup> setting share limits for each machine tool category
Japan	Ball bearings	Voluntary export restraint
Korea, Rep. of	Microwave ovens	Export monitoring
Korea, Rep. of	Video recorders	Export monitoring
<b>C. Textiles (outside MFA)</b>		
Bahrain	Cotton, wool, silk blends, vegetable and man-made fibres	Memorandum of understanding
Bulgaria	Cotton, wool, silk blends, vegetable and man-made fibres	Memorandum of understanding
Chinese Taipei	Cotton, wool, silk blends, vegetable and man-made fibres	Memorandum of understanding
Haiti		Bilateral agreement
Laos	Cotton and man-made fibres	Memorandum of understanding
Lebanon		Unilateral restraint
Lesotho	Cotton, man-made fibres	Bilateral agreement
Mauritius	Cotton, wool, silk blends, vegetable and man-made fibres	Bilateral agreement
Nepal	Cotton	Bilateral agreement
Oman		Unilateral restraint
United Arab Emirates	Cotton, wool, silk blends, vegetable and man-made fibres	Bilateral agreement
<b>D. Other manufactures</b>		
Japan	Pottery and chinaware	Export monitoring
Korea, Rep. of	Leather and rubber products	Export monitoring
Korea, Rep. of	Spectacles and frames	Export monitoring
Korea, Rep. of	Travel goods	Export monitoring
Korea, Rep. of	Some furniture products	Export monitoring

**Source:** Reproduced from GATT, *Trade Policy Review Report - United States 1994 (C/RM/S/45)*, 19 January 1994, table IV.4, p. 71.

**Note:** This table is an exact reproduction of the terminology used in table IV.4, which is that of GATT.

<sup>a</sup> Voluntary export arrangement.

cent of the total imports of the product concerned. This limit on cumulative application provides a degree of predictability for developing countries, particularly small suppliers and new entrants.

Article 9:2 stipulates that developing countries have the right to extend the period

of application of a safeguard measure for up to two years beyond the maximum period permitted (eight years). Developing countries also enjoy some privileges with respect to the reapplication of safeguard measures after half the period during which they were previously in force provided the period of non-application is at least two years (Article 7:5).

Table 3

## COVERAGE OF ARTICLE XIX ACTION (SITUATION AS OF 15 APRIL 1993)

	Number of invocations	Percentage of total invocations
<b>A. Coverage</b>		
Agricultural and food products	43	28.5
Textiles and clothing	27	17.9
Iron and steel	12	8.0
Electrical and electronic products	10	6.6
Footwear	9	6.0
Motor vehicles	6	4.0
Others	44	29.0
Total	151	100.0
<b>B. Duration</b>		
Less than one year	34	22.5
1 - 4 years	54	35.8
4 - 8 years	43	28.5
8 - 12 years	9	5.9
12 - 16 years	6	4.0
16 - 20 years	2	1.3
20 - 24 years	1	0.7
24 - 36 years	2	1.3
Total	151	100.0

Source: GATT, *Analytical Index*, Sixth edition, 1993.

### 11. Provisional safeguard measures

In critical circumstances where delay would cause damage which it would be difficult to repair, a member, as provided in Article 6, may take a provisional safeguard measure. However, that measure may only be taken in the form of tariff increases with a duration not exceeding 200 days. If the subsequent investigation determines that increased imports have not caused or threatened to cause serious injury to the domestic industry concerned, the tariff increases are to be promptly refunded.

### 12. Transparency

There has been a general recognition that maximum transparency should be maintained in this area and that all safeguard actions taken under Article XIX as well as "grey area" measures should be reported or notified to GATT. It is also recognized that the phasing out of

"grey area" measures should be the subject of multilateral surveillance. In order to achieve this objective, it has been agreed to establish a special surveillance body, entitled the Committee on Safeguards, to monitor and review the operation of the Agreement (Article 13).

Article 12 establishes more transparent procedures for notification and consultation, under which members are required to notify the Committee on Safeguards immediately upon: (a) initiating an investigatory process relating to serious injury or threat thereof and the reasons for it; (b) finding serious injury or a threat thereof caused by increased imports; and (c) taking a decision to apply or extend a safeguard measure. Members must also notify the Committee of: (i) all their pre-existing Article XIX measures taken under GATT 1947 (within 60 days after entry into force of the WTO Agreement); (ii) all "grey area" measures (within 60 days); (iii) all industry-to-industry measures; and (iv) all their laws, regulations and administrative procedures relating to safeguard measures as well as any modifications made to them.

Article 12:3 provides that a member proposing to apply or extend a safeguard measure



Table 4

## INVOCATION OF ARTICLE XIX ACTIONS

Country	Total	Period of invocation					Number of actions still in force
		1950-1959	1960-1969	1970-1979	1980-1989	1990-present	
Australia	38	2	15	17	4		
United States	27	11	3	9	4		
Canada	22	2	3	13	4		
EC	21			3	14	4	3
Greece	3	2	1				
Spain	2		2				
Italy	3		2		1		
France	2		2				
Germany	2	1	1				1
Austria	10	1	3		1	5	4
Chile	3				3		
South Africa	4				4		3
Finland	2			1	1		
Iceland	1			1			
New Zealand	1			1			
Nigeria	1		1				
Norway	1			1			
Peru	1		1				
Rhodesia	1		1				
Israel	1			1			
Switzerland	1				1		
Czech and Slovak Federal Republic	1					1	1
Hungary	3					3	1
Total	151	19	35	47	37	13	13

Source: GATT, *Analytical Index*, Sixth edition, 1993.

shall give adequate opportunity for prior consultations with those members having a substantial interest as exporters of the products concerned. If there are critical circumstances, notification shall be made before a provisional safeguard measure is taken and consultations shall be initiated immediately thereafter. The

results of the consultations with respect to Article 12, the duration (as referred to in Article 7:4), any form of compensation (Article 8:1) and proposed suspension of concessions or other obligations (Article 8:2) shall be notified to the Council for Trade in Goods by the members concerned.

### C. Implications

The achievement of an effective and efficient multilateral safeguard system for the application of GATT Article XIX was of paramount importance in strengthening trading disciplines and improving security of access to markets, particularly for developing countries

and other smaller and weaker trading partners. The lack of international consensus on the application of Article XIX has led to an ever-increasing incidence of selective trade-restrictive measures taken outside the legal framework of GATT (the so-called "grey area"

Table 5

**ARTICLE XIX ACTIONS BY COUNTRY AND BY PRODUCT  
(SITUATION AS OF 15 APRIL 1993)**

Country	Agri- culture and food products	Textiles and clothing	Iron and steel	Electrical and electronic products	Footwear	Motor vehicles	Other products	Total
Australia	2	9	5	3	4	5	10	38
United States	3	4	4	1	1	1	13	27
Canada	11	7			3		1	22
EC	14	1	1	4			1	21
Greece	1			1			1	3
Spain		1	1					2
Italy	2						1	3
France	1		1					2
Germany							2	2
Austria	4						6	10
Chile	3							3
South Africa		1			1		2	4
Finland		1					1	2
Iceland							1	1
Israel				1				1
New Zealand		1						1
Nigeria							1	1
Norway		1						1
Peru							1	1
Rhodesia		1						1
Switzerland	1							1
Czech and Slovak Federal Republic	1							1
Hungary							3	3
Total	43	27	12	10	9	6	44	151

Source: GATT, *Analytical Index*, Sixth edition, 1993.

measures such as voluntary export restraints and orderly marketing arrangements), which pave the way for arbitrary and unilateral actions by stronger partners. The proliferation of various trade-restrictive measures is generally aimed at new entrants, and this has a detrimental effect on the trade interests of developing countries wishing to obtain a share of the market.

The new Agreement on Safeguards has clarified and reinforced the disciplines for the application of safeguard measures and the strengthening of the multilateral trading system. From the point of view of developing countries, the new Agreement has the following positive elements:

- it defines more precisely the criteria of serious injury;
- it requires a substantial increase in transparency by establishing clear investigatory procedures for the application of safeguard measures, which include reasonable public notice, public hearings and the presentation of evidence and their views by other interested parties;
- it provides for time-limits on the duration of safeguard measures with a view to reducing the possibilities that such measures may be used to provide permanent protection, and calls for progressive liberalization in order to prevent these measures from going beyond what is necessary to facilitate structural adjustment to new conditions of competition;
- it prohibits new "grey area" measures and requires all the existing ones to be phased out within a period not exceeding four years, with the exception that each im-

porting member may maintain one specific measure up to 31 December 1999;

- it establishes a Committee on Safeguards to monitor and review the operation of the Agreement with clear notification and consultation procedures;
- it grants differential and more favourable treatment for the developing countries by means of:

a "threshold clause" under which safeguard measures will not be applied to a product of a developing country when the import share of the said country does not exceed 3 per cent, provided that developing countries with less than 3 per cent import share collectively account for not more than 9 per cent of total imports of the product concerned;

the extension of the period of application of safeguard measures by the developing countries; and

- it maintains the principle of non-discrimination by stipulating that the safeguard measures "should be applied to a product being imported irrespective of its source."

These improvements are designed to enhance security of access and predictability for the international trading community as a whole, particularly developing countries and smaller and weaker trading partners. However, certain provisions may be open to abuse.

Although the Punta del Este Declaration called for a comprehensive agreement on safeguards to be applicable to all product categories, special cases have been made for agricultural products, and for textiles and clothing. As noted above, trade in agricultural products and in textiles and clothing will be governed by the special safeguard regimes contained in the Agreement on Agriculture and the Agreement on Textiles and Clothing. This means that the Agreement on Safeguards covers all products other than agricultural products (which will be subject to special safeguard actions in the form of additional duties calculated on the basis of trigger volume and trigger prices) and textiles and clothing (many of which will continue to be subject to discriminatory measures until this sector is fully integrated into GATT after a 10-year transitional period). In other words, only 80 per cent of world trade

will be governed by the Agreement on Safeguards upon the date of entry into force of the WTO Agreement.<sup>64</sup> In the case of many developing countries, their trade will largely continue to be subject to the special safeguard regimes. This holds good for the area of textiles and clothing in particular, where the developed importing countries under the so-called transitional safeguard mechanism can continue to impose MFA-type restrictions on products except those integrated into GATT to which the Safeguards Agreement will apply. Such transitional safeguard measures could be applied on a country-by-country basis to both MFA and non-MFA members and would thus continue the practice of discriminatory application over the 10-year transitional period.

As for the textile and clothing products integrated into GATT, the Agreement on Textiles and Clothing provides that a safeguard measure under this Agreement may be taken on a textile product "during a period of one year immediately following the integration of that product into GATT" upon certain conditions. The exporting country concerned "shall administer such a measure" but... "shall not exercise the right of suspending substantially equivalent concessions or other obligations under the GATT as provided for under Article XIX:3(a) of GATT 1994". Frequent applications of such measures could not only disrupt the integration of the textiles sector into GATT but would also impair the effective application of the Agreement on Safeguards.

As indicated in table 3, as of 15 April 1993, 43 Article XIX actions had been taken concerning agricultural and food products and 27 actions concerning textiles and clothing; these accounted for nearly 47 per cent of the total number of Article XIX actions taken in the history of GATT. With regard to "grey area" measures (as shown in tables 1 and 2), about 50 per cent of all such measures maintained by the EC during 1991-1992 were related to agricultural products and to textiles and clothing. Among 24 such measures maintained by the United States,<sup>65</sup> 13 concerned agricultural products and textiles and clothing. It is obvious that this Agreement has not effectively brought all sectors under its control, though eventually all trade should be integrated into it. Therefore, the strengthening of all the multilateral disciplines in the area of safeguards will very much depend upon how the safeguard provisions contained in the Agreements on Agriculture and on Textiles and Clothing are respected and implemented.

<sup>64</sup> Estimates. See GATT, *International Trade Statistics 1993*.

<sup>65</sup> Recorded in the most recent GATT *Trade Policy Review - United States 1994* (C/RM/S/45), 19 January 1994, p. 71.

With the so-called "quota modulation" provisions, the Agreement appears to be moving in the direction of allowing for selectivity if imports from some members are shown to have increased "disproportionately" in relation to the total increase in imports of the product concerned, though in principle it requires safeguard actions to be non-discriminatory. The Agreement also explicitly allows quotas to be imposed, allocated on the basis of historical market shares, and envisages the option of administration of the quotas by the exporters concerned, upon mutual agreement, which has many of the characteristics of a VER.

Although some conditions were laid down, as illustrated in box 7, with a view to limiting the scope for an importing country to use "quota modulation" in seeking a departure, this may encourage arbitrary applications of this provision which could lead to abuse. Without close monitoring of the implementing legislation and administrative practices of major trading countries and effective surveillance by the Committee on Safeguards to which such measures must be justified, there would be a risk that "quota modulation" could become the rule rather than the exception, as a de facto selective safeguard clause. These provisions seem intrinsically skewed against new entrants in that a situation in which there would be an increase from a large variety of sources would be relatively unlikely, and there is a danger that the "quota modulation" provisions might provide a mechanism for dealing with increases of imports from "troublesome" new entrants without affecting the trade from traditional suppliers. In addition, the very attributes of the Agreement, such as the stringency of the injury text and phase-out periods, could encourage importing countries to resort to alternative protective devices with more flexible "trade remedy" provisions, such as under the Agreement on Anti-Dumping.

Another provision of the Agreement that might give rise to difficulties in interpretation is the phrase "absolute or relative to domestic production" to the original conditions<sup>66</sup> of Article XIX of GATT 1947 under which a safeguard action can be applied. The phrase "absolute or relative to domestic production" was taken from Section 201 of the United States Trade Act of 1974.<sup>67</sup> Under the language of Article XIX of GATT 1947, a safeguard action could only be taken by a contracting party against a product when that product "is being imported into the territory of that contracting party in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers in that territory of like or directly competitive products". The addition of the phrase "absolute or relative to domestic production" in the Safeguards Agreement means that a safeguard action can now be taken if imports have increased in absolute terms or have declined in absolute terms but have increased relative to domestic production (i.e. domestic production is falling at a faster rate than imports).<sup>68</sup> In other words, if consumption of the said product in the importing country is declining and imports take a relatively larger share of the total, even though not increasing - and perhaps even decreasing - the existence or threat of injury will have been established.<sup>69</sup> Therefore, in a period of recession, there could be more frequent recourse to such actions. With respect to the time period during which the increase in imports has to be determined, in the context of the United States law, import trends over the most recent five-year period would usually be examined. However, the Agreement makes no reference to this matter.<sup>70</sup>

Another important aspect of the Agreement is the prohibition of new "grey area" measures and the phasing-out of those in existence (as shown in box 9). This represents a major step in re-establishing the credibility of

<sup>66</sup> The original language of GATT Article XIX:1(a) reads "If, as a result of unforeseen developments and of the effect of the obligations incurred by a contracting party under this Agreement, including tariff concessions, any product is being imported into the territory of that contracting party in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers in that territory of like or directly competitive products, ....". With the new phrase, Article 2:1 (of the Safeguards Agreement, GATT 1994) states that "A Member may apply a safeguard measure to a product only if that Member has determined, ... that such product is being imported into its territory in such increased quantities, *absolute or relative to domestic production*, and under such conditions, as to cause or threaten to cause serious injury to the domestic industry that produces like or directly competitive products" (emphasis added).

<sup>67</sup> The wording used in Section (b) (2) (C) of the United States Trade Act of 1974 is "either actual or relative to domestic production".

<sup>68</sup> See "Communication from the United States on United States Procedures for Determining Injury in Article XIX Cases", GATT document MTN.GNG/NG9/W/13, 3 March 1988, p. 5.

<sup>69</sup> In this context, it is relevant to recall that the "escape clause" provisions in the United States scheme of trade policy legislation can operate in such a way as to deny "escape clause" action to domestic producers in situations where the decline of the market has been a greater factor than the increase in imports, even though the criterion of Article XIX of GATT 1947 as to quantities has been met.

<sup>70</sup> See also GATT document MTN.GNG/NG9/W/13, *op. cit.*

Table 6

**DEVELOPMENTS FOLLOWING THE EXPIRY OF VRAs<sup>a</sup> ON CERTAIN STEEL EXPORTS TO THE UNITED STATES, BY PARTNER COUNTRY, JUNE 1993**

Country	<i>VRA<sup>a</sup> on exports of certain steel products, 1984-1992</i>	<i>Anti-dumping duty order on certain flat-rolled steel products, 1993</i>	<i>Countervailing duty order on certain flat-rolled steel products, 1993</i>
Australia	yes	yes	no
Austria	yes	no	no
Brazil	yes	yes	yes
China	yes	no	no
Czechoslovakia	yes	no	no
European Communities	yes	yes	yes
Finland	yes	yes	no
German Democratic Republic	yes	no	no
Hungary	yes	no	no
Japan	yes	no	no
Korea, Rep. of	yes	yes	yes
Mexico	yes	yes	yes
Poland	yes	yes	no
Romania	yes	yes	no
Trinidad and Tobago	yes	no	no
Venezuela	yes	no	no
Yugoslavia	yes	no	no

**Source:** Reproduced from GATT, *Trade Policy Review - United States 1994 (C/RM/S/45)*, 19 January 1994, table IV.4, p. 71.

**Note:** This table is an exact reproduction of the terminology used in table IV.4, which is that of GATT.

**a** Voluntary restraint arrangement.

multilateral disciplines. However, there may be a tendency to seek alternative means of restricting imports. Past experience has shown that the removal of "grey area" measures has led to an increase of anti-dumping and countervailing measures. For example, as noted by the GATT Trade Policy Review Mechanism in its report on Japan in 1992, following the removal of restraint arrangements on exports to the United States, Japanese exporters faced an anti-dumping action as a result of complaints from major United States steel producers that Japanese steel was being dumped. The United States International Trade Commission ruled that there was reasonable evidence that the steel producers were

suffering material injury due to steel imports from 20 nations, including Japan, the Republic of Korea and Mexico.<sup>71</sup> Table 6 shows that a number of VERs on certain steel products were replaced, upon their expiry, by anti-dumping and/or countervailing measures. There is also the risk that VERs could "go underground" in the form of market sharing arrangements negotiated among private firms. Article 11:3 of the Agreement prohibits members from encouraging or supporting such practices, but the possibility of this sort of circumvention of the Safeguards Agreement is one of the main argument of the proponents of multilateral rules on competition policy.<sup>72</sup>

<sup>71</sup> See GATT, *Trade Policy Review - Japan 1992*, Vol. I, footnote 79. See also *Financial Times*, 12 August 1992.

<sup>72</sup> See discussion in chapter X.

The effective and meaningful implementation of the Agreement will also depend considerably on how far its provisions are respected by the members of the WTO, particularly those that are frequent users of Article XIX and "grey area" measures. As provided for in Article XVI:4 of the WTO Agreement, members are required to bring their national laws and regulations into conformity with this Agreement. However, it appears that the United States will replace its legislative authority for negotiating "orderly marketing agreements" with an authorization to negotiate quotas with principal supplying countries, which could appear to substantiate the con-

cerns expressed above.<sup>73</sup> The EC has to codify a number of administrative practices in its legislative system such as increased transparency and predictability in undertaking Article XIX actions.<sup>74</sup> It should also include time-limits in its legislation on safeguard measures, as the existing EC regulation is silent on this matter.<sup>75</sup>

The Agreement on Safeguards was essential to reestablish the credibility of multilateral disciplines and the security of market access. The vigilance of Members, and developing countries in particular, and their active participation in the Committee on Safeguards, would seem essential, however, to ensure that the Agreement is effectively implemented. ■

<sup>73</sup> See "Inside U.S. Trade", Special Report, March 1994, p. 4.

<sup>74</sup> See Perez-Lopez, "GATT safeguards: A critical review of Article XIX and its implementation in selected countries", *Case Western Reserve Journal of International Law*, Vol. 23, No. 3 (1991), pp. 555-556.

<sup>75</sup> See Council Regulation 288/82, 1982 O.J. (L.35) and GATT, *Trade Policy Review - European Communities 1991*, p. 48.

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## MULTILATERAL RULES ON ANTI-DUMPING MEASURES

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### A. Introduction

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A special extra customs duty, imposed on imported goods found to be sold for export at less than their price in the domestic market of the exporter (dumping), is a trade regulating device first applied by Canada early in this century. Other countries - such as the United States, Great Britain, Australia - in due course adopted this measure against price discrimination in import trade. When the General Agreement on Tariffs and Trade was drafted, provision was made for discriminatory, company-specific duties in Article VI. United States law imposed a condition that injury to the domestic industry by reason of dumping had to be shown; accordingly, this limitation on the use of anti-dumping duties was incorporated into Article VI.

In the years immediately before the Kennedy Round of multilateral trade negotiations (1962-1967), a number of exporting countries (e.g. the United Kingdom, the European Communities of Six) concluded that the United States anti-dumping law was being used increasingly to disturb trade. They were also of the view that the lack of an injury test in Canadian law could no longer be accepted. Thus the first multilateral effort to improve the implementation of Article VI of the General Agreement took place during the Kennedy Round. The Kennedy Round Anti-Dumping Code embraced detailed procedures, limited the use of preliminary measures and of retroactive application of anti-dumping duties, and required a test of injury to domestic industry before definitive duties could be levied.

A number of related developments in policy and administration followed the

Kennedy Round negotiations of the Code. First, anti-dumping duties came to be used frequently and rigorously by the major industrial countries: the United States, the European Communities, Canada, and Australia. Second, it became clear that the test of injury to the domestic industry was not difficult to meet: the industry had only to show that its prices or market shares had declined while dumping was taking place. Third, it became increasingly clear that, by and large, the calculation of a margin of dumping - the amount of price discrimination - in regard to imports was quite different from the measurement of discrimination in domestic commerce. This was taken to be protectionist. And, fourth, for domestic political reasons, the United States was not prepared to accept the Code threshold of "material" to define injury.

The second episode to improve the multilateral anti-dumping framework took place during the Tokyo Round of multilateral trade negotiations (1973-1979). The Kennedy Round Code was revised in some detail, but only incrementally in substance. It did provide, however, an opportunity for the United States to accept the Code concept of "material injury", but only after that was defined, in United States law, as being injury that was "not immaterial". Moreover, according to some, the causal link between dumping and injury was weakened; thus it became easier for domestic firms to seek relief from competition by dumped imports. The problem of calculating margins of dumping in a neutral, non-protectionist manner was not addressed.

Problems relating to the administration of national anti-dumping systems became more pronounced before and during the Uruguay Round of multilateral trade negotiations (1986-1993), the third episode to improve, clarify or expand multilateral rules and disciplines on anti-dumping measures, currently embodied in the 1979 Tokyo Round Anti-Dumping Code (hereinafter referred to as the 1979 Code). Exporting countries, including many developing countries which have made their presence felt in world export markets, alleged that anti-dumping measures were being applied to harass trade and protect domestic industries unjustifiably. Moreover, they claimed that national procedures and practices of doubtful conformity with the 1979 Code were facilitating unwarranted imposition of anti-dumping measures. Major importing countries were concerned that exporters were engaged in innovative practices to avoid or evade anti-dumping duties, thus eroding the effectiveness

of their anti-dumping measures. This issue was much discussed but in the end not addressed in the Uruguay Round Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (hereinafter referred to as the "1994 Agreement").

The 1994 Agreement is by far the most detailed multilateral instrument to regulate the application of anti-dumping measures. Whether another episode will be necessary to further improve those rules is better left for the future to answer. In the meantime, it remains to be seen whether the 1994 Agreement will cater to the objectives of each and every WTO member - as importers and as exporters - in the post-Uruguay Round trading system. Like many other trade policy instruments, the reality of anti-dumping provisions resides in the detail of national laws and administrative practices.

## B. Negotiations on anti-dumping in the Uruguay Round

The Punta del Este Declaration of September 1986 did not explicitly mandate negotiations on anti-dumping. Under the miscellaneous subject of MTN Agreements and Arrangements, the Declaration merely authorized negotiations to "improve, clarify, or expand, as appropriate, agreements and arrangements negotiated in the Tokyo Round of Multilateral Negotiations". It was therefore incumbent on interested participants to raise issues for negotiations on any of the MTN Agreements and Arrangements, other than the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade (Subsidies Code) on which negotiations were explicitly called for in the Declaration.

Several factors arising in the course of deliberations in the early 1980s on the question of launching a new round may explain why the 1979 Tokyo Round Anti-Dumping Code was not singled out for negotiations. First, obstacles to the widespread acceptance of the Subsidies Code stimulated so much controversy that this Code conspicuously presented itself as a target for new negotiations. Second, useful work was being done in the Committee on Anti-Dumping Practices which supervised the operation and implementation of the 1979

Code, notwithstanding problems that had already emerged with respect to features of certain national anti-dumping laws. In addition, discussions of esoteric anti-dumping issues did not attract the attention of contracting parties, many of which had not accepted the 1979 Code. And, third, the implementation of the Code was deemed satisfactory by several signatories, hence their initial reluctance to open it for widespread re-examination in the new round.

As the Uruguay Round negotiations unfolded, several participants which were also signatories to the 1979 Code identified areas that were in need of reform, several of which had been considered but not resolved in the Committee on Anti-Dumping Practices. In due course, the scope of issues raised for negotiations swelled beyond those discussed in the Committee, covering detailed procedural and substantive aspects of anti-dumping actions, as well as new issues aimed at modernizing the application of anti-dumping measures, including solutions to cope with 'circumvention'. Thus, the negotiations were transformed virtually into a full-scale renovation of the 1979 Code, as may be appreciated from the Chairman's inventory<sup>76</sup> of issues proposed for negotiations (see box 10).

<sup>76</sup> Negotiating Group on MTN Agreements and Arrangements, "Meetings of 31 January - 2 February and 19-20 February 1990" (MTN.GNG/NG8/16), 19 March 1990, pp. 3-59.



## ISSUES PROPOSED FOR NEGOTIATIONS

## OBJECTIVES AND PRINCIPLES OF RULES ON ANTI-DUMPING PRACTICES

*A. Scope of anti-dumping practices*

Principle that dumping is to be condemned if it causes or threatens material injury to a domestic industry in an importing country and that anti-dumping actions should be taken only when dumped imports cause material injury.

Principle that anti-dumping measures should not be taken to hamper comparative advantage and should not be used for purposes other than to counter dumping.

*B. Notion of dumping*

Distinction between price discrimination and pricing decisions taken in accordance with normal business practices and commercial considerations.

Alignment by exporters of their prices to those prevailing in the domestic market in the importing country.

*C. Impact of anti-dumping practices on the public interest**D. Effectiveness of procedures for the application of anti-dumping measures, in particular in the light of modern commercial realities**E. Uniformity and consistency in the implementation of international rules on anti-dumping practices and fairness and transparency of anti-dumping procedures*

## DETERMINATION OF THE EXISTENCE OF DUMPING

*A. Normal value*

Establishment of the normal value on the basis of domestic prices.

Circumstances in which there are no home market sales of the like product in the ordinary course of trade or in which such sales do not permit a proper comparison

meaning of the term "... not in the ordinary course of trade"; conditions under which home market sales at prices below cost of production can be considered to be not in the ordinary course of trade;

volume of home market sales which can be considered to be sufficient to permit a proper comparison.

Alternative methods for establishing the normal value

order of preference between export sales to third countries and use of a constructed value;

criteria for the selection of sales to a third country;

methodology for calculating a constructed value.

Determination of the normal value in cases referred to in the Second Supplementary Provision to paragraph 1 of Article VI in Annex I to the General Agreement.

Definition of certain terms

like product;

"... introduced into the commerce of another country";

related parties.

*B. Export price*

Use of reconstructed export prices.

**Box 10 (continued)***C. Comparison of normal value and export price*

- Factors for which allowances should be made and concept of "symmetry" of adjustments.
- Division of responsibility between investigating authorities and interested parties with regard to allowances.
- Consideration of possible special characteristics of the markets in which companies subject to investigation operate.
- Relationship between allowances made in the reconstruction of the export prices and allowances made in the establishment of the normal value.
- Use of weighted averages in the comparison of the normal value and the export price.
- Exchange rate fluctuations and inflation.

**DETERMINATION OF THE EXISTENCE OF MATERIAL INJURY CAUSED BY DUMPED IMPORTS***A. General*

- Concept of "material" injury.
- Degree of causality between dumped imports and material injury to a domestic industry.
- Treatment of instances in which exporters align their prices to those prevailing in the domestic market of the importing country.

*B. Criteria for determining the existence of material injury to a domestic industry caused by dumped imports*

- Factors to be considered in the determination of the existence of a causal relationship between dumped imports and material injury to a domestic industry.
- Weight to be accorded to certain factors.
- Consideration of factors other than dumped imports as a possible cause of material injury.
- De minimis* import volume and market penetration and *de minimis* margins of dumping.
- Cumulative injury assessment.

*C. Determination of the existence of threat of material injury*

- Recommendation concerning determination of threat of material injury.
- Other factors to be considered.

*D. Circumstances under which injury can be established on a regional basis**E. Definition of certain terms*

- Domestic industry.
- Like product.

**PROCEDURES FOR THE INITIATION AND CONDUCT OF ANTI-DUMPING INVESTIGATIONS***A. Initiation of anti-dumping investigations*

- Evidence required for the opening of investigations.
- Procedures to verify whether a petition has been filed on behalf of the domestic industry.
- Consideration of public interest factors in decisions to initiate anti-dumping investigations.
- Definition of certain terms
  - domestic industry;
  - "... introduction into the commerce of another country".

**B. Conduct of anti-dumping investigations**

## Scope of investigations

company-specific nature of investigations and possibility of limiting the scope of investigations to a representative number of parties, products and transactions;  
products subject to quantitative import restrictions;  
countries through which products are transshipped.

Definition of "interested party".

Rights of interested parties.

Use of best information available; Recommendation concerning best information available (ADP/21).

Procedures for on-the-spot investigations; Recommendation concerning procedures for an on-the-spot investigation (ADP/18).

Termination of investigations where the volume of imports is negligible or where the margin of dumping is *de minimis*; *de minimis* margin of dumping in cases of imports from developing countries.

**ANTI-DUMPING MEASURES****A. Provisional measures**

Substantive and procedural requirements for the application of provisional measures.

Timing of the application of provisional measures.

Period of validity of provisional measures.

**B. Undertakings**

Nature of undertakings in anti-dumping proceedings.

Criteria for and timing of the acceptance of offers of undertakings.

Level of price increase in an undertaking.

Undertakings in anti-dumping procedures involving imports from developing countries.

**C. Definitive anti-dumping duties**

Consideration of the public interest in the decision to impose anti-dumping duties.

Amount of anti-dumping duties.

Treatment of imports from companies which have not been investigated or which did not export during the investigation period and from small companies.

Retroactive application of anti-dumping duties.

Timing of and methodology for the assessment of anti-dumping duties and reimbursement of excessive anti-dumping duties.

**D. Duration of anti-dumping measures, administrative review and refund procedures**

Time-limit for the duration of anti-dumping duties and undertakings ("sunset clause").

Administrative reviews of determinations of dumping and injury.

Refund of excessive anti-dumping duties.

**CIRCUMVENTION OF ANTI-DUMPING MEASURES****A. Concept of circumvention of anti-dumping measures**

Situations in which circumvention of anti-dumping measures may occur.

Factors to be considered in the establishment of criteria to determine the existence of circumvention.

**Box 10 (continued)*****B. Possible remedies***

Inclusion of parts and components used in assembly or completion operations in the importing country or slightly altered and later-developed products within the scope of existing anti-dumping measures with respect to finished products.

Application of duties to products assembled or completed in the importing country.

Inclusion of products assembled or completed in a third country within the scope of existing anti-dumping measures with respect to finished products.

Retroactive application of measures against circumvention of anti-dumping duties.

Procedures for the opening and conduct of investigations to determine the existence of circumvention.

**RECURRENT INJURIOUS DUMPING*****A. Concept of recurrent injurious dumping***

Situations in which recurrent injurious dumping may occur.

Factors to be considered in the establishment of criteria for the application of measures against recurrent injurious dumping.

***B. Possible remedies***

Procedures for the initiation and conduct of accelerated investigations.

Retroactive application of anti-dumping duties.

Consideration of the effect of recurrent injurious dumping in injury determinations.

Valuation of imports in constructed value calculations in cases involving recurrent injurious dumping.

**REPEAT DUMPING*****A. Concept of repeat dumping***

Situations in which repeat dumping may occur.

Factors to be considered in the establishment of criteria for the application of measures against repeat dumping.

***B. Possible remedies***

Retroactive application of anti-dumping duties.

Duration of provisional measures.

**PUBLICATION AND EXPLANATION OF ANTI-DUMPING DETERMINATIONS*****A. Recommendation concerning transparency of anti-dumping proceedings (ADP/17)******B. Initiation of investigations***

Public notice of receipt of petitions.

Public notice of decisions to reject a petition.

Explanation of determinations to initiate investigations.

***C. Preliminary and final determinations***

Explanation of negative preliminary and final determinations.

***D. Undertakings***

Explanation of decisions to accept undertakings.

Public notice of contents of undertakings.

*E. Retroactivity*

Public notice of decisions to impose anti-dumping duties retroactively.

*F. Administrative reviews*

Public notice of initiation and results of administrative reviews.

**ANTI-DUMPING ACTION ON BEHALF OF A THIRD COUNTRY***A. Remedies in cases where material injury to a domestic industry is caused by dumped imports in a third country***JUDICIAL REVIEW OF ANTI-DUMPING DETERMINATIONS***A. Determinations which should be subject to judicial review**B. Parties which should have access to judicial review***DISPUTE SETTLEMENT***A. Review of Article 15 of the Anti-Dumping Code in the light of the results achieved in the Negotiating Group on Dispute Settlement**B. Specific issues relating to dispute settlement procedures under Article 15*

Nature of actions in respect of which the dispute settlement mechanism can be involved.

Timing of the establishment of panels.

Standing multilateral body to give advisory opinions.

Time period for the completion of the dispute settlement process.

Payment of compensation to exporters in cases where it is determined that investigations have been opened in a manner not in accordance with the applicable rules.

**TREATMENT OF LEAST DEVELOPED COUNTRIES**

Many attempts to nudge the negotiations forward by way of common negotiating texts were largely unsuccessful on account of differences among the participants' basic approaches to the negotiations. On the one hand, exporting participants, both developed and developing, proposed detailed formulations which importing participants considered to be unduly rigid and unrealistic. Their national administering authorities required room for flexibility in order to make decisions appropriate to the circumstances of the cases before them. Thus, they considered that several of the proposals would debase their national anti-dumping laws and circumscribe needed remedies to domestic industries buffeted by injurious dumping. On the other hand, the importing countries, particularly the major users of anti-dumping measures, wanted to update multilateral rules on anti-dumping that would cope with modern practices in their various guises of circumventing anti-dumping measures. Exporting participants criticized these proposals as going beyond the confines of the 1979 Code, or Article VI of the General Agreement, particularly

with respect to its basic precepts requiring the determination of the existence of dumping, of injury and their causal relationship before anti-dumping duties could be applied.

Positions on these issues progressively became so entrenched that the search for a common text for negotiations and efforts at forging compromises met with discouraging results. This explains why no formal texts for further negotiations were available at the Ministerial Meeting at Brussels in December 1990 to conclude the Uruguay Round negotiations. Despite the intensive efforts of mediators to break the impasse, the post-Brussels negotiations on anti-dumping were essentially no different from earlier phases of the negotiations. The text that emerged in the draft Final Act of December 1991 was an arbitrated text - itself a permutation of numerous informal drafts - considered unsatisfactory by many participants. Although several participants may have been prepared to tolerate the text, others were resolutely opposed to it on the grounds that it would unduly weaken their national anti-dumping systems. It was not sur-

prising therefore that the 1994 Agreement was achieved only during the final stretch of the Uruguay Round negotiations in December 1993.

In the course of the negotiations, dispute settlement procedures were increasingly invoked. Up to 1988, there had only been two anti-dumping disputes fully adjudicated under the General Agreement. The first dispute, involving anti-dumping duties imposed by Sweden on imports of stockings from Italy, was filed in 1954.<sup>77</sup> The second dispute took place in 1984 and concerned imports of transformers by New Zealand from Finland.<sup>78</sup> In both instances, the GATT resolved the disputes in favour of the complainants. The third dispute, filed by Japan in 1988, concerned the EEC regulation on imports of parts and components. This case, which was defended on grounds other than Article VI of the General Agreement, was also resolved in favour of the complainant.<sup>79</sup> A panel that was constituted under the auspices of the 1979 Code covered a complaint by Sweden on anti-dumping duties imposed by the United States on imports of certain stainless steel products.<sup>80</sup> The panel ruled in favour of Sweden on an important procedural requirement relating to the initiation of the anti-dumping investigation by United States authorities.

These recent cases appear to have paved the way for others also to invoke the provisions of the 1979 Code on consultations and dispute settlement. Together with disputes on countervailing duties, anti-dumping disputes, in their various stages, constitute the bulk of cases pending in the GATT system.<sup>81</sup>

The sudden upswing of panels to rule on disputes indicated the frustrations of exporters with anti-dumping investigations. It also illustrated that recourse to dispute settlement procedures could expose unwarranted anti-dumping actions, and that these actions could be reversed if concerned parties do not block adoption of panel reports. Rigorous standards applied by panels to interpret the 1979 Code may have elicited initiatives to explicitly define standards of review - which were eventually incorporated into the 1994 Agreement - that should be observed in the post-Uruguay Round trading system.

The Uruguay Round negotiations on anti-dumping differ from previous negotiations

in many respects. First, the negotiations have not been fully concluded. At their meeting in Marrakesh in April 1994 for the formal conclusion of the Round, the Ministers referred the matter of circumvention of anti-dumping duty measures for resolution by the committee established to supervise the implementation of the 1994 Agreement. Their decision was motivated by the desirability of the applicability of uniform rules in this area as soon as possible in view of the failure of negotiators during the Round to agree on specific language on the matter. Second, it took place in the context of negotiations on other subjects - trade in services, intellectual property rights, trade-related investments - that involved untouchable domestic prerogatives, eventually defined as "tradeable" for purposes of multilateral negotiations. The relevance of anti-dumping measures in the context of dramatic changes in world commerce and production was raised, but not addressed, in the negotiations. Third, the results of the negotiations would be implemented under the auspices of the World Trade Organization, which will administer a vastly improved system for the settlement of disputes, and where Ministers meeting periodically will have a greater say in the affairs of the Organization. These factors may influence the traditional episodic multilateral regulation of anti-dumping measures that characterized the pre-WTO trading system.

In retrospect, the controversy surrounding the negotiations generated widespread recognition, and appreciation, of the impact of anti-dumping measures on international trade and on the multilateral trading system. Depending on the viability of other contingency protection measures negotiated in the Uruguay Round - traditional safeguard measures, countervailing duties, and other safeguards specific to sectoral agreements such as agriculture and textiles - more national anti-dumping systems could sprout in the post-Uruguay Round trading system. Many developing countries which have dramatically liberalized their import regimes, including through extensive bindings of tariff rates, find themselves vulnerable to dumping and have introduced, or are in the process of introducing, anti-dumping legislation. This process is likely to be accelerated by the fact that all WTO members will be bound by the 1994 Anti-Dumping Agreement.

<sup>77</sup> GATT *BISD*, Third Supplement, June 1955, pp. 81-91.

<sup>78</sup> GATT *BISD*, Thirty-second Supplement, March 1986, pp. 55-70.

<sup>79</sup> GATT *BISD*, Thirty-seventh Supplement, July 1991, pp. 132-199.

<sup>80</sup> GATT, Committee on Anti-Dumping Practices, "United States - Imposition of Anti-Dumping Duties on Imports of Seamless Stainless Steel Hollow Products from Sweden, Report of the Panel" (ADP/47), 20 August 1990.

<sup>81</sup> See *Status of Work in Panels and Implementation of Panel Reports*, GATT document C/188, 10 June 1994.

## C. Problem areas and treatment

To improve and modernize the 1979 Tokyo Round Code, participants appraised basic principles and specific issues spanning the art and science of anti-dumping, such as: initiation and conduct of investigations; determination of the existence of dumping and of injury; calculation, imposition and collection of anti-dumping duties; duration, review and termination of anti-dumping measures; and settlement of disputes. Issues discussed virtually traced all the possible steps and decisions that national administering authorities would have to take to address domestic claims of injurious dumping. The degree of specificity of the proposals reflected in large part the unhappy experiences of economic operators subject to anti-dumping investigations. In addition, swift and effective action against various forms and techniques of circumventing anti-dumping duties was also considered. Given the universe of proposals to improve, clarify or expand the Code, the negotiations eventually pared them down to manageable proportions.

Proposals to reform the existing multilateral rules were anchored on the nature of anti-dumping measures as an administered remedy, susceptible to excessive vigilance and discretion. Thus, clear and more detailed rules were deemed necessary to enhance predictability and improve transparency, curb abuses, preclude arbitrary or biased calculations of price discrimination, discourage trivial complaints and, in general, ensure respect for the basic principles underlying Article VI of the General Agreement.

What follows below are brief discussions of some of the features of the 1994 Agreement. Since several jurisdictions were labelled major users of anti-dumping measures during the negotiations, the discussions mention their known current regulations and practices. This should not be taken however as a judgement on the nature of their anti-dumping systems.

### 1. Determination of dumping

#### (a) Volume of home market sales

Sales in the domestic market of the exporting country usually provide reference data for calculating normal value, and hence a comparison with the export price to determine a margin of dumping. Normal value may, how-

ever, be determined on the basis of other data "when there are no sales of the like product in the ordinary course of trade in the domestic market of the exporting country or when, because of the particular market situation or the volume of the sales in the domestic market of the exporting country, such sales do not permit a proper comparison ..." (Article 2, paragraph 2.2). Normal value may then be determined on the basis of either (i) export sales to an appropriate third country; or (ii) a constructed value of the product under investigation, i.e. the cost of production in the country of origin plus a reasonable amount for administrative, selling and general costs and for profits.

Normal value based on sales in the domestic market is preferred to the other alternatives, particularly constructed value. Constructed value entails complicated calculations that can lead to high normal values, thus increasing the prospect of unwarranted margins of dumping. Sales in the domestic market are hard data, and are therefore more reliable. To ensure the use of sales in the domestic market, exporters proposed predictable and transparent criteria for assessing whether sales in their domestic markets are sufficient for determining normal value.

The 1994 Agreement addresses this issue. Footnote 2 to paragraph 2.2 of Article 2 states that "Sales of the like product destined for consumption in the domestic market of the exporting country shall normally be considered a sufficient quantity for the determination of the normal value if such sales constitute 5 per cent or more of the sales of the product under consideration to the importing member, provided that a lower ratio should be acceptable where the evidence demonstrates that domestic sales at such lower ratio are nonetheless of sufficient magnitude to provide for a proper comparison". This provision incorporates the so-called '5 per cent representativity test', i.e. domestic sales will normally be considered as not allowing for a proper comparison if their volume is less than 5 per cent of the export quantity to the importing country.

The '5 per cent rule' is an improvement over the 1979 Code, and will harmonize current practices. Some investigating authorities calculate the 5 per cent threshold on the basis of sales by the exporting country to the market of the importing country; others calculate their threshold rates as a percentage of third country

exports, excluding the investigating importing country. The use of lower ratios of domestic sales as an exception to this rule may require them to change their practices if no exceptions are currently allowed. What is unclear in the rule is whether the 5 per cent threshold should be calculated on a quantity, model-by-model basis or on a like product-by-like product basis. This detail is important in cases where a foreign producer meets the 5 per cent threshold on its overall domestic sales of the like product, but does not meet it for some models, a situation that often happens in practice.

The 5 per cent threshold has already been used as a rule of thumb in the European Communities (EC) administrative practice, approved by the European judicial authorities. It can, therefore, be considered as a codification of existing EC practice. Similar rules applied in the United States and Canada may require modifications.

#### *(b) Sales below cost of production and constructed value*

Sales in the domestic market of the exporting country at prices below per unit average cost (fixed and variable) of production are disregarded in determining normal value on the grounds that they are not made in the ordinary course of trade. This practice is based on an 'Understanding' reached in 1978 among a few signatories to the Kennedy Round Code, although it was never incorporated into the 1979 Code. Exporting countries have criticized this practice as promoting high normal values, thus creating, or increasing, margins of dumping. The 1994 Agreement assimilates the aforementioned 'Understanding' into Article 2, paragraph 2.2.1.

The above provision stipulates several tests to be met before investigating authorities can proceed to disregard sales below cost: (i) such sales are made within an extended period of time, normally one year but no less than six months, in substantial quantities; and (ii) are at prices which do not provide for the recovery of all costs within a reasonable period of time. Additionally, if prices which are below per unit costs at the time of sale are above weighted average per unit costs for the period of investigation, such prices shall be considered to provide for recovery of costs within a reasonable period of time.

The tests for establishing substantial quantities are as follows:

- the weighted average selling price is below the weighted average per unit cost; or,
- the volume of sales below per unit costs represents not less than 20 per cent of the volume sold in transactions under consideration for the determination of the normal value.

In cases where sales below costs are disregarded, normal value may then be determined on the basis of remaining domestic sales, provided that they meet the 5 per cent representativity test.

The above provision leaves it to investigating authorities to define whether the expression "reasonable period of time" is identical to, or different from, the expression "extended period of time". It is also silent with respect to the calculation of substantial quantities, i.e. whether the measurement should be on a model-by-model, or product-by-product basis. A model-by-model measurement could be unduly restrictive. This provision, which appears to confirm the current practice of the EC, will require some modifications to United States and Canadian practice.

#### *(i) Cost allocation methods and start-up costs*

As said above, exporters are wary of constructed value because it involves complicated cost calculations and allocations. Issues raised in the negotiations pointed out the unfairness of certain methods in constructing normal value (such as minimum amounts for profit, as well as for general, selling and administrative expenses). The 1994 Agreement lays down in paragraph 2.2.1.1 of Article 2 detailed provisions regarding the calculation of costs for the purpose of determining sales below costs and of constructed value.

"For the purpose of paragraph 2, costs shall normally be calculated on the basis of records kept by the exporter or producer under investigation, provided that such records are in accordance with the generally accepted accounting principles of the exporting country and reasonably reflect the costs associated with the production and sale of the product under consideration. Authorities shall consider all available evidence on the proper allocation of costs, including that which is made available by the exporter or producer in the course of the investigation provided that such allocations have been historically utilized by the exporter or producer, in particular in relation to establishing appropriate amortization and depreciation periods and



allowances for capital expenditures and other development costs...".

The first sentence of the provision quoted above addresses current practices which hold that in cases of conflict between the exporting country's and importing country's generally accepted accounting principles, the latter shall prevail. Some investigating authorities normally (but not always) accept cost allocations made by exporters which are in accordance with the accounting principles of the country of exportation. The express wording inserted in the 1994 Agreement should make it more difficult for them to reject arbitrarily costs allocated in accordance with generally accepted accounting principles. However, as the Agreement also states that the costs should "reasonably reflect the costs associated with the production and sale of the product under consideration", it may not be very difficult to avoid the application of this provision in practice.

Allocations of costs in the context of calculating production costs in an anti-dumping investigation are important because the authorities must determine the per unit production costs of the product under investigation during the investigation period. The new rules will benefit exporters with sophisticated accounting systems.

Paragraph 2.2.1.1 of Article 2 also provides that "Unless already reflected in the cost allocations under this sub-paragraph, costs shall be adjusted appropriately for those non-recurring items of cost which benefit future and/or current production, or for circumstances in which costs during the period of investigation are affected by start-up operations". A footnote thereto states that "The adjustment made for start-up operations shall reflect the costs at the end of the start-up period or, if that period extends beyond the period of investigation, the most recent costs which can reasonably be taken into account by the authorities during the investigation".

As some jurisdictions allocate costs fully to the period during which they were incurred, this provision is helpful, although it has certain ambiguities which national implementing rules should clarify. For example, it does not stipulate how the adjustment for non-recurring cost items which benefit future and/or current production should be made. Similarly, where the start-up period extends beyond the investigation period, which will very often be the case, the guideline that costs should then reflect the most recent costs which can 'reasonably be taken into account by the authorities during the investigation' may be of limited significance. National implementing rules will also have to

define the 'circumstances in which costs during the period of investigation are affected by start-up operations'.

Adjustment for costs affected by 'start-up operations' is not currently granted in some jurisdictions. In the past, their investigating authorities have considered start-up costs as normal components of the cost of production in a market economy country, and treated such costs as actual expenses. This practice obviously made it easier to find sales below cost, thereby increasing the likelihood of a dumping finding as normal value would have to be constructed using very high start-up costs. Other major jurisdictions grant adjustments for start-up costs if it is demonstrated that this would be appropriate.

#### (ii) SGA and profit

Exporters have criticized practices of certain investigating authorities in deriving the constructed value of a product under investigation. For example, they claimed that statutory minimum amounts for selling, general and administrative expenses (SGA), and profit, being imposed arbitrarily, lead to calculation of artificial margins of dumping. If data show that SGA expenses actually incurred, or profits actually realized, are below the statutory minimum amounts, the latter are none the less used.

Paragraph 2.2.2 of Article 2 of the 1994 Agreement addresses this problem. It provides that in calculating constructed value, "the amounts for administrative, selling and general costs and for profits shall be based on actual data pertaining to production and sales in the ordinary course of trade of the like product by the exporter or producer under investigation". If it is not possible to determine the SGA and profit on this basis, this provision provides alternative methods, as follows:

- the actual amounts incurred and realized by the exporter or producer in question in respect of production and sales in the domestic market of the country of origin of the same general category of products;
- the weighted average of the actual amounts incurred and realized by other exporters or producers subject to investigation in respect of production and sales of the like product in the domestic market of the country of origin;
- any other reasonable method, provided that the amount for profit so established shall not exceed the profit normally realized by other exporters or producers on

sales of products of the same general category in the domestic market of the country of origin.

The provision does not specify whether the alternative methods should be used in the order of their enumeration. In the absence of an express requirement to that effect, investigating authorities are presumably at liberty to choose the method they prefer.

The above alternative methods largely correspond to the methods set out in the regulation of the EC. Paragraph 2.2.2 will require changes in United States law. Currently, the United States authorities use statutory minima of 8 and 10 per cent for profit, and for general, selling, and administrative expenses, respectively.

### (c) *Fair comparison*

Article 2:6 of the 1979 Code requires fair comparison between export price and domestic price, i.e. that these two variables be compared at the same level of trade, and due allowances made for differences in the circumstances of sales. Exporters have criticized the methods of comparison employed by some investigating authorities that essentially maximize the normal value while minimizing the export price. For example, direct and indirect selling expenses of, as well as a reasonable profit for, a related party in the importing country are deducted on the export side while only the direct selling expenses of the related party are deducted on the domestic side. Other investigating authorities allow an offset for indirect selling expenses incurred in the home market equal to the amount of indirect selling expenses incurred in the importing country.

The 1994 Agreement also requires, albeit more emphatically, fair comparison between normal value and export price. Paragraph 2.4 of Article 2 adds a number of factors to the list of differences that should be taken into account to ensure a fair comparison. Thus, allowances should be made for levels of trade, quantities, physical characteristics and any other differences which are demonstrated to affect price comparability.

As far as the level of trade allowance is concerned, certain investigating authorities seldom grant these adjustments. Only in the most extreme cases - such as where export sales are made on an Original Equipment Manufacturer (OEM) basis while domestic sales are made on an 'own brand basis' or vice versa - have differences in the level of trade been taken into

account. The same applies to allowances for differences in quantities, which in practice have always been rejected. The express wording inserted in paragraph 2.4 of Article 2 to make due allowances for differences in the level of trade and quantities may now require them to be less restrictive. It is also worth noting that regulations of certain investigating authorities contain a limited list of allowable adjustments while this provision contains what appears to be a non-exhaustive list of possible factors affecting price comparability. These authorities have frequently rejected claims for adjustments relating to differences in quantities or levels of trade on the basis that these adjustments do not appear in the list of allowable adjustments.

In contrast with the 1979 Code, the 1994 Agreement addresses for the first time the so-called 'symmetry' issue. Symmetry requires that if price comparability has been affected in cases where the export price is constructed, the investigating authorities shall either establish the normal value at the same level of trade as the export price or make due allowances to ensure price comparability.

Until recently, certain investigating authorities have refused any adjustments to the normal value when the export price is constructed, even though price comparability was clearly affected. Thus, they calculate the ex-works export price on the basis of the resale price to the first unrelated customer in the market of the importing country minus all direct and indirect costs incurred between importation and resale (therein included a reasonable amount for overhead and profits incurred by the related importer in the importing country), while the ex-works normal value is based on selling prices to first independent purchasers in the domestic market minus direct selling expenses only. This practice often resulted in a very biased comparison and led to the calculation of artificial margins of dumping.

In some recent cases, the investigating authorities were prepared to use a selective normal value or to grant adjustments in order to ensure price comparability. However, the use of a normal value at the same level of trade as the constructed export price, or the granting of allowances to ensure price comparability, is not a standard practice. Hopefully, the express wording in the 1994 Agreement in this respect will oblige them to adopt measures necessary to ensure fair price comparability in cases where a constructed export price is used.

Finally, it is worth noting that the 1994 Agreement (Article 2, paragraph 2.4) expressly mentions that "the authorities shall indicate to the parties in question what information is

necessary to ensure a fair comparison and shall not impose an unreasonable burden of proof on those parties". This burden of proof is less strict than the current practice of granting adjustments only when claimed and justified by the parties concerned.

#### *(d) Currency conversion*

The comparison between normal value and export price normally involves a conversion of currencies. Typically, prices of export transactions must be converted into the exporting country's currency in order to compare such prices with domestic home prices or domestic constructed value. Where foreign exchange rates fluctuate, currency conversion leads to artificial margins of dumping. Accordingly, the Agreement attempts to address this irregularity. After all, exchange rate fluctuations are more pronounced today than they were when the 1979 Code was drafted.

The 1994 Agreement introduces, in paragraph 2.4.1 of Article 2, requirements to govern the use of exchange rates in dumping calculations. In particular, it provides that the exchange rate on the date of sale should be used for the purpose of comparing prices. However, the exchange rate in forward contracts will be used if the export transaction is directly linked thereto. Certain investigating authorities have always ignored the use of exchange rates in forward contracts.

This provision also requires that fluctuations in exchange rates should be ignored, and that exporters should be allowed at least 60 days to adjust their export prices to reflect sustained movements in exchange rates during the period of investigation. Administering authorities may have to formulate detailed rules to carry out these requirements.

#### *(e) Averaging of prices*

The conventional definition of 'dumping' appears straightforward enough to suggest that calculation of a margin of dumping is elementary. If normal value exceeds export price, dumping exists; conversely, if normal value is equal to or less than export price, there is no dumping. In the real world of investigative techniques, the method used to compare these two variables may distort calculations of a margin of dumping. The 1979 Code does not prescribe any specific method of calculation other than to require proper and fair comparison.

Several investigating authorities customarily calculate a weighted-average margin of dumping by comparing a weighted-average

normal value with export prices on a transaction-by-transaction basis. Where negative dumping margins - the amount by which the normal value is below an export price - are found, they are ignored in deriving the weighted average margin of dumping, expressed in percentage terms. This method is considered biased. Accordingly, to preclude technical findings of dumping, the use of neutral methods of comparison were proposed - comparison of a weighted average normal value with a weighted average of export prices, or comparison of normal values and export prices on a transaction-to-transaction basis. (It may be noted that there would be no credits for negative margins of dumping under the transaction method.)

The 1994 Agreement provides in paragraph 2.4.2 of Article 2 that the margin of dumping shall "normally be established on the basis of a comparison of a weighted average normal value with a weighted average of prices of all comparable export transactions or by a comparison of normal value and export prices on a transaction-to-transaction basis". It permits an exception to this general rule where export prices differ significantly among different purchasers, regions or time periods. In such a case, a weighted average normal value may be compared with individual export transactions. The authorities will then have to explain why margins of dumping cannot be calculated on the basis of the other methods. Thus, while the Agreement provides an equitable methodology for calculating margins of dumping, it also gives the investigating authorities express authority to address 'hidden dumping' or 'selective dumping,' terminologies used to describe certain perceived practices of economic operators.

The provision on 'averaging' is a very important attempt to balance the competing concerns of the participants. To the extent that it encourages consistent application of the prescribed methods for calculating margins of dumping (in both investigations and administrative reviews), this provision may prove to be a real improvement. Recourse to the dispute settlement system should check frivolous invocation of the exception.

## **2. Determination of injury**

### *(a) Cumulation*

The 1994 Agreement codifies the practice of 'cumulative injury assessment', i.e. cumulation of imports from countries which are simultaneously subject to anti-dumping

investigations for the purpose of determining injury to domestic industry.

The consistency of cumulation practices with the 1979 Code had been much discussed, but not resolved, in the 1980s. Opinions of signatories to the Code differed on this matter. On the one hand, some criticized country cumulation practices on the grounds that they facilitate affirmative determination of injury (thus diluting the benefits of the injury test to individual signatories), to the detriment of exporting countries with low or insignificant market shares or whose export trends are declining. On the other hand, others justified country cumulation because it makes no difference whether a certain quantity originates from one source or from various sources; it is the combined effect of the dumped imports that injures the domestic industry. Moreover, they interpreted the silence of the Code on the matter as permitting the practice. The 1994 Agreement settles the question by incorporating the following provision in paragraph 3.3 of Article 3:

"Where imports of a product from more than one country are simultaneously subject to anti-dumping investigations, the investigating authorities may cumulatively assess the effects of such imports only if they determine that (a) the margin of dumping established in relation to the imports from each country is more than *de minimis* as defined in paragraph 8 of Article 5 and the volume of imports from each country is not negligible and (b) a cumulative assessment of the effects of the imports is appropriate in light of the conditions of competition between the imported products and the conditions of competition between the imported products and the like domestic product."

The impact of this provision has to be seen in the light of Article 5:8 which defines, for purposes of termination of anti-dumping investigations, thresholds of *de minimis* margins of dumping and negligible volumes of dumped imports. This provision may be criticized on grounds that the volume threshold is low or less meaningful than current practices in certain jurisdictions. Moreover, the impact of negligible imports is assessed separately from that of other imports. In this sense, the 1994 Agreement may make it less difficult to cumulate imports.

#### (b) Injury factors and causality analysis

One of the proposals of the participants in the negotiations pertained to margins analy-

sis. If the margin of dumping is less than the margin of price undercutting, factors other than the dumped imports may be causing injury to the domestic industry of the importing country. Thus, they proposed the inclusion of the magnitude of dumping among injury factors for purposes of examining the impact of dumped imports on the domestic industry. Paragraph 3.4 of Article 3 of the 1994 Agreement accordingly embodies this factor:

The examination of the impact of the dumped imports on the domestic industry concerned shall include an evaluation of all relevant economic factors and indices having a bearing on the state of the industry, including actual and potential decline in sales, profits, output, market share, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; *the magnitude of the margin of dumping*; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investments. This list is not exhaustive, nor can one or several of these factors necessarily give decisive guidance (emphasis added).

This provision mandates margins analysis, which is permissible, but not obligatory, in certain jurisdictions. Other jurisdictions do not carry out such analysis at all. Instead, they compare dumping margins with injury margins, and anti-dumping duties are based on the lower of the two.

The weight that investigating authorities of importing countries should attach to margins analysis is nowhere indicated in the above provision. Ideally, the magnitude of dumping ought to have a major influence where the discrepancy between the margin of dumping and undercutting is substantial and the dumping margin itself is more than *de minimis*.

Another concern raised by participants in connection with injury relates to weak causality analysis between dumped imports and injury. Paragraph 3.5 of Article 3 shows an attempt to address this concern by providing that "the demonstration of a causal relationship between the dumped imports and the injury to the domestic industry shall be based on an examination of all relevant evidence before the authorities". Moreover, Article 12 (Public Notice and Explanation of Determinations) requires investigating authorities, in public notices or reports, to make information available and explain their determinations, including "considerations relevant to the injury determination" (paragraph 12.2.1(iv)). These improvements should prevent arbitrary or opaque determinations of injury to domestic industry.

### (c) Threat of injury

The provision of the 1979 Code is concise with respect to the determination of threat of injury to domestic industry. The 1994 Agreement expands on the 1979 Code by recommending in paragraph 3.7 of Article 3 that investigating authorities consider several illustrative factors in making their determinations, as follows:

- "a significant rate of increase of dumped imports into the domestic market indicating the likelihood of substantially increased importation;
- sufficient freely disposable, or an imminent, substantial increase in, capacity of the exporter indicating the likelihood of substantially increased dumped exports to the importing member's market, taking into account the availability of other export markets to absorb any additional exports;
- whether imports are entering at prices that will have a significant depressing or suppressing effect on domestic prices, and would likely increase demand for further imports; and
- inventories of the product being investigated".

These factors mirror those that were incorporated in a recommendation concerning determination of threat of material injury that was adopted in the Committee on Anti-Dumping Practices in October 1985.<sup>82</sup>

### 3. Initiation and conduct of anti-dumping investigations

Article 5 of the 1994 Agreement requires that written applications for anti-dumping investigations shall contain more detailed information on such issues as the existence of dumping and injury to the domestic industry. It also requires that investigating authorities "shall examine the accuracy and adequacy of the evidence provided in the application to determine whether there is sufficient evidence to justify the initiation of an investigation" (paragraph 5.3). Although the requirement with respect to information is somewhat weakened by

the expression 'such information as is reasonably available to the applicant', improvements under Article 5 should contain trivial applications for anti-dumping investigations.

#### (a) Complaint on behalf of a domestic industry

Article 5:1 of the 1979 Code provides that "an investigation to determine the existence, degree and effect of any alleged dumping shall normally be initiated upon a written application by or on behalf of the domestic industry". The term 'industry' takes its meaning from the definition of domestic industry in Article 4:1 which states that in determining injury "the term domestic industry shall be interpreted as referring to the domestic producers as a whole of the like products or to those of them whose collective output of the products constitutes a major proportion of the total domestic production of those products, ...".

The expression 'a major proportion' had been difficult for signatories to the 1979 Code. Accordingly, participants proposed numerical standards to define the expression. Compounding the lack of agreement on this issue is the practice of certain investigating authorities to presume that a case is brought on behalf of the domestic industry unless there is active opposition to it. This raised questions on the representativeness of applications for anti-dumping investigations and the role of investigating authorities in ascertaining the validity thereof before initiating investigations. The 1994 Agreement settles these and other subsidiary issues.

Article 5 of the Agreement requires that an investigation shall not be initiated unless investigating authorities have determined that an application has been made by or on behalf of the domestic industry. This settles the question of presumption of industry support. In addition, Article 5 addresses the problem of the notion of 'a major proportion' of the domestic industry by defining it as those domestic producers whose collective output represents more than 50 per cent of the total production of the like product produced by that portion of the domestic industry expressing either support for or opposition to the application. Thus, producers which do not make their positions known on an application for investigation will not be included in the calculation. Article 5, footnote 14, further notes that "...employees of domestic producers of the like product or rep-

<sup>82</sup> GATT document ADP/25, 31 October 1985.

representatives of those employees may make or support an application for an investigation...".

In any event, domestic producers expressly supporting an application have to account for a minimum threshold of 25 per cent of total production of the like product produced by the domestic industry.

The Agreement will bring much needed discipline and certainty to this area of anti-dumping administration. It may, however, make it less difficult to obtain standing if there are signatories to the 1979 Code applying stringent thresholds (whether unofficially or officially) of 50 per cent of total domestic production.

#### (b) *De minimis* dumping margins and import volumes

In contrast with the 1979 Code, which exhorted immediate termination in cases where the margin of dumping or the volume of dumped imports, actual or potential, or the injury is negligible, the 1994 Agreement provides quantitative criteria for immediate dismissal of anti-dumping cases (Article 5, paragraph 5.8). These criteria, which should have been more meaningful, are as follows:

- the margin of dumping is *de minimis*, i.e. less than 2 per cent, expressed as a percentage of the export price; or
- the volume of dumped imports from a particular country accounts for less than 3 per cent of imports of the like product in the importing member. However, this rule will not be applicable when countries each having less than 3 per cent of the imports of the like product in the importing member collectively account for more than 7 per cent of imports of the like product in the importing member; or
- the injury is negligible.

Both the EC and the United States currently apply the concept of *de minimis* dumping margins. In the EC, the threshold is 1.5 per cent of the c.i.f. export price. It will thus be required to increase slightly its current standard. The EC furthermore tends to terminate proceedings on the basis of no injury if the market share of any particular country is less than 1.5 per cent of total EC consumption. In the United States, the *de minimis* dumping margin threshold is 0.5 per cent.

Under the current EC practice, the *de minimis* import volume is 1.5 per cent of total EC consumption. This appears to be more

generous than the *de minimis* import volume (in terms of import shares) provision in the Agreement. In other important jurisdictions, there is also a negligibility standard related to volume which has, for example, applied where individual sources have 0.9 per cent of consumption. The *de minimis* standard in terms of volume therefore appears weak in the 1994 Agreement.

#### (c) *Notification*

Article 5 of the Agreement obliges authorities, after receipt of a properly documented application and before proceeding to initiate an investigation, to notify the government of the exporting country concerned. This procedural requirement should prove helpful to enterprises, in view of the tight deadline for responding to questionnaires (at least 30 days from the date of receipt thereof) as provided for in Article 6 (Evidence). However it is unclear how far in advance the exporting country government may be notified of the initiation of a proceeding. The current practice of some jurisdictions is to inform exporting country governments of proceedings upon initiation. In other jurisdictions, a complaint that is filed is publicly available on the day of filing.

### 4. Evidence

#### (a) *Best information available*

Of possible practical benefit to investigated parties, particularly small enterprises, is paragraph 6.8 of Article 6 regarding the provision of information to investigating authorities. Complaints abound about the use of information made available by petitioners in instances where the investigated parties do not cooperate or are deemed not to provide information according to the specifications of investigating authorities. Best information available has earned the designation of 'worst information possible' from the perspective of investigated parties. The provision states as follows:

In cases in which any interested party refuses access to, or otherwise does not provide, necessary information within a reasonable period or significantly impedes the investigation, preliminary and final determinations, affirmative or negative, may be made on the basis of the facts available. The provisions of Annex II shall be observed in the application of this paragraph.

Annex II of the Agreement provides guidelines that spell out the consequences of delayed submission of required information, while alleviating the practical burdens on investigated parties, and controlling arbitrary or capricious rejection of information submitted by them.

### *(b) Sampling*

The 1994 Agreement provides that, as a rule, an individual dumping margin will be calculated for each known exporter or producer under investigation (paragraph 6.10 of Article 6). However, it permits investigating authorities to limit their examination by using 'statistically valid' samples (or the largest volume of exports from the country in question) which can reasonably be investigated in cases where the number of exporters, producers, importers or types of products involved is so large as to make the calculation of individual margins impracticable.

This provision strives to balance the interests of producers in exporting countries, producers in importing countries (so that investigations can be concluded expeditiously), and investigating authorities (for reasons of administrative convenience). The 1979 Code contains no provision on sampling; the 1994 Agreement tends to codify existing practices.

Additionally, paragraph 6.10.1 of Article 6 states that "Any selection of exporters, producers, importers or types of products made under this paragraph shall preferably be chosen in consultation with and with the consent of the exporters, producers or importers concerned". One major jurisdiction has in practice always sought the express agreement of exporters before limiting their investigations to a sample.

After the authorities have selected a sample, paragraph 6.10.2 of Article 6 offers an opportunity, in principle, for calculating individual margins of dumping for interested parties not initially selected in the sampling. It provides that "Voluntary responses shall not be discouraged". At present, voluntary responses are accepted in many major jurisdictions. An interested party which is willing to cooperate and participate in a proceeding should be able to obtain its own dumping margin.

## **5. Provisional measures**

There is one innovation of practical interest in Article 7: the period of validity of provisional measures may be extended up to nine months in cases where the authorities ex-

amine whether a duty lower than the margin of dumping would be sufficient to remove injury. Under the 1979 Code, the maximum period of validity of provisional measures was six months. Thus, the EC, which applies the 'lesser duty' rule, would be authorized to extend the period of validity of provisional duties. Foreign producers or exporters should benefit from this change, which should enable the authorities to effect a thorough investigation after the preliminary investigation.

## **6. Imposition and collection of anti-dumping duties**

### *(a) Refund of excess duties paid*

One of the basic principles underlying Article VI of the General Agreement stipulates that an anti-dumping duty not be greater in amount than the margin of dumping. The 1979 Code expands on this by requiring quick reimbursement of excess duties if duties collected exceed the actual margin of dumping. To address delays in reimbursement of excess duties paid, exporters proposed time-limits for refund proceedings.

An issue related to the general problem of delays in reimbursement pertains to the practice of deducting anti-dumping duties paid by importers as a cost in refund proceedings. Under this practice, which mainly occurs when foreign producers sell through related parties in the importing country, the export price is normally constructed, and all costs incurred between importation and resale by the related party, as well as the profit of that party, are deducted from the resale price to the first independent customer. This means that the related party has to increase its resale price by twice the amount of the anti-dumping duties in order to obtain a refund (which made refunds difficult to obtain). Exporters were concerned about this practice, and proposed that Code provisions should be clarified accordingly.

With respect to reimbursements, the 1994 Agreement introduces time-limits for refund proceedings, which should normally take 12 months, and in no case exceed 18 months. The Agreement also tries to resolve the thorny issue of whether anti-dumping duties paid by related importers should be deducted as a cost in the computation of the constructed export price for the purpose of the refund determination.

According to paragraph 9.3.3 of Article 9, the export price should be calculated, in

principle, with no deduction for the amount of anti-dumping duties paid. However, this provision provides for certain ambiguous conditions to be fulfilled to apply this non deductibility rule. The extent to which the jurisdiction concerned will be required to change its practice is therefore unclear. For example, it must be proved that the movement in the resale price is duly reflected in subsequent selling prices. This may be a difficult task because related importers will have to convince their independent purchasers to cooperate with the refund application. In addition, related importers or the parent company do not control the pricing practices of their independent customers.

### (b) Duty for non-sampled producers

In situations where authorities resort to sampling (paragraph 6.10 of Article 6), the question of the level of duties applicable to producers not included in the sample arises. Paragraph 9.4 of Article 9 prescribes two methods for calculating these duties, which shall not exceed:

"the weighted average margin of dumping established with respect to the selected exporters or producers or,

where the liability for payment of anti-dumping duties is calculated on the basis of a prospective normal value, the difference between the weighted average normal value of the selected exporters or producers and the export prices of exporters or producers not individually examined, provided that the authorities shall disregard for the purpose of this paragraph any zero and *de minimis* margins and margins established under the circumstances referred to in paragraph 8 of Article 6. The authorities shall apply individual duties or normal values to imports from any exporter or producer not included in the examination who has provided the necessary information during the course of the investigation, as provided for in subparagraph 10.2 of Article 6".

In calculating the duty to be imposed with respect to non-sampled producers, zero and *de minimis* margins, as well as margins established on the basis of the best information available, must be disregarded. Excluding the margins based on best information available for the purpose of the calculation of the weighted average dumping margin is fair because producers who have not been investigated should not suffer from the consequences of non-cooperation by others to furnish required

data. The exclusion of zero and *de minimis* margins (which are currently not excluded in Canada, for example) is inappropriate because it can lead to artificially higher dumping margins for the companies that were not investigated.

At present, several anti-dumping systems impose a so-called 'residual duty' with respect to three categories of producers/exporters: (i) non-cooperating producers; (ii) newcomers, i.e. producers that did not export during the investigation period but only started exporting afterwards; (iii) cooperating but non-investigated producers.

In one of these systems, the residual duty for all three categories is equal to the weighted average duty imposed on cooperating investigated producers, without taking into account producers with a zero or a *de minimis* dumping margin. As paragraph 9.4 of Article 9 would apply to the weighted average dumping margin to non-sampled producers, excluding, however, dumping margins based on the best information available rule and zero or *de minimis* dumping margins, this provision codifies this practice.

In another major anti-dumping system, the residual duty applied to non-cooperating producers and newcomers is equal to the highest duty imposed with respect to any cooperating producer. It has been argued that to rule otherwise would constitute a bonus for non-cooperation. The duty applied to non-sampled producers (third category), according to the latest policy, is the weighted average duty imposed on cooperating producers, including producers with a zero or *de minimis* dumping margin, on a country-by-country basis. Thus, Article 9.4 is actually less generous than this present practice.

### (c) Newcomers

As indicated above, exporters or producers that have not exported during the original period of investigation are subject to 'residual duties' in several anti-dumping systems. Paragraph 9.5 of Article 9 reflects an effort to rectify this unfairness. It sets forth two requirements for exporters or producers to qualify as newcomers:

- no exports of the product during the investigation period; and,
- no relationship to any of the producers/exporters subject to anti-dumping duties.



An accelerated review is to be carried out to determine individual margins of dumping for any exporter or producer meeting these requirements, and they will not be subject to any anti-dumping duty from the date of initiation of the accelerated newcomer review until the date of completion of the review. The authorities may withhold appraisal and/or request a guarantee to ensure that, if dumping is found with respect to the exporter or producer, the authorities can collect the duties retroactively to the date of initiation of the newcomer review.

In one of the major anti-dumping systems, residual duties imposed on newcomers are the weighted average duty imposed with respect to cooperating producers, excluding those producers with zero or *de minimis* dumping margins. In another anti-dumping system, newcomers are subjected to the highest duty imposed with respect to any cooperating producer. In the latter, the effect of its approach has been alleviated by opening the possibility for newcomers to ask for expedited reviews. This was necessary because, under its regulations, foreign producers or exporters have to wait at least one year from the date of imposition of definitive duties (or acceptance of undertakings) before they can ask for a review.

As set out originally, the conditions for requesting an expedited newcomer review required the newcomer to provide evidence that it started exporting after the imposition of the anti-dumping duty. This requirement was impossible to meet as the residual duty *de facto* precluded most newcomers from exporting in the first place. However, in the first newcomer review applications examined by the authorities, they adopted a flexible attitude by considering it sufficient if the newcomer could show evidence of plans to export. As in such cases an export record would be lacking, and consequently calculation of any dumping margin was impossible, the authorities imposed anti-dumping duties in the form of a minimum price equal to the normal value found for the newcomer concerned. The authorities did require the newcomer to pay the anti-dumping duties as long as it had not completed the newcomer review.

Paragraph 9.5 of Article 9 is an endorsement of the fundamentals of the newcomer review possibility developed in the EC practice. There is one difference though: this provision only allows the importing country to withhold appraisal or to request guarantees during the review, while under current EC practice newcomers remain subject to the residual duty until the conclusion of the newcomer review.

## 7. Sunset clause

Several participants in the negotiations proposed a 'sunset clause' to clarify the principle in the 1979 Code that "an anti-dumping duty shall remain in force only as long as, and to the extent, necessary to counteract dumping which is causing injury". In support of this proposition, they cited instances of anti-dumping measures being maintained indefinitely or for very long periods, even if such measures were no longer necessary or justified in the light of market conditions. Hence, a 'sunset clause' should mandate automatic termination of such measures within a reasonable period of time.

Paragraph 11.3 of Article 11 of the 1994 Agreement provides that any definitive anti-dumping duty is to be terminated on a date not later than five years from its imposition unless the authorities determine, in the context of a review, that the "expiry of the duty would be likely to lead to continuation or recurrence of dumping and injury". For purposes of recording the date of imposition of outstanding anti-dumping measures (the 'sunset' provision is also applicable to price undertakings), the Agreement considers the date to be not later than the entry into force of the Agreement Establishing the World Trade Organization, except for those measures already covered by existing sunset provisions of domestic legislations.

The 1994 Agreement would codify the EC's and Canada's sunset clause period of five years. Experience with the sunset clause in these jurisdictions has been positive, a considerable number of measures having expired since the 1980s because of lack of interest on the part of domestic industry in their continuation. However, in Canada, in particular, where industry does support extension, the standard for extension has been evidence of a likelihood to resume dumping and the vulnerability of the industry to such renewed dumping. It is likely that countries that do have the sunset clause will follow the Canadian approach.

Arguably, the standard of review in this provision - that "expiry of the duty would be likely to lead to continuation or recurrence of dumping and injury" - is somewhat hypothetical. None the less, the provisions of Article 6 on evidence and procedure will be applicable to these reviews, as specified in paragraph 11.4 of Article 11. It will be interesting to see the de-

tails of the standard of sunset reviews in national implementing legislations. At the very least, the sunset clause in the 1994 Agreement has increased the prospect of eliminating permanent anti-dumping duties in those countries currently without sunset clauses in their legislations.

## **8. Consultation and dispute settlement**

The consultation and dispute settlement provisions of the 1994 Agreement and of the 1979 Tokyo Round Code differ in very many important respects, on account primarily of major changes in the trading system brought about by the Uruguay Round negotiations. In the context of the single undertaking philosophy of the Round, acceptance of the results thereof as a whole is obligatory (with the exception of the Plurilateral Trade Agreements) under the terms of the Final Act and of the WTO Agreement. Hence, WTO members' rights and obligations will be standardized and unified and, in the particular case of anti-dumping measures, their rights and obligations will reside in Article VI of the General Agreement 1994 in conjunction with the 1994 Agreement.

Under the previous GATT system, contracting parties not signatories to the 1979 Code had their rights and obligations on anti-dumping lodged under Article VI of GATT 1947, whereas contracting parties signatories to the Code had two sets of rights and obligations: one, as Code signatories, and, two, as contracting parties to GATT 1947. In so far therefore as consultations and dispute settlement procedures were concerned in the GATT system, the prospect of 'forum-shopping' was somewhat problematic, notwithstanding the admonition in the 1979 Code that if disputes arise between parties relating to rights and obligations under the Code, they should complete the dispute settlement procedures therein before availing themselves of any rights which they have under GATT. Forum-shopping will therefore be arrested under the WTO system, in view particularly of the Understanding on Rules and Procedures Governing the Settlement of Disputes.

This Understanding, annexed to the Agreement Establishing the World Trade Organization, provides that its rules and procedures shall apply to disputes brought pursuant to the consultation and dispute settlement pro-

visions of the 'covered agreements', among which is the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade of 1994. The Understanding further stipulates that its rules and procedures shall apply subject to such special or additional rules and procedures on dispute settlement contained in the covered agreements, and to the extent that there is a difference between its rules and procedures and the special or additional rules and procedures, the latter will prevail. The special or additional rules and procedures of the 1994 Agreement are contained in paragraphs 17.4 to 17.7 of Article 17 thereof (see box 11).

From a general standpoint, perhaps the most important feature of the Understanding, that will safeguard the reliability of the trading system to a great extent, pertains to the adoption of panel reports. Under Article 16 of the Understanding, adoption of panel reports is automatic, unless either of the disputants appeals the report to the standing Appellate Body, or the Dispute Settlement Body (DSB) decides not to adopt the report by consensus. Likewise, adoption of the Appellate Body report is automatic unless the DSB decides not to adopt the same by consensus.

Under this process of panel report adoption, which is subject to maximum time-limits, the status of panel reports will be in a sense preordained - either they are adopted or rejected. WTO members which believe that panel reports are defective or are otherwise domestically-charged, will have the opportunity to appeal their case. Following completion of the appeals process, no WTO member may then use its weight to delay or block the adoption of Appellate Body reports unfavourable to its position, and thus prevent the complaining member from obtaining satisfaction against an offending measure, or prevent the respondent member from having its position sustained by the DSB. It is probably premature to predict that this will indeed be the case. In the context of the 1994 Agreement on anti-dumping, the first case to test its provisions through the Understanding will shape new traditions on dispute settlement. Hopefully, the improved system on dispute settlement will induce more careful application of anti-dumping measures by broadening confidence in challenging unwarranted anti-dumping actions.

With respect to the provisions of the Agreement itself, there are two changes that are immediately recognizable. First, the deletion of the conciliation phase provided for in the 1979 Code. Second, the explicit definition of standards of review by panels.

**ARTICLE 17 CONSULTATION AND DISPUTE SETTLEMENT**

17.1 Except as otherwise provided herein, the Dispute Settlement Understanding is applicable to consultations and the settlement of disputes under this Agreement.

17.2 Each Member shall afford sympathetic consideration to, and shall afford adequate opportunity for consultation regarding, representations made by another Member with respect to any matter affecting the operation of this Agreement.

17.3 If any Member considers that any benefit accruing to it, directly or indirectly, under this Agreement is being nullified or impaired, or that the achievement of any objective is being impeded, by another Member or Members, it may, with a view to reaching a mutually satisfactory resolution of the matter, request in writing consultations with the Member or Members in question. Each Member shall afford sympathetic consideration to any request from another Member for consultation.

17.4 If the Member that requested consultations considers that the consultations pursuant to paragraph 3 have failed to achieve a mutually agreed solution, and if final action has been taken by the administering authorities of the importing Member to levy definitive anti-dumping duties or to accept price undertakings, it may refer the matter to the Dispute Settlement Body ("DSB"). When a provisional measure has a significant impact and the Member that requested consultations considers that the measure was taken contrary to the provisions of paragraph 1 of Article 7, that Member may also refer such matter to the DSB.

17.5 The DSB shall, at the request of the complaining party, establish a panel to examine the matter based upon:

- a written statement of the Member making the request indicating how a benefit accruing to it, directly or indirectly, under this Agreement has been nullified or impaired, or that the achieving of the objectives of the Agreement is being impeded, and
- the facts made available in conformity with appropriate domestic procedures to the authorities of the importing Member.

17.6 In examining the matter referred to in paragraph 5:

- in its assessment of the facts of the matter, the panel shall determine whether the authorities' establishment of the facts was proper and whether their evaluation of those facts was unbiased and objective. If the establishment of the facts was proper and the evaluation was unbiased and objective, even though the panel might have reached a different conclusion, the evaluation shall not be overturned;
- the panel shall interpret the relevant provisions of the Agreement in accordance with customary rules of interpretation of public international law. Where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation, the panel shall find the authorities' measure to be in conformity with the Agreement if it rests upon one of those permissible interpretations.

17.7 Confidential information provided to the panel shall not be disclosed without formal authorization from the person, body or authority providing such information. Where such information is requested from the panel but release of such information by the panel is not authorized, a non-confidential summary of the information, authorized by the person, body or authority providing the information, shall be provided.

The elimination of the conciliation phase of the consultation and dispute settlement procedures as established in the 1979 Code indicates a dissatisfaction with its operation and its unintended effect of delaying resolution of disputes. Under those procedures, if the Committee fails to effect a mutually satisfactory

solution between the parties involved, the aggrieved party may resort to panel adjudication only after three months have elapsed following conciliation efforts in the Committee. The elimination of the conciliation phase will obviously speed up recourse to intervention by panels.

The standards of review under the 1994 Agreement differ somewhat from the standard set out in Article 11 (Function of Panels) of the Understanding. Article 11 states as follows:

*"The function of panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, a panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements. Panels should consult regularly with the parties to the dispute and give them adequate opportunity to develop a mutually satisfactory solution"* (emphasis added).

Paragraph 17.6(i) of Article 17 of the 1994 Agreement provides that:

*"in its assessment of the facts of the matter, the panel shall determine whether the authorities' establishment of the facts was proper and whether their evaluation of those facts was unbiased and objective. If the establishment of the facts was proper and the evaluation was unbiased and objective, even though the panel might have reached a different conclusion, the evaluation shall not be overturned"*.

Moreover, paragraph 17.6(ii) thereof provides that:

*"the panel shall interpret the relevant provisions of the Agreement in accordance with customary rules of interpretation of public international law. Where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation, the panel shall find the authorities' measure to be in conformity with the Agreement if it*

*rests upon one of those permissible interpretations"*.

The above standards appear to leave open the possibility of multiple interpretations of the provisions of the 1994 Agreement and are clearly more flexible with respect to the application of anti-dumping measures. However, it is unclear to what extent this provision will influence panel rulings. It can, moreover, be doubted whether the application of this provision would have significantly affected the outcome of recent panel rulings overturning decisions reached by investigating authorities.

The explicit definition of standards may have been a response to concerns by participants that panels have overstepped their functions in those areas of the 1979 Code that were vague or that lent themselves to various ways of implementation. Moreover, the nature of anti-dumping measures as a right of contracting parties and as an exception to the fundamental principles of the General Agreement has been subject to differing interpretations. It can therefore be said that the 1994 Agreement settles these questions.

At their meeting at Marrakesh in April 1994 to bring the Uruguay Round to a formal conclusion, Ministers took several decisions bearing on dispute settlement in other areas. First, they decided that "The standard of review in paragraph 6 of Article 17 of the Agreement on Implementation of Article VI of GATT 1994 shall be reviewed after a period of three years with a view to considering the question of whether it is capable of general application". Second, they also recognized, "with respect to dispute settlement pursuant to the Agreement on Implementation of Article VI of GATT 1994 or Part V of the Agreement on Subsidies and Countervailing Duties, the need for consistent resolution of disputes arising from anti-dumping and countervailing duty measures".

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## D. Conclusions

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The quick survey above of the changes incorporated into the 1994 Agreement shows sufficiently clearly that an attempt has been made to improve on vague or imprecise formulations in the 1979 Code. In several instances, some rules have been clarified or made precise through numerical standards. Procedural requirements have been amplified in greater detail with respect, for example, to initiation of in-

vestigations, evidence and, notably, transparency. Attempts to control some controversial national practices have succeeded to a certain extent but at the price of codifying them into the Agreement.

The explicit standards of review on settlement of disputes constitute a unique feature of the 1994 Agreement, reached through

an unavoidable compromise in order to conclude the Uruguay Round. These standards, which would essentially require greater deference to decisions by national administering authorities, have to be judged in the light of the automatic adoption of panel reports in the Understanding on Rules and Procedures Governing the Settlement of Disputes. Moreover, whether they will insulate inordinately the national regulations of all WTO members from successful challenges will have to be weighed against the clearer rules developed in several areas. In such instances, the standards would probably not make a difference. It is in those areas where the rules remain vague that the standards will make a real difference. Practice and case law should in due course reveal the full implications of these standards.

Improvements in the Agreement on details should in their totality constrain administrative discretion and zeal. As might be expected in negotiations covering anti-dumping, there are qualifying clauses to permit continuation of restrictive application of the rules. The practical impact of the improvements should not be underestimated, but nor should it be overestimated. The improvements should not be underestimated if they are faithfully reflected in implementing laws and regulations. Conversely, they should not be overestimated if implementing regulations reverse what was agreed in the negotiations. Hence, it is only in the details of national anti-dumping laws and administrative regulations and their subsequent implementation in practice that the full consequences of the new rules will be known.

There is no doubt that the 1994 Agreement embodies many improvements that were proposed by a number of participants in the negotiations. At the same time, the codification in the Agreement of certain practices deemed protectionist could be criticized as legitimizing them multilaterally, but it could also be argued that it is better to control them in some fashion multilaterally, mainly through procedural safeguards (which, if appropriately exploited, could make a difference in favour of exporting countries).

The Uruguay Round negotiations on anti-dumping measures represent a 'deepening' of the multilateral rules and disciplines, which should contain excessive administrative zeal, reduce scope for unilateral interpretations, promote predictability and inspire confidence in the dispute settlement process. In general, therefore, the Agreement should reduce the scope for abuse in the application of anti-dumping measures for reasons other than to remedy the injurious effect of dumping on do-

mestic industries. These assertions, couched more in terms of hopes, are premised on the will of governments to resist vigilant domestic interests deeply attached to maintaining anti-dumping measures as a tool for selective safeguards against import competition, whether or not imports are 'fairly traded'. There is no denying that domestic interests will test the rules severely.

In the context of the WTO system, vigilance can be exercised through the institution established in the 1994 Agreement to supervise its implementation. The Committee on Anti-Dumping Practices under the 1979 Tokyo Round Code did useful work on several issues which found their way into the 1994 Agreement. That Committee also regularly deliberated on legislation and implementing regulations of Code signatories. If the Committee of the same name in the 1994 Agreement continues the past tradition, full participation in its deliberations, including in the reviews of legislation and regulations, is necessary. Also, vigilance should begin at the start of applications for investigations. Participation in national anti-dumping investigations, although expensive, is undoubtedly unavoidable.

If anti-dumping measures become the preferred instrument of protection for many WTO members in the post-Uruguay Round era, commensurate resources should be poured into national structures to administer anti-dumping investigations, particularly by those members that have no tradition of practising the art and science of applying anti-dumping measures. Otherwise, improperly imposed measures could be reversed under dispute settlement proceedings. As anti-dumping measures are the tools of protection of the elite, their systems, practices and traditions readily serve as models. However, the 1994 Agreement should remain the basis for ensuring the conformity of national legislation and implementing rules and regulations.

There has been a tendency in some quarters to minimize the significance of anti-dumping measures as a barrier to trade by citing the insignificant percentage of imports, even those of the main users of anti-dumping duties actually subject to anti-dumping duties. This conceals the real protective effect of anti-dumping actions, which are usually targeted on a number of sensitive product categories from specific countries (described as "laser beam" protection). The objective of the industries initiating anti-dumping actions is not only the imposition of anti-dumping duties or price undertakings from exporters. It is also to convince all foreign suppliers of a given product to

raise their export prices. This obviously penalizes new entrants to the market.

Anti-dumping legislation is seen as a defence against predatory pricing and other anti-competitive practices. However, anti-dumping legislation can be used to preserve anti-competitive situations (i.e. dominant shares in the domestic market) and encourage anti-competitive behaviour (i.e. price fixing). Thus, the accelerating debate on multilateral compe-

tition rules will be of particular relevance for anti-dumping legislation.

In this context, it should be stressed that until recently, anti-dumping duties have been applied by only a very limited number of countries. With the adoption of anti-dumping legislation by many developing countries, and the perception that anti-dumping measures are the "trade remedy" subject to discipline under the WTO, the widespread resort to anti-dumping actions may prove a major challenge to the WTO. ■

## THE EVOLUTION OF MULTILATERAL TRADE POLICY RULES ON SUBSIDIES

### A. Introduction

This chapter examines the evolution of current trade policy rules on subsidies from the provisions first set out in GATT 1947 to the 1979 Tokyo Round Code and finally to the Uruguay Round Agreement on Subsidies and Countervailing Measures.<sup>83</sup> It should be noted that it is only with the latest Agreement - and taking into account the provisions on subsidies in the Uruguay Round Agreement on Agriculture, and the negotiations still under way for an Agreement on Civil Aircraft and for a Multilateral Steel Agreement - that a comprehensive negotiated set of rules on subsidies has begun to emerge.

While subsidies - in the form of forgiveness of tax, grants of land or buildings or, more frequently, grants of sole rights to trade in a given territory or product - may well be as ancient a practice as import tariffs, commercial policy has, until fairly recently, treated subsidies in an incomplete and fragmentary fashion, while dealing with tariffs in a very detailed, product-specific manner.<sup>84</sup> Systems of imposts on imported goods (and on ships carrying such goods) originated primarily as sources of revenue. They were not unlike tolls on roads or bridges in that, before income tax was introduced together with the administrative

machinery necessary to levy and collect it, the simplest method of collection was to fix points where goods in transport could be controlled and fees paid. Until this century customs duties and sumptuary taxes (on tobacco, alcohol, coffee, etc.) were the principal sources of revenue for States and, therefore, the main subject of economic negotiation among them. Aside from matters of war and peace, and the defining of territorial sovereignty, foreign policy was, for many countries, particularly smaller countries, largely about the levying of tariffs and bargaining over tariff levels with other countries.

Thus GATT 1947, essentially the commercial policy provisions taken over from the larger context of the discussions on the proposed International Trade Organization at Havana in 1947-1948, dealt with subsidies in two Articles only (VI and XVI), while tariffs were the subject of detailed national item-by-item schedules of bound rates, either most-favoured-nation rates or preferential rates. In theory, it should have been possible to negotiate a maximum rate of subsidization for each product, which could then have been itemized and set out in schedules of obligation. But the GATT founders were primarily concerned with outlawing quotas and ensuring that tariff rates

<sup>83</sup> See GATT Secretariat, *Legal Instruments Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations Done at Marrakesh on 15 April 1994*, Vol. 27 (Sales No. GATT/1994-7), 1994.

<sup>84</sup> To give an example of how little attention was paid to subsidies before the GATT began to consider the special problems of export subsidies in the mid-1950s, a classic text: *Commercial Treaties and Agreements - Principles and Practices* (1951) written by Harry C. Hawkins, an experienced United States trade negotiator, refers only briefly to subsidies: those on shipping, and export "bounties" or grants, in the context of the United States countervailing duty law. Early bilateral trade agreements rarely refer to subsidy practices.

could not be raised arbitrarily. Consequently, they approved only a general, rather ambiguously worded obligation to consult with other signatories as to the "possibility of limiting the subsidization" if it was determined that subsidization was causing or threatening "serious prejudice to the interests of any other contracting party". These are the key provisions in the opening paragraph of GATT Article XVI.

One developing country (Cuba) noted in 1947 that subsidies were allowed in the GATT scheme but quotas were permitted only in narrowly defined situations. But as subsidies require government revenue to finance them they are less accessible to the developing countries, which would thus seem compelled to rely on quotas to protect local industry.<sup>85</sup>

## B. The structure of obligations before the Tokyo Round

When the Tokyo Round negotiations addressed the question of drafting more detailed rules on subsidies than those in Article XVI, and of establishing detailed rules regarding the use of countervailing duties (i.e. duties that offset subsidies paid on products exported) under Article VI, they had before them a structure of rights and obligations developed from the Havana Charter and the drafting of the GATT Articles, as well as from discussions associated with the Review of the GATT in 1955, some GATT jurisprudence, and some important interpretations of GATT Article VI rights by United States administrators of countervailing duty legislation. The main elements of this structure are as follows:

- A broad obligation to notify GATT about any significant subsidy practice, and to be willing to consult upon request (Article XVI:1).
- An obligation not to grant export subsidies on primary products that would result in "more than an equitable share of world export trade in that product" (Article XVI:3).
- As from 1958, an obligation on the part of those developed countries which accepted it not to grant export subsidies on non-primary (i.e. manufactured) products. In 1960, an Illustrative List of such prohibited export subsidies was prepared by a working party. (As revised, this became an important element of the Tokyo Round SCM Code.)
- Accepted GATT jurisprudence that a GATT tariff concession would be "nullified or impaired" (the language of the dispute settlement provisions of Article XXIII) by the granting of a subsidy to domestic producers in the country which had made the concession.<sup>86</sup> Moreover, it was clear that a negotiating signatory could attach conditions about subsidization to a tariff rate binding. In actual fact this version of "nullification and impairment" had little effect on subsidy practices, and the procedure noted above had little practical influence.
- Subsidies deemed to have been paid could be offset by an equivalent countervailing duty, if material injury was caused or threatened to domestic industry by such subsidized imports. The procedure for calculating the extent of subsidization and the existence of injury was a matter for national administrations (Article VI). This provision in GATT was made necessary by the existence of a countervailing duty law in the United States. While that law, introduced late in the previous century, had been concerned primarily with overt export subsidies, it was addressed to subsidies on goods exported to the United States, which might or might not be paid as export subsidies.<sup>87</sup> The United States countervailing duty law was not concerned with the legality of subsidy practices such as provisions of Article XVI prohibiting export subsidies; it dealt with all imported products that had benefited from some sort of subsidy. For example, in 1973, the

<sup>85</sup> See John H. Jackson, *World Trade and the Law of GATT: A Legal Analysis of the General Agreement on Tariffs and Trade* (Indianapolis: Bobbs-Merrill, 1969), p. 313 and footnote 19. Chapter 13 of this standard reference work provides the best short history of the evolution of the GATT subsidy provisions prior to the Tokyo Round.

<sup>86</sup> GATT, *Basic Instruments and Selected Documents (BISD)*, Third Supplement, p. 224; see discussion in Jackson, *op. cit.*, pp. 182-183.

<sup>87</sup> A distinction should be made between domestic or production subsidies, which may benefit a product that may also be exported, and a subsidy given to a product contingent on export.



United States had countervailed a number of Canadian domestic subsidy programmes that were deemed to constitute subsidies on exports in the celebrated "Michelin" case. It was argued that it was reasonable to do so because some 75 per cent of the production of the subsidized plant was exported to the United States.<sup>88</sup> But the view of the United States Treasury - which administered the law at the time - was that if as much as 10 per cent of the subsidized production was exported, the subsidies could be countervailed, because the countervailing duty provisions were not explicitly directed against export subsidies only.<sup>89</sup>

The position of the United States has been crucial in the evaluation of multilateral disciplines in this area, particularly because of the United States' critical attitude to subsidies, and its role as the main user of countervailing duties, which it has applied without a "material injury" test, contrary to GATT Article VI but permitted under the legal cover of the Protocol of Provisional Application (the "grandfather clause").

The negotiations on subsidies and countervailing duties, considered by many to be the key element in the Tokyo Round negotiations as a whole, sought to update and codify these obligations and rights. The United States offered to conform to GATT Article VI by incorporating an injury test in its countervailing duty law (which was sheltered by the "grandfather clause"), in return for more stringent multilateral disciplines on subsidies, which many observers believed were becoming more economically important and an increasingly vital trade policy issue.

The Tokyo Round Agreement on Interpretation and Application of Articles VI, XVI and XXIII of GATT provided, as does Article VI of the General Agreement, a sure remedy for injurious subsidization of imports; against import replacement subsidization, however, it provided a far less certain procedure of consultation, complaint, conciliation and countermeasures, building on (but only in a limited way) the provisions of Articles XVI and XXIII. The uncertainty was largely due to lack of precision in the criteria for determining serious prejudice. A major shortcoming of the Tokyo

Round Agreement was this asymmetry between the rights of signatories to deal under their domestic law with injurious subsidies on imports and their more limited and largely ineffective right to seek redress through the use of the international machinery available to protect themselves against injurious import replacement subsidies.

The asymmetry of possible remedies was paralleled by the asymmetry of obligations on subsidies. The industrialized countries signatories to the Agreement had reaffirmed their commitment not to grant export subsidies on non-primary products; as for other forms of subsidy, they agreed merely that they would "seek to avoid causing" injury to the domestic industry of another signatory, nullification or impairment of benefits, or serious prejudice. Proposals were advanced for more detailed and binding obligations regarding domestic subsidies, but were rejected as being too ambitious. It was these proposals that were reverted to in the Uruguay Round.

It was one of the stated objectives of the United States, Australia and Canada in the Tokyo Round that there should be more stringent rules to limit export subsidies on agricultural products. There was extensive GATT jurisprudence involving the interpretation of Article XVI:3. Paragraph 3 states that if a contracting party "grants directly or indirectly any form of subsidy which operates to increase the export of any primary product from its territory, such subsidy shall not be applied in a manner which results in that contracting party having more than an equitable share of world trade in that product". This would appear to allow export subsidization to capture a given market and to displace an established supplier if the subsidizing exporter does not thereby increase its share of world trade (having lost a share in a market elsewhere). To try to improve on this state of affairs was one of the most difficult issues in the Tokyo Round. In the Agreement there was an attempt to define the notion of "equitable share" as follows: "... 'more than an equitable share of world export trade' shall include any case in which the effect of an export subsidy granted by a signatory is to displace the exports of another signatory, bearing in mind the developments on world markets ...". The Agreement also added a new concept: "Signatories further agree not to grant

<sup>88</sup> Gary C. Hufbauer: "Subsidy issues after the Tokyo Round" in W.R. Cline (ed.), *Trade Policy in the 1980s* (Washington, D.C.: Institute of Economic Relations, 1983), p. 352.

<sup>89</sup> The United States view of subsidy practices and the rules of Article XVI prior to the Tokyo Round, were summed up by Jackson, *op. cit.*, p. 377, as follows: "The net effect of these Article XVI obligations is to impose no constraint on subsidies that operate as a protectionist device, except to report and consult; to impose a slight constraint (not to use subsidies to get more than an equitable share of the market) on primary product-export subsidies; and, for a small group of developed countries only, to impose a constraint against use of export subsidies on non-primary goods".

export subsidies on exports of certain primary products to a particular market in a manner which results in prices materially below those of other suppliers to the same market", which served to weaken, rather than strengthen, the provisions of Article XVI, as these were governed by the phrase "bearing in mind the developments on world markets". In practice, these words became non-operational as they were interpreted by the European Community as not limiting significantly the ability to dispose of agricultural surpluses. Cases that have arisen since the end of the Tokyo Round have made it clear that this was indeed the case.

The Tokyo Round Code dealt with subsidies in largely normative language (except for the revision of the Illustrative List of prohibited export subsidies), and left still unsolved a number of features of countervail that were unsatisfactory to exporters to the United States. The Tokyo Round Code did not correct the basic asymmetry in the overall system in that countervail was an effective, or, at least, a damaging, measure applied under domestic law to restrain the competition of subsidized imports. There were no comparable remedies under domestic law to deal with either subsidies to domestic competitors or with competition for export markets by subsidization.

The asymmetry penalizes smaller countries. A world-scale plant established with a certain quantum of subsidization in a smaller country may, typically, export from 45 per cent to 85 per cent of its production. Also quite typically, the bulk of such exports may go to only one of the larger trading entities, and new world-scale plants must export a much higher proportion of their total production if they are to operate efficiently and not rely unduly on the domestic market. As subsidized exports from smaller countries are liable to countervailing action in the larger trading countries, such action, because it bears on a particularly high proportion of the total output of the plant in question, can be very damaging. By contrast, a similar plant financed by similar subsidies within a larger trading country will export only a small portion of its total production, and its profitability will not be seriously affected by countervailing duties applied against its exports to some small country. It could be argued that the logic and effect of the use of countervailing duties by countries would be to encourage investors to locate their production in the country that is taking the countervailing duty action and benefit from available subsidies.

A variety of questions remained unresolved to be addressed in the Uruguay Round. These included a group of issues that related to the very language of the GATT provisions: the

meaning of "injury", the meaning of "material" (in the sense of "material injury"), the significance of "cause" (in the sense of injury being "caused" by subsidization), given that causality is a complex legal concept. Other questions addressed were whether subsidies for basic infrastructure were available to a wide range of firms and activities, defined by broad criteria, such as an investment tax credit (United States practice, as it developed, was against countervailing such "generally available" subsidies, and singled out subsidies paid only to "specific" firms) and whether subsidization for R&D should be countervailable (given that Article VI provides for countervail only in regard to subsidies on "manufacture, production or export").

In the case of subsidies for regional economic development, the Tokyo Round led to a negative development. The United States Treasury had followed the practice of deducting certain sums from the gross amount of a subsidy to arrive at the "net amount of subsidy". The United States 1979 Trade Agreements Act, implementing the Tokyo Round, introduced the concept of "net subsidy" and provided for specific deductions, namely, any application fee or deposit to qualify for the subsidy; any loss due to deferral of payment; and any export tax imposed to limit the amount of the domestic subsidy on exported goods. This list was to be "all inclusive", and specifically disallowed the previous Treasury practice of deducting from a regional economic development subsidy the increased costs incurred by a firm in locating in a less-than-prime location.

Other serious issues were raised by the increasing ingenuity of domestic producers in seeking relief from import competition under the countervail provisions. One was the problem of so-called "upstream" subsidies: to what extent was a subsidy on an input to be considered as a subsidy on the product which incorporated such an input? This is important for many developing countries which may subsidize, in one way or another, a natural resource-based product that may be an input to a processing industry. And what about natural resources? In many countries access to natural resources - timber, minerals, oil and gas - is controlled by the State or may be the property of the State or of sub-national units. If access to exploiters of resources is awarded for less than the price that would be fetched in an open market, arm's length (auction) transaction, is there a subsidy on the goods produced from those resources? Another question, addressed in detail by United States case law, is the extent to which additional equity participation by the State in state-owned

(or partially owned) enterprises may constitute a subsidy.

Disputes involving subsidies and countervailing measures have been a frequent feature in the GATT dispute settlement mechanism, especially after the Tokyo Round when the Subsidies Code entered into force. In

1948-1992, 13 out of more than 100 GATT panel reports were devoted to subsidies and countervailing measures; 10 of such cases occurred in 1981-1992. As of 10 June 1994, 15 out of 50 existing GATT dispute settlement cases at different stages were related to subsidies and countervailing measures.<sup>90</sup>

### C. Main elements of the Uruguay Round Agreement on Subsidies and Countervailing Measures

In reviewing the main elements of interest in the new Uruguay Round Subsidies Agreement, two general observations should be made. The first is that, as in the case of the Tokyo Round Code, the full implications of the provisions will become evident only with the development of practice and jurisprudence, both under national implementing legislation and under international procedures, including discussion in the WTO administering committee (Article 24 of the Agreement). The second is that the Agreement must be kept in perspective. The fact that for the first time there is a definition of "subsidy" and that subsidies are classified into prohibited, non-actionable and, presumably, actionable would appear to reflect an international consensus on the appropriate role for governments in supporting production and exports. However, the strength of this consensus will be tested in the application of countervailing duties or the particular "remedies" invoked against "actionable" subsidies (Article 7). The "non-actionability" of regional aid (as defined and notified) and aid for research and development are limited (Article 9) and subject to review within a period of four and a half years (Article 31), but are already being viewed in the United States as major concessions.

The obligations of the Agreement are built around the following definitions and concepts:

*Subsidy:* In Article 1 a subsidy is defined as involving "a financial contribution by a government or any public body" and "a benefit is thereby conferred". The "financial contribution" may involve a direct transfer of funds, potential direct transfers of funds or liabilities (e.g. loan guarantees), revenue foregone (tax credit), the purchase of goods by a government or its provision of goods and services other than general infrastructure.

*Specificity:* Specificity is a key concept in the Agreement in that the remedies provided against "prohibited" subsidies in Part II, "actionable" subsidies under Part III, or countervailing duties, can be applied only if a subsidy is "specific" to an enterprise or industry or a group of enterprises or industries. The main criterion (Article 2) is that the "granting authority" or the relevant legislation explicitly limits access to a subsidy to certain enterprises when subsidies are granted on the basis of "objective criteria or conditions" "clearly spelled out in law, regulation or other official document". However, this "non-specificity" can be challenged if certain factors are observed in practice, such as "the granting of disproportionately large amounts of subsidy to certain enterprises". Specificity also exists when a subsidy is limited to "certain enterprises located within a designated geographical region". However, this is qualified by the sentence stating that "the setting or change of generally applicable tax rates by all levels of government entitled to do so shall not be deemed to be a specific subsidy for the purposes of this Agreement". This so-called "Canada clause" was intended to deal with countries with a federal system of government, but the limits of this provision may be tested by measures adopted by lower levels of government. As discussed below, assistance to disadvantaged regions (which are non-specific in the context of the region), subject to certain criteria, is "non-actionable".

In the Tokyo Round Code the language is imprecise (Article 11:3) regarding the possibility of granting subsidies "with the aim of giving an advantage to certain enterprises". Subsequently, in United States countervail practice, a sharp distinction was made between subsidies that were "specific" to particular firms and those that were considered to be "generally

<sup>90</sup> GATT document C/188, 10 June 1994.

available". The latter were held not to be countervailable, but it might be argued that the United States countervail provisions did not make such a clear distinction, and that the provisions of Article 2 of the Subsidies Agreement, which defines the nature of a "specific" subsidy, combined with Article 8, paragraph 8.1(a), which provides that non-specific subsidies are "non-actionable", represents a major advance and concession by the United States as regards its countervail practice. A more definitive assessment would require a review of a significant number of United States countervail decisions on what constitutes a countervailable subsidy in the light of the guidance given in Article 2.

*Prohibited subsidy:* Article 3 prohibits members from granting or maintaining subsidies that are contingent, in law or in fact, upon export performance (11 examples are provided in the illustrative list in Annex I to the Agreement). It also prohibits subsidies that are contingent upon the use of domestic over imported goods. The only exception to this would be the practices covered by the Agreement on Agriculture in which case the provisions of that Agreement (in which disciplines are generally stated in terms of negotiated quantitative limits rather than prohibitions) would apply. The rigorous standard required would be met when facts demonstrate that the granting of such a subsidy that has not been made legally contingent on export performance is in fact tied to actual or anticipated exportation or export earnings. The mere fact of a subsidy's being granted to enterprises engaged in exporting would not be sufficient grounds for a practice to be regarded in this light.

The Agreement contains specific, comprehensive and strict remedies to deal with subsidies that are prohibited. Apart from provisions for consultation among members, the matter could be referred to the dispute settlement body (DSB) if no mutually agreed solution is found within 30 days. Another new feature of the Agreement is the establishment of a Permanent Group of Experts (PGE), to consist of five independent persons highly qualified in the fields of subsidies and trade relations. Panels may request the assistance of the PGE if in doubt as to whether a particular measure is a prohibited subsidy.

*Actionable subsidies:* This category of subsidies, which is dealt with in Part III, can be granted or maintained provided they do not have adverse effects on the interests of other

members. Adverse effects are defined in terms of injury to the domestic industry of another member, nullification or impairment of benefits accruing directly or indirectly to other members under GATT 1994 and serious prejudice to the interests of the other member concerned. Article 6 provides detailed guidance on determination of serious prejudice. Serious prejudice would be deemed to exist in the following cases: (a) the total ad valorem subsidization of a product exceeds 5 per cent<sup>91</sup> (in anticipation of the negotiation of specific multilateral rules for an Agreement on Civil Aircraft, this threshold is not applicable to civil aircraft); (b) subsidies to cover operating losses sustained by an industry; and (c) subsidies to cover operating losses sustained by an enterprise, with the exception of one time, non-recurrent measures to provide time for development of long-term solutions and to avoid acute social problems. Serious prejudice may also be deemed to exist (d) by forgiveness of government-held debt and grants to cover debt repayment. Both Articles 5 and 6 dealing with Adverse Effects and Serious Prejudice respectively do not apply to subsidies maintained on agricultural products, as established in Article 13 of the Agreement on Agriculture.

In order to ensure that determination of serious prejudice does not lend itself to subjective judgements, detailed guidance is provided on arriving at such a determination. Remedies are provided in Article 7 for consultation among members, establishment of panels and other procedures in the event of injury to domestic industry, nullification or impairment or serious prejudice.

*Non-actionable subsidies:* Article 8 provides that subsidies which are not specific (as defined in Article 2); specific subsidies for industrial research and pre-competitive development activities (subject to precise conditions and tests set out in this Article); assistance to "disadvantaged regions" (as defined in the same Article) and assistance for adaptation to "new environmental requirements" (again, as defined and as limited by Article 8) are to be non-actionable, that is, not subject to countervailing duties or other remedial action. All these subsidy programmes "shall be notified in advance of ... implementation to the Committee ..." (Article 8, paragraph 8.3). This is a mandatory provision: in the absence of notification a programme otherwise falling within these categories will be countervailable under United States law. Moreover, under Article 9, if such

<sup>91</sup> Annex IV provides guidance for calculating the level of subsidies in terms of the provisions of Article 6, paragraph 6.1. The calculation shall be made in terms of the cost to the granting government.

a "non-actionable"<sup>92</sup> programme is found (by the Committee) to result in "serious adverse effects to the domestic industry ... such as to cause damage which would be difficult to repair ...", and the Committee's recommendation for modification of the programme at issue "is not followed within 6 months", the complaining signatory will be authorized to "take appropriate countermeasures" (which could be, if imports are at issue, a countervailing duty). Only experience will show whether this is a serious limitation on the concept of "non-actionability" set out in Article 8. The detailed provisions regarding industrial research and pre-competitive development subsidies, regional aid, or aid for compliance with environmental laws, appear to offer scope for adequate subsidy programmes in these categories. However, the notification and consultation requirements in paragraphs 3, 4 and 5 of Article 8 embody the longstanding objective of one member that subsidy programmes should be notified and approved before implementation. It remains to be seen, of course, whether, as a practical matter, signatories of the Agreement will try to seek authority (under Articles 5, 6 and 7 of the Code) for countermeasures against otherwise "non-actionable" subsidies (i.e. subsidies that have not been notified and approved) which do not bear on imports (i.e. that are within the scope of countervail). Subsidies that may bear on exports to a third country are likely to attract more concern than will import replacement subsidies.

It is important to note that, under Article 3, the provisions on "non-actionable" subsidies are to run for five years only, and are to be reviewed six months before the end of that period. Pressures to eliminate this relief are already in evidence.

The provisions of Article 28 "Existing Programmes" are important: those that are inconsistent with the new Agreement must be notified within 90 days of the entry into force of the WTO Agreement for that member country, the scope of such programmes must not be extended, nor may the programmes be renewed upon expiration, and they must be brought into conformity with the Agreement within three years. Until such programmes have been brought into conformity with the Agreement (including notification and approval) they will presumably remain countervailable under

United States law. There will thus be an incentive to bring regional aid, research and environmental subsidies into conformity with the criteria and conditions of Article 8, including, of course, notification and approval, for all programmes bearing on exports to the United States.

*Subsidies for "assistance to disadvantaged regions"*: It was noted above that the concept of calculating whether or not regional aid amounted to a "net" subsidy under United States countervailing duty law, by deducting from the gross amount of the subsidy the additional costs incurred by the firm concerned, had been expressly prohibited by the Senate in its consideration of the 1979 Trade Act (implementing the Tokyo Round Code). In the new Agreement there is a different approach: a non-actionable subsidy is defined by positive criteria, such as per capita income, level of employment, and so on. The earlier concept of "netting out" the additional costs to the firms involved was theoretically reasonable, but detailed and difficult to apply. The new provisions, although carefully and precisely drafted, and "hedged" by Article 9 and by the five-year period, have apparently proved controversial in the United States.

*Track II*: The term "track II" was jargon often used in the Tokyo Round to refer to the procedures and remedies for injurious subsidies other than those subject to the discipline of countervail. Broadly speaking, experience since then has demonstrated that these procedures and associated remedies have provided no real discipline compared to countervail; this situation has been described above as an "asymmetry". The new Agreement gives more precision to the "track II" provision (Articles 5, 6 and 7), which, taken in conjunction with the revised, reinforced dispute settlement provisions (of the WTO) and the surveillance provisions of the Agreement (Articles 24, 25 and 26), may perhaps provide the basis of a somewhat more effective system. This "asymmetry" as between countervailable subsidies and other subsidies might then be reduced. Only experience will show how far this is true.

*Precision regarding subsidies causing serious prejudice*: Article 6 defines "serious prejudice to the interests of another Member" by a series of fairly precise provisions: prejudice

<sup>92</sup> In the draft list of proposed changes to United States law (as distributed to the House of Representatives Committee on Ways and Means, 2 March 1994), this is noted. *Inside US Trade*, Washington D.C., 11 March 1994, p. 6. Proposed amendment to Section 1671a of the US CVD law, Footnote 35 to Article 10 of the Agreement provides that "... in the case of a subsidy referred to in paragraph 2 of Article 8, conferred pursuant to a programme which has not been notified in accordance with paragraph 3 of Article 8, the provisions of Part III or V may be invoked, but such subsidy shall be treated as non-actionable if it is found to conform to the standards set forth in paragraph 2 of Article 8".

is "deemed to exist" if subsidization of a product exceeds 5 per cent ad valorem (paragraph 6.1(a)); if the subsidies are to cover operating losses "sustained by an industry" (6.1(b)); and if subsidies are to cover operating losses of a single firm unless they are "non-recurrent". These will remain countervailable. On the other hand, in regard to "track II", the doctrine that there must be some "trade effect" for a measure to be actionable under GATT is reflected in Article 6, paragraph 6.3, which sets out the effects that must be demonstrated for "serious prejudice" to be found to exist. Seemingly precise language is also used to elaborate the notion of an "increase in the world market share" as one of the effects constituting "serious prejudice". This language is not only new but goes further than the guidance in the domestic legislation of the United States.

*Remedies:* Countervail will remain as an effective offsetting measure for import subsidies that cause material injury to domestic industries. As for the rest, the procedures (Article 7) provide for almost immediate recourse to the Dispute Settlement Body

(DSB), which, in the case relating to prohibited subsidies, may be assisted by the Permanent Group of Experts. At the end of the day, the complaining party may be authorized to take "countermeasures, commensurate with the degree and nature of the adverse effects".<sup>93</sup>

*"Transformation into a market economy":* Article 29 endorses a fairly broad exception for countries in transition from a centrally planned economy to a market economy: they may "apply programmes and measures necessary for such a transformation". The meaning of this is not entirely clear, however, particularly in view of the precise provisions that follow (Article 29, paragraph 29.2). Such countries are not immediately subject to the prohibition on subsidies under Article 3; their obligation is to phase out (or "bring into conformity") subsidy programmes within seven years; Article 4 (Remedies) will not apply; but countervail will be applicable as will the remedies against Adverse Effects and Serious Prejudice in relation to actionable subsidies under Article 7, except for subsidies in the form of direct forgiveness of debt.

## D. Differential and more favourable treatment of developing countries

Part VIII, Article 27, of the Agreement deals with developing country members and outlines the provisions for special and differential treatment in favour of developing country members. The preambular provision in Article 27, paragraph 27.1, is similar to Article 14.1 of the Tokyo Code, in embodying the recognition by members that subsidies may play an important role in economic development programmes of developing country members. An analysis of the two Articles, if carried out merely by comparing their provisions, could lead to the conclusion that the Tokyo Round Code provided greater flexibility for developing countries as regards the maintenance of subsidies for economic development programmes. Article 14:5 of the Tokyo Round Code constituted a "best endeavour" formulation, i.e. that a developing country signatory should "endeavour to enter into a commitment to reduce or eliminate export subsidies when the use of such export subsidies is inconsistent with its competitive

and development needs". In practice, the flexibility provided by this provision was rendered ineffective, in part, through the provisions of Article 19:9 of the Tokyo Round Code relating to non-application of the Agreement, which, in practice, means non-application of the material injury test by the United States in applying countervailing duties. In the years after the conclusion of the Tokyo Round Code, the United States sought and obtained bilateral commitments for the phase-out and elimination of particular subsidy practices which the developing country members, the new signatories to the Code, claimed to have been instituted in pursuance of economic development programmes.<sup>94</sup> In accordance with a commitment under Article 14:5 that is being undertaken and applied multilaterally in the Tokyo Round Committee on Subsidies and Countervailing Measures, developing country signatories of the Code benefited from the provisions of Articles 14:6 and 14:8 to the effect that countermeas-

<sup>93</sup> See chap. IX.

<sup>94</sup> The following developing country signatories to the Code were known to have signed bilateral commitments (some of which were notified to the Tokyo Round Subsidies Committee) in order to achieve the benefit of the injury test in the United States or to be recognized as a party to the Code: Brazil, Chile, Colombia, India, Indonesia, Israel, Mexico, Pakistan, Philippines, Republic of Korea and Uruguay.

ures in pursuance of Parts II and VI of the Code would not be instituted against such countries.

The situation indicated above illustrates that the flexibility available to developing country signatories of the Tokyo Round Code was, in practice, rather limited in scope owing to the bilateral commitments extracted under threat of non-application by one Code signatory. Under the Uruguay Round Agreement, the flexibility is delineated in more specific terms and all members are required to apply the provisions on countervailing duties, including the injury criterion. The special and differential treatment in favour of developing countries is predicated on specific and legally-enforceable provisions for a special dispensation in their favour, including precise and objective "graduation" criteria. The more significant highlights of these are outlined below:

- The two categories of developing country members of the Agreement (referred to in Annex VII): (a) least developed countries designated as such by the United Nations, which are members of the WTO, and (b) a list of other countries, so long as their GNP per capita remains less than \$1,000 per annum (i.e. Bolivia, Cameroon, Congo, Côte d'Ivoire, Dominican Republic, Egypt, Ghana, Guatemala, Guyana, India, Indonesia, Kenya, Morocco, Nicaragua, Nigeria, Pakistan, Philippines, Senegal, Sri Lanka and Zimbabwe), are exempt from the blanket prohibition in Article 3, paragraph 3.1(a), which deals with subsidies contingent, in law or in fact, upon export performance, including those in the illustrative list in Annex I to the Agreement. Other developing countries, i.e. those not listed in Annex VII, will be exempt from this prohibition for a period of eight years provided the subsidies are progressively phased out during this period.<sup>95</sup> In addition, the other prohibition contained in Article 3, paragraph 3.1(b), regarding subsidies contingent upon the use of domestic over imported goods will not be applicable to developing countries for five years and for the least developed countries for a period of eight years from the entry into force of the WTO Agreement.

- Developing country members will also be required to phase out export subsidies for products in which they have reached a state of export competitiveness, defined as a share of at least 3.25 per cent in world trade of that product for two consecutive calendar years.<sup>96</sup> Least developed countries and other developing countries listed in Annex VII are allowed flexibility to phase out such subsidies over a period of eight years while other developing countries have to do so in two years. During the periods in which they are permitted to apply otherwise prohibited subsidies, the remedies provided for prohibited subsidies in Article 4 will not apply; instead the remedies in respect of serious prejudice in Article 7 will be applicable. With respect to "actionable" subsidies, there will be no presumption of serious prejudice in respect of subsidies granted by developing country members so the existence of serious prejudice would have to be determined. Similarly, such countries are entitled to additional flexibility to phase out actionable subsidies.<sup>97</sup>

A major innovation providing for special and differential treatment in the Agreement is that any countervailing investigation of a product originating in a developing country member will be terminated if it is determined that the overall level of subsidies granted upon the product in question does not exceed 2 per cent of its value calculated on a per unit basis, or the volume of the subsidized imports represents less than 4 per cent of the total imports of the like product in the importing country, unless imports from developing country members whose individual shares of total imports represent less than 4 per cent collectively account for more than 9 per cent of total imports of the like products in the importing Member. For developing countries which have phased out their export subsidies within eight years and developing countries covered by Annex VII, the figure will be 3 per cent. It remains to be seen if these thresholds will be meaningful and provide developing countries with real relief in facing countervail. On the other hand, the Agreement codifies the practice of cumulative assessment of injury, which had been opposed by develop-

<sup>95</sup> There are also provisions for a Committee review of subsidies contingent in law or in fact upon export performance to determine the necessity of maintaining these subsidies over and above this period.

<sup>96</sup> A product is defined in Article 27, paragraph 27.6, as a section heading of the Harmonized System Nomenclature.

<sup>97</sup> Article 27, paragraph 27.9, stipulates that: "Regarding actionable subsidies granted or maintained by a developing country Member other than those referred to in paragraph 1 of Article 6, action may not be authorized or taken under Article 7 unless nullification or impairment of tariff concessions or other obligations under GATT 1994 is found to exist as a result of such a subsidy, in such a way as to displace or impede imports of a like product of another Member into the market of the subsidizing developing country Member or unless injury to a domestic industry in the market of an importing Member occurs".

ing countries. To be "cumulated", imports must be less than *de minimis*.

An interesting feature relating to developing countries is that countervailing duties in respect of actionable subsidies, provided for in Part III, will not apply to direct forgiveness of debt or to subsidies to cover social costs when these are granted within and directly to a privatization programme of a developing country member, provided that both the programme

and the subsidies involved are granted for a notified duration and that the programme results in eventual privatization of the enterprise concerned. This appears likely to encourage subsidization if it is linked to foreign direct investment in the context of privatization. The stipulation that this would be for a limited period and would be notified to the Committee may act as a check against misuse of this provision.

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## E. Annexes

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The Annexes give precision to the obligations and guidance with respect to the identification or calculation of the essential concepts. The Illustrative List of Export Subsidies in Annex I contains new features which go beyond the comparable list in the Tokyo Round Code. Items (h) and (i) incorporate a reference to inputs that "are consumed in the production of the exported product" instead of "physically incorporated in the exported product". Annex IV, for example, sets out rules on how to calculate the per unit ad valorem rate of subsidization; Annex II "Guidelines on Consumption of Inputs in the Production Process" deals with subsidization by excessive rebates of indirect taxes on inputs into exported products. Annex III addresses the issue of how to determine whether a "substitution drawback system" is an export subsidy. These technical

annexes deal with matters that have been exhaustively discussed between the Tokyo Round and the Uruguay Round and that fill the gaps in the system that were evident when the Tokyo Round negotiations had concluded. One "miscellaneous" provision should be noted in Article 21. In the new provisions on countervail it is provided that a definitive duty "shall be terminated" in five years (unless the authorities determine that there may be a continuation or recurrence of subsidization and injury). This was a modest concession by countervailing countries; however, for existing countervailing measures it should be noted that the five-year provision runs from the date the WTO enters into force. In overall terms, however, the Agreement applies to a larger number of countries and the disciplines are much stronger than in the Tokyo Round Code.

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## F. Agriculture

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Multilateral, bilateral and national problems generated by the use of trade-distorting subsidies have been most intractable in the agricultural sector. Subsidies on agricultural production were seen as necessary to respond to domestic socio-political considerations, and to address the vulnerability of agriculture to climatic conditions and other natural events. However, enormous subsidies led to massive surpluses, which in turn prompted the use of export subsidies, and set off open-ended export subsidy competition. This operated to the detriment of competitors in developing countries

in particular, which lacked the huge budgets of the subsidizing agencies in the major developed countries. Mounting budgetary expenditures have now forced national authorities to review their support policies. While some developing countries importers of essential foodstuffs were able to obtain them at low prices, subsidized food imports often undermined the interests of traditional agricultural producers, with serious economic and social consequences in many developing countries.<sup>98</sup> Operationally ineffective rules and disciplines on agricultural subsidies developed in previous multilateral negotiations

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<sup>98</sup> Under the Ministerial Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least Developed and on Net Food-Importing Developing Countries, it was agreed that appropriate mechanisms be established to ensure that the results of the Uruguay Round on agriculture do not adversely affect the availability of food aid at sufficient levels to meet food needs of developing countries.



exacerbated the asymmetry between the stringency of rules on agricultural and on industrial products. To reverse the privileged treatment of agriculture in the multilateral trading system, the Punta del Este Declaration stated that the aims of the negotiations included that of "improving the competitive environment by increasing discipline on the use of all direct and indirect subsidies and other measures affecting directly or indirectly agricultural trade, including the phased reduction of their negative effects and dealing with their causes".<sup>99</sup> At the Mid-term Review Meeting at Montreal in 1988, it was agreed that "the long-term objective of the agricultural negotiations is to establish a fair and market-oriented agricultural trading system"<sup>100</sup> and that this objective "is to provide for substantial progressive reductions in agricultural support and protection sustained over an agreed period of time, resulting in correcting and preventing restrictions and distortions in world agricultural markets".<sup>101</sup> Thus, the Uruguay Round negotiations have begun a process, through the Agreement on Agriculture, of prompting and supporting national adjustments of domestic policies in the agricultural sector, some of which had already been effected autonomously.

As noted elsewhere in this chapter, the Agreement on Subsidies and Countervailing Measures is interspersed with references to the Agreement on Agriculture, to exclude agricultural subsidies from the ambit of its disciplines. First, the prohibition of certain subsidies, including export subsidies, under Article 3 of the Subsidies Agreement does not apply to agricultural products. Second, the exhortation in Article 5 that no WTO member should cause adverse effects to the interests of other members does not apply to subsidies maintained on agricultural products. Third, Article 6, which appears to make the application of the notion of "serious prejudice" more operationally workable, does not apply to subsidies maintained on agricultural products. Fourth, the remedies provided for in Article 7 are similarly not applicable with respect to agricultural products. Fifth, Article 10 (Application of Article VI of GATT 1994) states that countervailing duties may only be imposed pursuant to investigations initiated and conducted in accordance

with the provisions of the Subsidies Agreement and the Agreement on Agriculture.

The foregoing are restated in the Agreement on Agriculture. Hence, the approach to regulating the use of agricultural subsidies is fundamentally different from that adopted in the Agreement on Subsidies and Countervailing Measures. Rather than compartmentalize the use of subsidies - prohibited, actionable and non-actionable - and prescribe avenues for remedial measures, the Agreement on Agriculture basically adopted a commitments-oriented approach in the three areas of market access, domestic support and export competition, underpinned by rules essentially aimed at protecting the integrity of those commitments. The results-oriented approach of the reform programme launched by the Agreement on Agriculture was probably the only viable way to begin regulating the delicate connection between domestic agricultural policies and more open trade policies. The reform programme may rightfully be criticized as being less bold than was contemplated in the draft Final Act of December 1991, but it is nevertheless a good beginning to the process of whittling away the heritage left by the founders of the General Agreement in constructing Article XVI thereof, and to weaken the resistance to accepting more meaningful changes pursued in the multilateral trade negotiations.

Domestic support reduction commitments, expressed and implemented in terms of "Total Aggregate Measurement of Support" (AMS) and "Annual and Final Bound Commitment Levels", were embodied as legally binding in schedules of participants. According to the modalities<sup>102</sup> for establishing such commitments, the total AMS<sup>103</sup> obtaining during the base period 1986-1988 was to be reduced by 20 per cent (13.3 per cent for developing countries; least developed countries were not required to make reduction commitments) over a period of six years (10 years for developing countries). As may be noted, the commitments are not product specific. For example, the Schedule of the United States includes a commitment to reduce its total AMS from \$23 billion to \$19 billion; that of Japan from yen 4,800 billion to yen 3,900 billion; and that of

<sup>99</sup> *Uruguay Round: Papers on Selected Issues* (UNCTAD/ITP/10), 1989, Annex I, p. 374.

<sup>100</sup> GATT document MTN.TNC/11, 21 April 1989, p. 9.

<sup>101</sup> *Ibid.*

<sup>102</sup> See "Modalities for the establishment of specific binding commitments under the reform programme", GATT document MTN.GNG/MA/W/24, 20 December 1993.

<sup>103</sup> Calculated as the sum of the value of all Aggregate Measurements of Support and Equivalent Measurements of Support.

the EC from ECU 73 billion to ECU 61 billion.<sup>104</sup>

Not all domestic support measures in favour of agricultural producers were required to be included in the calculation and reduction of domestic support. Those included in the "Green Box" of subsidies deemed to have "no, or at most minimal, trade-distorting effects" (Annex 2) were exempted from reduction commitments.

Direct payments under production limiting programmes (Article 6.5), which appear to cover the United States "deficiency payments" and the new compensation payments under the reformed EC Common Agricultural Policy, were also excluded, in addition to *de minimis* product-specific and non-product specific domestic support, defined as not exceeding 5 per cent of the value of total production of a basic agricultural product and of total agricultural production respectively. For developing countries, the *de minimis* threshold is 10 per cent.

Additional exemptions for developing countries from reduction commitments cover investment subsidies generally available to their agriculture, agricultural input subsidies generally available to low-income or resource-poor producers, and domestic support to producers to encourage diversification out of illicit narcotic crops. As the expression "generally available" is not defined in the Agreement on Agriculture, the provisions of Article 2 (Specificity) of the Subsidies Agreement may be applicable to determine what are generally available investment subsidies and input subsidies. Special and differential treatment for developing countries was also recognized with respect to the criteria for the application of certain "Green Box" measures - public stockholding for food security purposes and domestic food aid (paragraphs 3 and 4 of Annex 2 of the Agreement on Agriculture).

Some of those exemptions were the result of the intensive negotiations between the EC and the United States after the presentation of the draft Final Act, and in fact during the final weeks of the Round (December 1993). These bilateral negotiations resulted in the exemption of two important subsidy programmes, as noted above. Another outcome was that the AMS commitments became global rather than product specific, thus safeguarding the flexibility of WTO members to design their internal agricultural support policies as they deem appropriate. For example, they are not constrained from switching support from one

agricultural product to another, or from varying cuts in support among different products, as long as the global commitments reflected in their individual schedules are respected.

Commitments limiting domestic supports represent new obligations. The Uruguay Round was the first occasion when such commitments were made and incorporated in GATT schedules in such a systematic and transparent manner. Under GATT 1947, the obligations on subsidies in general (which operate to increase exports or to reduce imports) are to notify them (Article XVI:1, first sentence) and to discuss the possibility of limiting them where they cause or threaten serious prejudice to the interests of other contracting parties (Article XVI:1, second sentence). Compliance with the former obligation has been somewhat unsatisfactory, while the latter has been operationally unenforceable, especially in the case of agricultural products.

The reform programme to control domestic supports under the Agreement on Agriculture is definitely an improvement over current rules and disciplines. By securing the commitments to limit domestic supports through their incorporation in the schedules, their enforcement by way of the improved dispute-settlement system should not prove controversial. Transparency of domestic supports would not be encumbered by the expression "which operate to increase exports or to reduce imports". Claims for "Green Box" domestic supports and other exempted measures provided for in Article 6 of the Agreement are notifiable (Article 18:3) and must be substantiated (Article 7:2(a)). The general disciplines on domestic support (Article 7) enhance predictability in the sense that possible directions of domestic support policies in the future are more certain, e.g. the "Green Box" supports, and the other exempted domestic support policies mentioned in Article 6. Perhaps quite significant is the discipline that a WTO member shall not provide support to agricultural producers in excess of *de minimis* thresholds where no total Aggregate Measurement of Support (AMS) commitment was registered in its Schedule (Article 7:2(b)).

As noted above, the reform programme suffers from certain weaknesses. First, "direct payments under production limiting programmes" were exempted from reduction commitments. Thus, there is no impediment (except perhaps the availability of resources) to WTO members emulating such programmes already in place in other members. Second, AMS commitments are global rather than product

<sup>104</sup> The EC has also made specific commitments with respect to subsidized production of oilseeds.

specific, whose implications were noted above. None the less, comfort can be taken in the fact that in the post-Uruguay Round era maximum limits for "intolerable" domestic supports have been established, and that the next episode of multilateral negotiations could further reduce them. To the extent that there were no credible multilateral controls on domestic supports in the pre-Uruguay Round period, the new discipline, however modest, is a step in the direction of dismantling entrenched trade-distorting policies in the agricultural sector, while accommodating the conflicting concerns and interests of WTO members.

In contrast with the prohibition of the use of export subsidies in the Subsidies Agreement, the results-oriented approach through binding commitments was also employed for agricultural export subsidies. Unlike the approach taken with respect to domestic support (where the exempted measures were defined), the Agreement on Agriculture indicates which types of export subsidies are subject to reduction commitments (Article 9). Hence, those measures which do not fall under Article 9 were exempted from such commitments. Reduction commitments apply to budgetary outlays (36 per cent by developed countries, and 24 per cent by developing countries; least developed countries were not required to make reduction commitments), and to quantities benefiting from such subsidies (21 per cent by developed countries and 14 per cent by developing countries) during the base period of 1986-1990 (or alternative base years of 1991-1992 with respect to volumes of subsidized exports as provided for in Annex 8 of the note by the Chairman of the Negotiating Group on Market Access of December 1993, which refers to modalities for reduction commitments).<sup>105</sup> These commitments are also laid out in detail in the schedules which specify the amounts and quantities for each subsidized sector for each of the six years covered by the implementation period (10 years for developing countries). A significant feature of the Agreement is the obligation that a WTO member shall not provide export subsidies (identified in Article 9) in respect of any agricultural product not specified in section II of Part IV of its schedule (Article 3:3).

Apart from the lower cuts and the longer period for effecting their commitments, developing countries benefit from special and differential treatment by way of exemptions from commitments to reduce export subsidies aimed at reducing the cost of marketing exports, including internal transportation and freight (Article 9:4).

Commitments limiting export subsidization also represent new obligations assumed and incorporated in GATT schedules, systematically and transparently. In GATT 1947, there is an exhortation that the use of subsidies on exports of primary products should be avoided and, if not avoided, such subsidies shall not be applied to obtain a more than equitable share of world export trade in a subsidized product (Article XVI:3). This provision (as well as its elaboration under the 1979 Subsidies Code) had also been considered operationally ineffective. The "equitable share" obligation is widely regarded as a dead letter owing to the difficulty of demonstrating that export subsidies are the determining factor (greater than any other factors) in increased market share or market displacement. The reduction commitments as specified in individual schedules plus the obligation not to circumvent them are to become the core obligations on agricultural export subsidies.

It may be noted that the product coverage of the Agreement is defined in Annex 1 thereto, which is more precise than the general definition of primary products in Article XVI of GATT 1947. The notes and supplementary provisions to Article XVI state that for purposes of Section B of that Article, a "primary product is understood to be any product of farm, forest or fishery, or any mineral, in its natural form or which has undergone such processing as is customarily required to prepare it for marketing in substantial volume in international trade". Since fish and fishery products and forestry products are excluded from Annex 1 of the Agreement on Agriculture, subsidization of these sectors would presumably be governed by the Agreement on Subsidies and Countervailing Measures.

The modalities for reduction commitments specify the particular products or product groups (if exports are subsidized) on which the outlay and quantity commitment levels should be established. These are: wheat and wheat flour, coarse grains, rice, oilseeds, vegetable oils, oilcakes, sugar, butter and butter oil, skim milk powder, cheese, other milk products, bovine meat, pigmeat, poultry meat, sheepmeat, live animals, eggs, wine, fruit, vegetables, tobacco, and cotton. Scope was also allowed for negotiating commitments on particular products within product groups.

Since the reduction commitments were embodied in schedules of WTO members, it should not be inordinately difficult to enforce them. To ensure the integrity of export subsidy commitments, provisions to prevent their cir-

<sup>105</sup> GATT document MTN.GNG/MA/W/24, *op. cit.*

cumvention are stipulated in Article 10, the most notable of which perhaps is the onus of proof on a member to establish, in cases where it is claimed that any quantity exported in excess of a reduction commitment level is not subsidized, that no export subsidy, whether listed in Article 9 or not, has been granted in respect of the quantity of exports in question (Article 10:3). Undertakings to develop internationally agreed disciplines on export credits, export credit guarantees or insurance programmes were envisaged in Article 10:2. Presumably, these disciplines would be negotiated under the auspices of the WTO, although it is not certain whether this would, in fact, be the case. There are many good grounds for advocating that multilateral disciplines on the above practices should be negotiated under the aegis of the WTO.

The Agreement also entails, under the provisions on circumvention (Article 10), obligations for WTO members that are donors of international food aid (paragraph 4) to ensure that such aid (i) is provided "to the extent possible in fully grant form or on terms no less concessional than those provided for in Article IV of the Food Aid Convention 1986"; (ii) is not tied directly or indirectly to commercial exports.

Additional disciplines governing the application of export prohibitions and restrictions on foodstuffs in conformity with Article XI:2(a) of the General Agreement were stipulated in Article 12 of the Agreement on Agriculture. The new provisions were apparently a response to the concerns expressed by several participants during the negotiations regarding certain export embargoes applied in the 1970s. Developing countries, other than net-food exporters of specific foodstuffs, are exempted from the new disciplines.

The modalities for reduction commitments mentioned in part that "commitments may be negotiated to limit the scope of subsidies on exports of agricultural products as regards individual or regional markets. The markets to which such commitments apply shall be specified in the lists of commitments on export competition".<sup>106</sup> Unless commitments were assumed in this regard and accordingly reflected in the schedules, the Agreement does not directly limit export subsidy practices that target individual markets *per se* other than generally to reduce outlays and quantities available under reduction commitments. Thus limitations on targeted export subsidy practices or product scope are not governed by any general guidelines under the reform pro-

gramme, but were left to be dealt with under bilateral and plurilateral negotiations. There is a danger that commitments not to subsidize exports to individual markets would be tantamount to carving the world market into separate zones of influence and establishing market-sharing. On the other hand, the Agreement deals with commitments to limit the use of trade-distorting devices rather than commitments not to export, although for certain markets the two are synonymous.

Schedules of some major export-subsidizing jurisdictions seen so far do not specify commitments on export subsidies aimed at individual or regional markets, presumably because there were none. In any case, it is interesting to note the annual consultations envisaged in paragraph 5 of Article 18 (Review of the Implementation of Commitments) in the Committee on Agriculture with respect to the participation of WTO members "in the normal growth of world trade in agricultural products within the framework of the commitments on export subsidies" under the Agreement on Agriculture.

Article 13 of the Agreement (Due Restraint), termed the "peace clause," insulates agricultural subsidies, where the commitments are respected, from the relevant "remedies" available under the Subsidies Agreement. However, countervailing duties may be applied except against Annex 2 ("Green Box") subsidies (see box 12).

The exclusion of agricultural subsidies from the disciplines and remedies mentioned above obviously indicates that the period of reform is a testing period for WTO members. Moreover, the trading community is apparently not ready to entertain the notion of banning export subsidies on agricultural products, or to apply the normative rules developed in the Agreement on Subsidies and Countervailing Measures to control trade-distorting forms of domestic support in the agricultural sector. However, they have agreed to continue negotiations on reform one year before the end of the implementation period.

At the very least, the Agreement on Agriculture offers the prospect of truly effective multilateral control of domestic support and export subsidies. Against the backdrop of the huge budgetary costs of supporting the agricultural sector and the endemic distortions in multilateral trade, participants have gathered the various national reforms already taking place unilaterally into a reinforced contractual framework. This would prevent a return to old

<sup>106</sup> See again GATT document MTN.GNG/MA/W/24.

**'PEACE CLAUSE' PROVISIONS**

Domestic support measures exempted from reduction commitments ('Green Box').

- Non-actionable for purposes of countervailing duties.
- Exempt from actions based on Article XVI of GATT 1994 and Part III of the Subsidies Agreement.
- Exempt from actions based on non-violation nullification or impairment of the benefits of tariff concessions in the sense of Article XXIII:1(b) of GATT 1994.

Domestic support measures subject to reduction commitments; other exempted subsidies, such as direct payments conforming to requirements of Article 6:5; *de minimis* domestic support levels:

- Exempt from the imposition of countervailing duties unless injury or threat thereof is determined in accordance with Article VI of GATT 1994 and Part V of the Subsidies Agreement.
- Exempt from actions based on Article XVI:1 of GATT 1994 or Articles 5 and 6 of the Subsidies Agreement, provided that such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year.
- Exempt from actions based on non-violation nullification or impairment of the benefits of tariff concessions in the sense of Article XXIII:1(b) of GATT 1994, provided that such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year.

Export subsidies in conformity with Part V of the Agreement on Agriculture:

- Subject to countervailing duties only upon a determination of injury or threat thereof.
- Exempt from actions based on Article XVI of GATT 1994 or Articles 3, 5 and 6 of the Subsidies Agreement.

habits and ensure the emergence of improved opportunities for the naturally efficient producers and traders.

Had the normative refinements of Article XVI:1 and Article XVI:3 of the General Agreement as they apply to agriculture been negotiated in the Uruguay Round, they would have become mired in hopelessly ineffectual

improvements. The reduction commitments on domestic support and on export subsidies, as reflected in individual schedules - even when prompted by autonomous actions owing to the growing budgetary difficulties of some participants - have been locked in, to be available as possible inputs for use in the next episode of multilateral negotiations on agriculture under the auspices of the World Trade Organization.

## G. Other sectoral exceptions

In anticipation of the negotiation of specific multilateral rules on trade in civil aircraft, certain provisions of the Agreement on Subsidies do not apply to this sector. Two of the criteria for the assumption of the existence of serious prejudice, the 5 per cent ad valorem threshold (Article 6:1(a)), and the forgiveness of government-held debt (Article 6:1(d)), do not apply fully to civil aircraft nor to the provision on the "non-actionability" of assistance for research activities (Article 8:2(a)). Renegoti-

ations of the Agreement on Civil Aircraft, which will be included in Annex 4 of the WTO Agreement are continuing with the objective of incorporating the results of bilateral negotiations between the United States and the EC.

Furthermore, the Multilateral Steel Agreement on which negotiations are continuing, is expected to include more stringent disciplines on subsidies than those of the Agreement on Subsidies and Countervailing Measures.

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## H. Conclusions

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The first conclusion that emerges from a preliminary analysis of the Agreement is that some of the more contentious issues in relation to subsidies have been, or will possibly continue to be, negotiated outside the scope of the Agreement. Mention has already been made that some of the provisions related to prohibited and actionable subsidies - including their adverse effects, the serious prejudice they may cause, and the remedies to deal with them - may not apply to steel, agriculture and civil aircraft, or may eventually apply to them in a different manner. The specific provisions of the Agreement on Agriculture and its Article 13, in respect of actionable subsidies, will apply to agricultural products. As regards the parallel negotiations on a Multilateral Steel Agreement and an Agreement on Trade in Civil Aircraft, it is not yet clear whether multilaterally negotiated instruments will emerge or whether the text of the Agreement on Subsidies and Countervailing Measures will finally apply, with some modifications, to trade in these two sectors.

To the extent that the Agreement strengthens the capacity of governments to resist demands for subsidization in terms of practices which have been clearly prohibited, the operation of the Agreement will obviously be beneficial for the multilateral trading system. Similarly, the fact that other subsidies have been categorized as permissible, but actionable, with comprehensive guidance on determination of adverse effects and serious prejudice, together with detailed remedies for these, may also inject a degree of predictability into international trade in so far as governmental use of such subsidies is concerned.

In overall terms, the approach of the new Agreement is to give members three years to bring existing programmes into conformity with its provisions. During this period, members would not be subject to the provisions of Part II of the Agreement, which deals with prohibited subsidies and the remedies for them. It could be argued that this three-year period would in fact imply a continuation of the status quo prevailing before the establishment of the WTO. And yet, considering the extremely difficult situation obtaining in the area of subsidies in international trade, and the natural reluctance of governments to take on vested interests which subsidies inevitably create, it is,

in effect, a clear and positive step forward. Similarly, the flexibility given to developing countries, i.e. other than the countries listed in Annex VII, would be exempt from the blanket prohibition on certain categories of subsidies for a period of eight years. In respect of subsidies contingent upon the use of domestic over imported goods, they have flexibility for five years and least developed countries would have such flexibility for eight years.

The implementation of the Agreement would be entrusted to a Committee on Subsidies and Countervailing Measures. A new institutional feature is the establishment of a Permanent Group of Experts (PGE), composed of five independent persons, who are highly qualified in the fields of subsidies and trade relations. It is not yet clear exactly what role the PGE would be required to play, although Article 4.5 stipulates that it would be called upon to assist panels in determining whether a particular measure is a prohibited subsidy.

The Agreement contains provisions relating to remedies against prohibited and actionable subsidies and non-actionable subsidies, which are graded in terms of time constraints. In the Dispute Settlement Body (DSB), the membership of which will replicate the membership of the General Council of the WTO and of the Trade Policy Review Body, there is a certain automaticity in the operation of the dispute settlement procedures, and the establishment of the panels. In the case of prohibited subsidies, the DSB would be required to establish a panel if reference is made to it within 30 days, unless the DSB decides by consensus not to do so. The panel would be required to submit its report within 90 days. On receipt of the panel report the DSB is required to adopt the report within 30 days, unless one of the parties to the dispute formally notifies it of its decision to appeal to the Appellate Body. These time-limits are more flexible in the case of remedies against actionable subsidies, the periods noted above being extended to 60 days for a mutually agreed solution, 120 days for the panel to issue its findings and 60 days for the Appellate Body. In order to ensure that the dispute settlement process is not derailed the DSB would be required to accept the decision of the Appellate Body, unless the DSB decides by consensus not to adopt the appellate report.

The provisions of the Understanding on Rules and Procedures Governing the Settlement of Disputes, in so far as they provide for automaticity for the establishment of panels, and the adoption of a decision, through the Appellate Body mechanism, as to whether the report of the panel is to be accepted or not, will hopefully eliminate the difficulties that arose in the implementation of the Tokyo Round Code, when whichever party to the dispute was adversely affected by the panel's findings could block the report unilaterally. The procedures now require a decision not to adopt the panel or Appellate Body report to be taken by consensus. The practical effect will be to impart greater certainty to the procedure for adoption of panel reports, and curb the tendency to offset adverse findings against other trade concessions.

In the final analysis, the successful implementation of the Agreement will depend on the collective will of its members. To the extent that the Agreement offers a comprehensive definition and categorization of subsidies, together with detailed remedies, should enforce greater discipline on the use of subsidies with the resultant benefits to international trade. The Agreement similarly provides for more detailed provisions than its predecessor in respect of initiation of countervailing duty investigations, calculation of the amount of subsidy

in terms of benefit to the recipient, and definition of injury to a domestic industry or undertakings. Some of the issues that were not negotiated during the Uruguay Round, on which the provisions of the new Agreement carry over the texts of the previous Tokyo Round agreements as regards actions which governments might take indirectly, particularly the levy and collection of countervailing duties, are likely to encourage governments to resort to dispute settlement with a view to testing them and seeking panel rulings to enforce their respective positions.

As explained above, the negotiations on this issue have been closely focused on the United States, both as a demandeur with respect to subsidies and as the main user of countervailing duties. While the United States is still the principal user, with 42 cases initiated in 1992-1993 (followed by Australia with 12), many developing countries, with the liberalization of their import regimes, consider themselves to be particularly vulnerable to subsidized imports and are introducing countervailing duty laws. It is possible that developed countries will challenge the application of countervailing duties by developing countries, *inter alia*, on procedural grounds (as in the EC-Brazil case)<sup>107</sup> with a view to discouraging them from resorting to this mechanism. ■

<sup>107</sup> Brazil's countervailing duty proceeding concerning imports of milk powder from the EC. See GATT, "Status of work in panels and implementation of panel reports - Report by the Director-General" (C/188), 10 June 1994.

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## AGREEMENT ON TEXTILES AND CLOTHING

### A. Background of the MFA and its impact

The textiles and clothing sector has served as the engine of growth for many developing countries, accounting for nearly 45 per cent of the developed market-economy countries' imports from the developing countries (see charts 1 and 2). The shares of textiles and clothing in total manufacturing value added and employment in the developing countries are substantial. Their combined share in value added varies between 15 and 30 per cent and in employment between 20 and 40 per cent for the majority of developing countries.<sup>108</sup> Since the early 1960s, when developing countries began to acquire comparative advantages in the textiles and clothing sector, developed countries sought a special arrangement which would permit them to escape certain GATT obligations<sup>109</sup> and to negotiate quantitative restraint arrangements on a discriminatory basis. By alleging that imports from "low-cost" suppliers were likely to cause "market disruption" to their domestic industries, the developed countries obtained an agreement to treat textiles and clothing as exceptions from the GATT rules and to allow them to impose import restrictions on a selective basis. This agreement was first known as the Short-Term Cotton Arrangement in 1961, then as the Long-Term Cotton Arrangement in 1962, and eventually as the Arrangement Regarding International Trade in

Textiles in 1974, or the Multi-Fibre Arrangement (MFA) for short.

The MFA sets the terms and conditions to govern the imposition of quantitative restrictions on textile and clothing exports of developing countries, either through negotiations of bilateral agreements or on a unilateral basis. The terms of such bilateral agreements and/or unilateral measures are notified to the Textiles Surveillance Body (TSB). The role of this body is to ensure that the obligations in the MFA regarding such arrangements are respected. Under the MFA, the bilateral agreements negotiated between importing and exporting countries contain provisions relating to the products traded (e.g. volumes of trade to which annual growth rates are applied), but they differ in detailed terms according to the products covered and countries concerned. Developed countries, under the MFA, chose not to impose restrictions on imports from other developed countries,<sup>110</sup> with the exception of Japan. Many do, however, apply relatively high tariffs on textile products.

Since the inception of the MFA, successive negotiations for its extension have continually increased its product and country coverage and intensified its discriminatory character. Over the years the implementation

<sup>108</sup> See Ying-Pik Choi, Hwa Soo Chung and Nicolas Marian, *The Multi-Fibre Arrangement in Theory and Practice* (London and Dover, New Hampshire: Frances Pinter (Publishers) Ltd., 1985), pp. 60-61.

<sup>109</sup> Article XIX of GATT requires that all safeguard actions should be non-discriminatory in application and temporary in duration, and it provides the right to equivalent compensation for the loss of market suffered by the affected parties.

<sup>110</sup> Sometimes, however, developed countries do take actions against each other outside the MFA. For example, during the period 1980 to 1983 the EC initiated three anti-dumping actions against exports of textiles from the United States. Two resulted in the imposition of a definitive duty, and one in a finding of no dumping.

of the MFA has diverged from the original spirit and aims of the Arrangement. The 1986 Protocol of Extension has made the MFA more restrictive in several important respects, especially with regard to enlarged fibre coverage. The regime began with restraints on cotton textiles and eventually extended its coverage to synthetic fibres and wool. With the renewal of the MFA in 1986 its application was finally extended to all vegetable fibres and silk blends. Consequently all fibres, with only a few exceptions, are covered by the MFA. It permits importing countries to apply import restrictions even on products in which there is no domestic production. Developing exporting countries accepted this extension under strong pressure from developed countries.<sup>111</sup> On 9 December 1993, the MFA was further extended for another year from 1 January to 31 December 1994. As of 24 November 1993, the MFA had 44 signatories.<sup>112</sup> For the bilateral restraint agreements under the MFA as of 31 December 1993 see table 7.

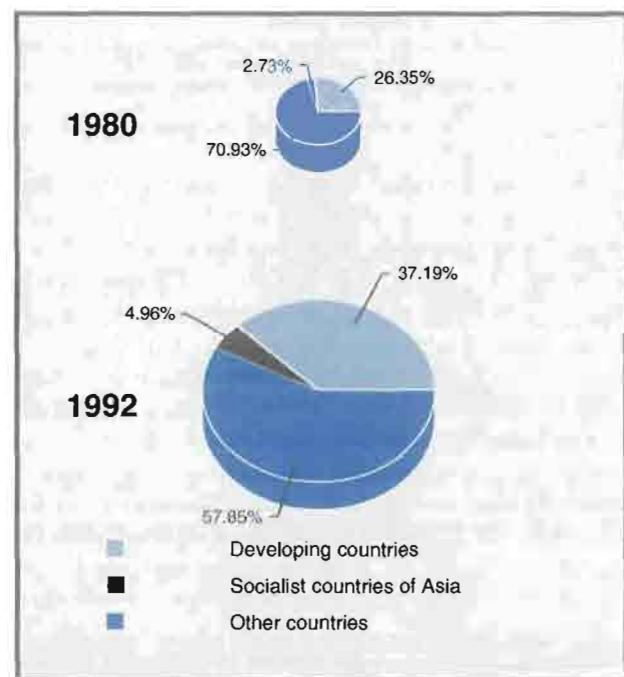
With every extension of the MFA,<sup>113</sup> restraints were intensified and the country and product coverage was enlarged. Bilateral agreements concluded under the MFA have become increasingly restrictive. The importing countries have also tended to resort to additional restrictive measures despite the quota restrictions in operation under the existing Arrangement.<sup>114</sup> Increased usage of several new MFA measures tends to further erode the trust which developing countries had originally placed in the MFA.<sup>115</sup>

Although in recent years exports of developing countries to developed countries have been increasing, the adverse impact of the MFA on the exports of the developing countries should not be discounted. Without the MFA, exports of textiles and clothing from developing to developed countries would be greater. A number of studies have found the

decline in export opportunities from the MFA to be substantial for developing countries. For example, it is estimated in a study by the United States International Trade Commission that the value of exports of currently constrained suppliers to the United States market would rise by 20.5 per cent for textiles and 36.5 per cent for clothing, or an average of 35 per cent in both product groups.<sup>116</sup> Another recent study estimated that, without the MFA, exports from MFA exporters to MFA importers would increase by 26 per cent for clothing and 10 per cent for textiles.<sup>117</sup>

Chart 1

## DMECs' IMPORTS OF TEXTILES AND CLOTHING BY SOURCE



Source: United Nations Statistical Office, COM-TRADE.

<sup>111</sup> See Madhavi Majmudar, "The Multi-Fibre Arrangement (MFA IV) 1986-1991: A move towards a liberalized system?", *Journal of World Trade*, April 1988.

<sup>112</sup> These included Argentina, Austria, Bangladesh, Brazil, Canada, China, Colombia, Costa Rica, Czech Republic, Dominican Republic, EC, Egypt, El Salvador, Fiji, Finland, Guatemala, Honduras, Hong Kong, Hungary, India, Indonesia, Jamaica, Japan, Lesotho, Macau, Malaysia, Mexico, Norway, Pakistan, Panama, Paraguay, Peru, Philippines, Poland, Republic of Korea, Romania, Singapore, Slovak Republic, Sri Lanka, Switzerland, Thailand, Turkey, United States and Uruguay. See GATT document COM.TEX/75/Rev. 1, 26 November 1993.

<sup>113</sup> With the exception of the last three extensions which were initiated to coincide with the conclusion of the Round.

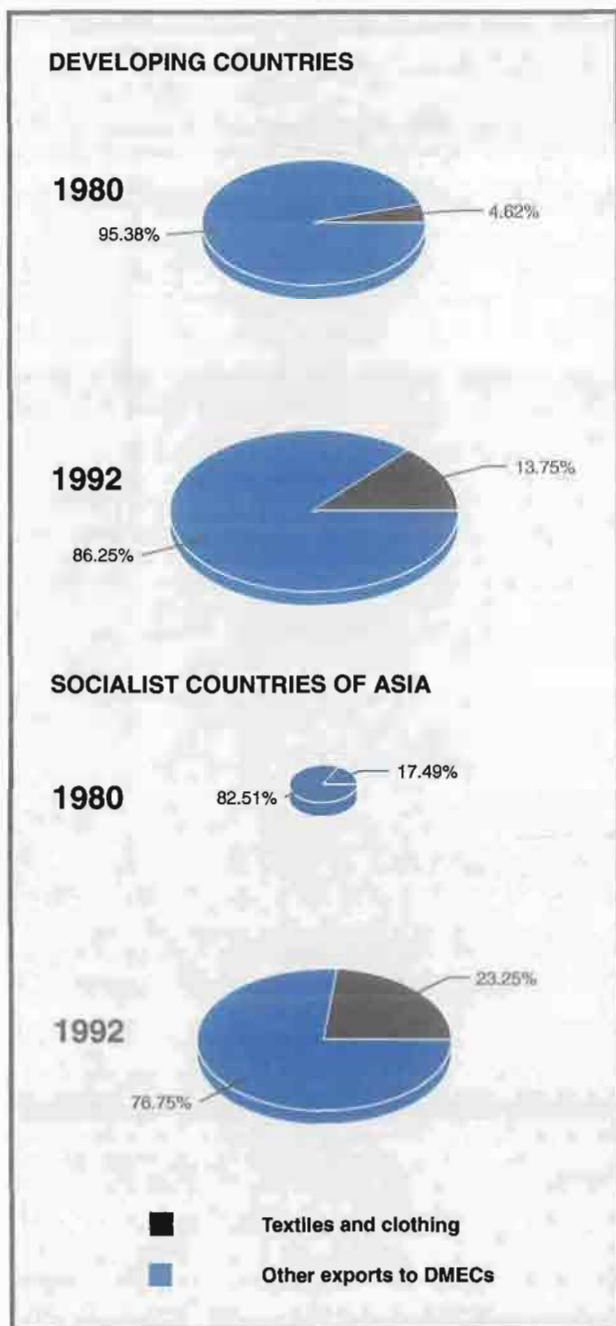
<sup>114</sup> According to the UNCTAD *Trade and Development Report, 1988* (United Nations publication, Sales No. 1988.II.D.8), 1989, about one half of the imports of textiles and clothing into the developed countries are subject to NTMs, both within and outside the MFA; in fact, for this sector the ratio of imports into major developed countries from the developing countries covered by NTMs exceeds 70 per cent.

<sup>115</sup> See the Chairman's summing up of the meeting of the International Textiles and Clothing Bureau held in Macau on 1-4 September 1987.

<sup>116</sup> See USITC, "The economic effects of significant U.S. import restraints", ITC Publication 2222, October 1989.

<sup>117</sup> See Y. Yang, "The impact of MFA phasing out on world clothing and textile markets", National Centre for Development Studies, Australian National University, Canberra, Australia (1993) (forthcoming in *Journal of Development Studies*).

Chart 2

EXPORTS TO DMECs: SHARE OF  
TEXTILES AND CLOTHING

Source: United Nations Statistical Office, COM-TRADE.

Since the difficulties of the textile and clothing industries of the developed countries are largely structural, one of the basic objectives of the MFA was to provide a 'breathing space' for these industries to adjust to international shifts of comparative advantage. In spite of the long years of protection, employment

has continued to decline. The employment problem which developed countries used to justify protection cannot be resolved by this method alone. Employment in textiles and clothing has been declining, mainly due to productivity increases reflecting the substitution of machines for labour through automation, computerization and other labour-saving devices. The MFA has helped to stabilize production levels in most developed importing countries. The industry has also benefited from heavy capital investment of a labour-saving nature. The loss of employment as a result of this and of technological developments has nevertheless continued. Even if the domestic industry maintains its share of the market, the declining trend of employment will persist, spurred on in some countries by high wages in the textile industry. As a result, the MFA is increasingly becoming a regime for protecting machines rather than jobs.

The MFA also has adverse effects on consumer prices and expenditure in the developed countries. Such effects have been amply described in studies by such bodies as the World Bank and OECD. According to the *World Development Report 1987*,<sup>118</sup> the protection of textiles and clothing in the United States cost the consumer many billions of dollars. A study by OECD<sup>119</sup> indicated that the burden of protection in textiles and clothing fell most heavily on the lower-income households of the OECD region, in which clothing accounted for a larger share of their consumption expenditure. Another study has calculated that protecting the Canadian clothing industry cost lower-income households four times as much as higher-income households. For the United States, according to the Economic Report of the President (1988),<sup>120</sup> the protection of textiles and clothing costs between \$200 and \$400 a year per household.

The introduction of the concept of "market disruption" paved the way for an institutionalized derogation from the fundamental principles and rules of the General Agreement, thus creating an imbalance of rights and obligations. Its perpetuation and proliferation have disrupted the autonomous processes of structural adjustment, which are essential to maintain the equilibrium of a healthy world economy. Past experience has shown that certain important provisions of the MFA concerning structural adjustment and the

<sup>118</sup> World Bank, *World Development Report 1987* (Washington, D.C., 1987).

<sup>119</sup> OECD, *Costs and Benefits of Protection* (Paris, 1985).

<sup>120</sup> See Economic Report of the President, transmitted to the United States Congress, February 1988.

Table 7

## BILATERAL MFA RESTRAINT AGREEMENTS IN FORCE ON 31 DECEMBER 1993

Suppliers	Restraining importers						Number of Agreements
	Austria	Canada	European Communities	Finland	Norway	United States	
Argentina			x				1
Bangladesh		x				x	2
Brazil		x	x			x	3
China	x	x	x	x	x	x	6
Colombia		x				x	2
Costa Rica						x	1
Czech Republic		x <sup>a</sup>	x		x	x	4
Dominican Republic		x				x	2
Egypt						x	1
El Salvador						x	1
Guatemala						x	1
Hong Kong	x	x	x	x	x	x	6
Hungary		x	x		x	x	4
India	x	x	x	x	x	x	6
Indonesia		x	x		x	x	4
Jamaica						x	1
Macau	x	x	x	x	x	x	6
Malaysia		x	x		x	x	4
Mexico						x	1
Pakistan		x	x		x	x	4
Panama						x	1
Peru			x				1
Philippines		x	x		x	x	4
Poland		x	x		x	x	4
Republic of Korea	x	x	x	x	x	x	6
Romania		x	x		x	x	4
Singapore		x	x	x	x	x	5
Sri Lanka		x	x	x	x	x	5
Thailand	x	x	x		x	x	5
Turkey		x				x	2
Uruguay		x					1
Total	6	22	19	7	16	28	98

Source: ITCB estimates, and GATT documents COM.TEX/SB/1799 and 1873.

<sup>a</sup> Including the Slovak Republic, as a result of the conversion of the previous agreement with the former Czech and Slovak Federal Republic into two agreements.

need to avoid proliferation have been disregarded in its implementation,<sup>121</sup> and that the perpetuation of restraints has disrupted autonomous industrial adjustment. Voluntary export restraints such as those inherent in the MFA have been extended to the areas of steel, auto-

mobiles, consumer electronics, footwear, metal products, wood products, machine tools and semiconductors. In this sense, the integration of this sector into GATT 1994 has a profound significance for the multilateral trading system.<sup>122</sup>

<sup>121</sup> Article 1:4 of the MFA provides that: "Actions taken under this Arrangement shall not interrupt or discourage the autonomous industrial adjustment process of participating countries. Furthermore, actions taken under this Arrangement should be accompanied by the pursuit of appropriate economic and social policies, in a manner consistent with national laws and systems, required by changes in the pattern of trade in textiles and in the comparative advantage of participating countries, which policies would encourage businesses which are less competitive internationally to move progressively into more viable lines of production or into other sectors of the economy and provide increased access to their markets for textile products from developing countries." For its part, Article 1:7 states the following: "The participating countries recognize that, since measures taken under this Arrangement are intended to deal with the special problems of textile products, such measures should be considered as exceptional, and not lending themselves to application in other fields".

<sup>122</sup> See Xiaobing Tang, "Textiles and the Uruguay Round of Multilateral Trade Negotiations", *Journal of World Trade*, Vol. 23, No. 3, June 1989, pp. 54-56.

## B. Textiles and clothing and the multilateral trade negotiations

### 1. Textiles and clothing in the previous GATT Rounds

Owing to the persistent protectionist pressures from the textile and clothing industries in the developed countries, the previous rounds of GATT multilateral trade negotiations had done little to liberalize trade in the textile sector.<sup>123</sup> While each of the GATT rounds led to trade liberalization in products of major export interest to the developed countries, trade in textiles and clothing, a sector of increasing export interest to the developing countries, evolved in the opposite direction. During the Dillon Round, the Short-Term Arrangement (STA) came into being. This subsequently evolved into the Long-Term Arrangement (LTA). Both these covered cotton textiles only. During the Kennedy Round the importing countries made attempts to extend the coverage to wool and man-made fibres. This led to the negotiation of the Multi-Fibre Arrangement (MFA) prior to the launching of the Tokyo Round.

During the Kennedy and Tokyo Rounds, in anticipation of increasing competition from the developing countries, political pressures built up in the United States and the European Communities (EC) against any possible liberalization of trade barriers in the textiles sector. In fact, commitments on the part of the United States Administration to ensure that the LTA and MFA would be extended were preconditions for the granting of negotiating authority by the United States Congress for the each of these Rounds, in turn. While developing countries pressed hard for the removal or reduction of such barriers in this sector of particular export interest to them, the result was only minimal liberalization in respect of quantitative restrictions and tariffs.<sup>124</sup>

### 2. Textiles and clothing and the 1982 Ministerial Meeting

In view of their unhappy experience with the 1977 Protocol of Extension of the MFA and the retention clauses, which facilitated the loosening of MFA disciplines such as 'good-will', 'exceptional cases' and 'anti-surge' in the 1981 Protocol of Extension, in 1982 the developing countries worked together to ensure that the "textiles issue" was addressed at the 1982 Ministerial Meeting. The proposal by the developing countries, which was substantially diluted by the developed countries in the course of negotiation, was finally included in the GATT Ministerial Declaration of 1982 and its work programme.<sup>125</sup>

Pursuant to these decisions, a Working Party on Textiles and Clothing was established and three broad options were identified.<sup>126</sup> However, owing to the divergent views among the participants, it was not possible to reach a consensus recommendation on any particular option. Developed countries contended that progress towards further trade liberalization was a responsibility shared by all participants. Developing countries stated that only those countries that were maintaining restrictions inconsistent with GATT provisions had the responsibility for liberalizing such measures, which should not be borne by the victims of discriminatory restrictions on their exports.

The GATT Working Party on Textiles and Clothing therefore confined its work to identifying three options for possible liberalization of trade in this sector, and failed to move on to a fuller examination of the consequences of phasing out restrictions or of the continua-

<sup>123</sup> For details, see Thomas B. Curtis and John Robert Vastine, Jr, *The Kennedy Round and the Future of American Trade* (New York: F.A. Praeger, 1971), and UNCTAD, "Assessment of the results of the multilateral trade negotiations" (TD/B/778/Rev. 1), 1982.

<sup>124</sup> For example, a special provision or the so-called "snapbook clause" was incorporated into the United States Trade Agreement Act of 1979 for the implementation of the Tokyo Round results as Section 504. This Section called simply for the restoration of textiles and apparel tariffs to the level which existed on 1 January 1975 if the MFA was not renewed. See Public Law 96-39, 93 Stat. 189 (16 July 1979).

<sup>125</sup> GATT document L/5424, 29 November 1982.

<sup>126</sup> (A) Full application of GATT provisions with a movement towards liberalization; (B) full application of GATT provisions as envisaged in Option A, combined with liberalization of trade measures irrespective of their GATT conformity; and (C) liberalization under existing frameworks. See *GATT Activities 1985*.

tion of restrictions under the existing regime. As a result, the 1982 Ministerial Meeting had no visible impact on the containment of protectionist trends in the United States even though demand for textiles expanded rapidly from 1983 onwards. Restrictions and additional measures proliferated rapidly, and efforts to work out constructive modalities for liberalization were thwarted.

### 3. Negotiations on textiles and clothing in the Uruguay Round

#### (a) Negotiating mandate

Attributed to the efforts of the developing countries, the Punta del Este Ministerial Declaration included a special negotiating mandate for the textiles and clothing sector as follows:<sup>127</sup>

Negotiations in the area of textiles and clothing shall aim to formulate modalities that would permit the eventual integration of this sector into GATT on the basis of strengthened GATT rules and disciplines, thereby also contributing to the objective of further liberalization of trade.

Thus, for the first time the textiles and clothing sector was specifically included as a subject in the multilateral trade negotiations, and the objectives of liberalizing trade in this sector and of reintegrating it into the GATT system were recognized by all participants in the Uruguay Round. Although the mandate was ambiguously formulated, this is in sharp contrast to earlier GATT Rounds in which the textiles and clothing sector was dealt with before the negotiations began or else parallel to the Rounds, though certain reductions in textiles and clothing tariffs were negotiated.

#### (b) Negotiating process

In February 1987, a Negotiating Group on Textiles and Clothing (NGTC) was established to examine techniques and modalities for integration on the basis of proposals submitted by the participants,<sup>128</sup> with a view to completing such an examination by the Mid-Term Review to be held at Montreal at the end of 1988.<sup>129</sup> However, it proved impossible to conclude the examination before the Mid-Term Review, and the NGTC was unable to agree on a consensus text for consideration by the Ministers before the Montreal meeting.<sup>130</sup>

At the Montreal Ministerial Meeting in December 1988, textiles and clothing constituted one of the four key issues on which no agreement was reached. The participating countries decided that the problems in these four areas should be resolved in Geneva and in the meantime the negotiations in the other areas would remain frozen.<sup>131</sup>

In April 1989, the Trade Negotiations Committee (TNC) recognized the importance of the textile sector and its key role in the Uruguay Round, and agreed that the modalities for the integration of the textiles and clothing sector into GATT should cover the phase-out of the MFA and other GATT-inconsistent restrictions. The modalities should also include the time-span and the progressive character of the integration process, which should commence after the conclusion of the Round, and deal with the question of special treatment for the least developed countries. The TNC invited participants to put forward additional proposals not later than 30 June 1989.<sup>132</sup>

The Mid-Term decision of the TNC in April 1989 was of particular importance since it implied a commitment on all sides to achieve

<sup>127</sup> GATT document MIN.DEC, 20 September 1986.

<sup>128</sup> See GATT document MTN.GNG/NG4/1, 24 February 1987.

<sup>129</sup> See GATT document MTN.GNG/NG4/5, 15 December 1987.

<sup>130</sup> For details, see GATT, "News of the Uruguay Round of MTNs" (NUR 023), 14 December 1988.

<sup>131</sup> The developing textile-exporting countries insisted on a freeze on further import restrictions under the MFA IV, an agreement to negotiate the winding down of the MFA, with the process starting upon the expiry of the MFA IV, and a time-frame set for the end of this process and integration of the sector into GATT. The EC, with the support of other developed textile-importing countries, insisted on a commitment by developing countries regarding trade liberalization in this sector and linkage with other issues, such as enhanced intellectual property rights protection. As no agreement was reached by the Ministers at Montreal, textiles and clothing together with other three other issues, i.e. agriculture, safeguards and TRIPs, would require further negotiation. It appeared from the failure of the Ministers to achieve a consensus on textiles and clothing at Montreal that some developed countries, namely the United States and the EC, still lacked the political will to negotiate. See Xiaobing Tang, *op. cit.*, p. 64; GATT documents MTN.GNG/NG4/W/10 of 15 February 1988, MTN.GNG/NG4/W/11 of 27 April 1988, MTN.GNG/NG4/W/12 of 24 May 1988, MTN.GNG/NG4/W/15 of 17 June 1988, MTN.GNG/NG4/W/21 of 28 September 1988, MTN.GNG/NG4/11 of 11 November 1988, and MTN.TNC/7(MIN) of 9 December 1988.

<sup>132</sup> See GATT document MTN.TNC/11, 21 April 1989.

integration into GATT after the expiry of the MFA in 1991. It also reflected the desire of all participants that the process of integration should be gradual and progressive. It was accepted that the MFA would be succeeded by a transition period that would ensure the achievement of full integration by the time it came to an end.

The TNC decided in July 1989 that national positions should be tabled and discussed before the end of the year. Intensive negotiations to bridge the outstanding differences should begin in January 1990. However, the negotiations could not take place in the first half of 1990 because of the basic difference in the approaches of the participants. Most of them were in favour of an MFA-based approach,<sup>133</sup> but Canada and the United States insisted on the substitution of global quotas for the existing restrictions at the beginning of the transition period.<sup>134</sup> This disparity prevented the NGTC from developing a framework for the transition period before the summer break.<sup>135</sup>

The actual negotiations began after the 1990 summer break on the basis of a text prepared by the Chairman of the NGTC on his own responsibility.<sup>136</sup> The principal issues in the negotiations on textiles and clothing were product coverage during the transition period, the phase-out of the MFA restrictions, the procedures for transitional safeguards and the application of strengthened GATT rules and disciplines.

At the end of 1990, the negotiations gathered pace after the United States indicated its willingness to proceed on the basis of the MFA approach.<sup>137</sup> At the Brussels Ministerial Meeting in December 1990, the Chairman's text was the basis of discussion. However, the negotiations on textiles and clothing ended in an impasse. They were resumed the following year, but wide differences still remained on the central problem of the so-called "economic package", consisting of the product coverage of the agreement, the percentage for the integration of products in stages, increases in the growth rates for products not yet integrated and the duration of the agreement.<sup>138</sup>

In order to break the stalemate, the Director-General of the GATT, on 20 December 1991 exercised his best judgement and arbitrated on the outstanding issues by introducing a text of the agreement on textiles and clothing as part of the package of the so-called "Dunkel Draft" of the Final Act embodying the results of the Uruguay Round.<sup>139</sup> Apart from codifying the agreements reached early in the negotiating process, the Dunkel text on textiles and clothing resolved the outstanding issues such as the duration of the transition period, growth rates to be applied to existing and new quotas, transitional safeguards, and the relationship of the transition process with the strengthened GATT rules.<sup>140</sup>

The domestic protectionist pressures continued during the course of the negotiations and even after the conclusion of the Uruguay Round.<sup>141</sup> On the eve of the final deadline for

<sup>133</sup> See GATT documents MTN.GNG/NG4/W/23 of 8 June 1989 (ITCB proposal); MTN.GNG/NG4/W/28 of 13 October 1989 (India's proposal); MTN.GNG/NG4/W/24 of 20 July 1989, MTN.GNG/NG4/W/36 of 2 February 1990, MTN.GNG/NG4/W/40 of 5 March 1990 and MTN.GNG/NG4/W/51 of 12 June 1990 (EC proposals); MTN.GNG/NG4/W/35 of 1 February 1990, MTN.GNG/NG4/W/48 of 14 May 1990 and MTN.GNG/NG4/W/54 of 14 June 1990 (Japan's proposals).

<sup>134</sup> See GATT documents MTN.GNG/NG4/W/27 of 25 September 1989 and MTN.GNG/NG4/W/42 of 5 March 1990 (Canada's proposals); MTN.GNG/NG4/W/26 of 21 September 1989, MTN.GNG/NG4/W/33 of 14 December 1989, MTN.GNG/NG4/W/37 of 5 February 1990, MTN.GNG/NG4/W/43 of 5 March 1990 and MTN.GNG/NG4/W/46 of 14 May 1990 (United States proposals). See also Xiaobing Tang, *op. cit.*, pp. 62-64.

<sup>135</sup> See GATT documents MTN.GNG/NG4/W/56 of 12 July 1990 and MTN.GNG/NG4/W/56, Rev. 1 of 18 July 1990.

<sup>136</sup> Uruguay Round, Trade Negotiations Committee, "Draft agreement on textiles and clothing" (MTN/TNC/W/35 Rev. 1), 3 December 1990.

<sup>137</sup> On 17 July 1990, the United States Senate approved legislation (HR 4328), the Textiles, Apparel, and Footwear Trade Act of 1990, to restrict the growth of textile imports to 1 per cent a year. In addition, the legislation provided for a freeze on footwear imports to 1989 levels, tied quota increases to the exporter's purchases of United States farm imports, and provided for the creation of a quota auctioning programme in 1991 for 20 per cent of imported textiles and apparel. The bill passed by a vote of 68-32 in the Senate. On 18 September 1990, the United States House of Representatives approved an identical bill by a vote of 271-149. President Bush vetoed the bill on 5 October 1990. On 10 October 1990, the House failed to overturn the presidential veto with a 275-152 vote, 10 votes short of the two thirds necessary to block the veto. See 136 *U.S. Congress Rec.* H9,326-40 (daily ed., 10 October 1990). For details see also Terence P. Stewart (ed.), *The GATT Uruguay Round - A Negotiating History (1986-1992)*, Vol. I: *Commentary* (Deventer (Netherlands), Boston: Kluwer Law and Taxation Publishers, 1992), pp. 326-330.

<sup>138</sup> GATT document MTN.TNC/W/89/Add.1, 7 November 1991.

<sup>139</sup> GATT document MTN.TNC/W/FA, 20 December 1991.

<sup>140</sup> See Stewart, *op. cit.*, pp. 351-356.

<sup>141</sup> For example, textiles and clothing were excluded from the United States Omnibus Trade and Competitiveness Act of 1988 and as a result the United States Administration had no mandate to negotiate for several years. See also the

the conclusion of the negotiations on 15 December 1993, some developed countries were threatening to break the deal by demanding significant market access offers in textiles and clothing from some developing countries. In the end a small change, but nevertheless important in view of the position of the major developed importing countries, was made in the Dunkel draft on textiles and clothing.<sup>142</sup> Textiles and clothing continued to be a contentious issue, however, until the Marrakesh Ministerial Meeting in April 1994 when the Final Act, including the Agreement on Textiles and Clothing, was eventually adopted.<sup>143</sup>

### (c) *Main issues*<sup>144</sup>

In the course of the negotiations, several aspects connected with the process of integration were the subject of intensive negotiations. Among them the following were important: modalities for phasing out the MFA restrictions; the extent of product coverage during the transition period; the nature of transitional safeguards; the application of strengthened GATT rules and disciplines; the duration of the transition period; and new entrants, small suppliers, and cotton-producing and least developed countries.

*Phasing out MFA restrictions:* The modality for the phase-out of MFA restrictions during the transition period was the core of the negotiations. Several ways of dismantling these restrictions in a progressive manner were suggested.

The developing exporting countries, represented by the International Textiles and

Clothing Bureau (ITCB)<sup>145</sup> in Geneva proposed the following three elements for the phase-out: (i) liberal action to be taken at the beginning of the transition process. Such action should include the immediate integration of certain products like children's clothing, products of vegetable fibres and silk blends, hand-woven fabrics and products made thereof. It should also provide for the immediate removal of restrictions on small suppliers and least developed countries; (ii) a programmed elimination of the remaining restrictions, following the stages of processing. The restrictions on tops and yarns would be removed initially, followed by those on fabrics, and then on made-up articles and, in the last stage, restrictions on clothing would be lifted; (iii) an accelerated expansion of the quotas while they were awaiting the phase-out. In general, the developing countries have consistently emphasized that the dismantling of the restrictions should commence from the very beginning and continue progressively throughout the transition period until completed.

The ASEAN countries submitted a proposal<sup>146</sup> which generally followed the ITCB approach. With regard to the existing MFA restrictions, the ASEAN and Nordic countries<sup>147</sup> adopted the progressive enlargement of quotas as the technique for phasing out. They proposed that the quotas should be progressively increased in such a manner that by the end of the transition period they would have lost all restrictive effect and become redundant.

The EC shared the developing countries' approach in respect of progressive inte-

statement of Mr. Ronald J. Sorini, Fruit of the Loom, Inc., before the Subcommittee on Trade, Committee on Ways and Means, of the United States House of Representatives, 4 November 1993, and the statement of the American Textile Manufacturers Institute before the Subcommittee on Trade, Committee on Ways and Means, of the United States House of Representatives, 5 November 1993. Both statements requested a longer MFA phasing-out period (15 years) and the opening of developing country markets to United States exports of textiles and clothing.

<sup>142</sup> The original language of Article 7:1 (i) of the Dunkel Draft states that members to the Agreement shall take action to "promote improved access to markets for textile and clothing products through such measures as tariff reductions and bindings, reduction or elimination of non-tariff barriers, and facilitation of customs, administrative and licensing formalities". Finally, at the insistence of the United States and the EC, it was agreed to amend the text by replacing the word "promote" by "achieve". See SUNS, No.3206, 16 December 1993, Third World Network, pp. 3-8.

<sup>143</sup> See the article on "GATT envoy's role: A lightning rod", in the *International Herald Tribune*, 14 April 1994, p. 9.

<sup>144</sup> See Xiaobing Tang, *op. cit.*, pp. 59-66, and Stewart, *op. cit.*, pp. 294-345.

<sup>145</sup> The International Textiles and Clothing Bureau (ITCB) has been established, since 1985, as an independent inter-governmental organization with the aim of strengthening the process of cooperation and coordination among developing countries in the field of textiles and clothing. The Bureau acts, *inter alia*, as a forum where members exchange views among themselves in order to evolve a common position in the textile negotiations. Its present members are: Argentina, Bangladesh, Brazil, China, Colombia, Costa Rica, Egypt, El Salvador, Hong Kong, India, Indonesia, Jamaica, Macau, Maldives, Mexico, Pakistan, Peru, Republic of Korea, Sri Lanka, Turkey, Uruguay and former Yugoslavia (provisional). For its proposals see GATT documents MTN.GNG/NG4/W/11 of 27 April 1988, MTN.GNG/NG4/W/20 of 28 September 1988, MTN.GNG/NG4/W/22 of 10 November 1988, MTN.GNG/NG4/W/23 of 8 June 1989, MTN.GNG/NG4/W/31 of 13 December 1989, MTN.GNG/NG4/W/44 of 13 March 1990 and MTN.GNG/NG4/W/49 of 5 June 1990.

<sup>146</sup> See GATT documents MTN.GNG/NG4/W/17 of 19 July 1988 and MTN.GNG/NG4/W/52 of 12 June 1990.

<sup>147</sup> See GATT document MTN.GNG/NG4/W/30 of 13 December 1989.



gration,<sup>148</sup> their proposals being based on the existing MFA restrictions as the starting-point for phase-out. Both the EC and the developing countries adopted a system of stages with intermediate steps with a view to arriving at integration at the end of the transition period. But the EC differed as regards the phase-out modality, proposing a liberalization target for each stage consisting of an agreed proposition for the volume of restraint levels. Within this target, each restraining country would be free to pick and choose quotas for removal, according to its convenience. However, this differed from the developing countries' approach of adopting a programmed elimination of restrictions in line with the degree of processing.

The United States proposed another approach which was to set up a global-type quota system to replace the MFA for a 10-year transition period starting on 1 January 1992. The global quota for each product would initially consist of allocations for countries already covered by bilateral agreements and, in addition, a non-selective "global basket". The "global basket" would increase annually according to multilaterally agreed growth rates while the initial country allocations would remain constant for the transition period.<sup>149</sup> Canada supported this approach, and proposed a special safeguard arrangement under which alternative restrictions could be imposed during the transition period. The special safeguard restrictions would eventually be phased out, giving way to improved GATT rules covering textiles and clothing, as in the case of other sectors.<sup>150</sup>

*Product coverage during the transition period:* Another aspect of the process of integration, related to the phase-out of restrictions, was product coverage of the transitional agreement. Developing countries represented by the ITCB based their proposal for integration into GATT on the existing restrictions, which were to be rolled over from 1 August 1991. This implied that the products under restrictions would be carried over into the transitional agreement and that the unrestricted MFA products remaining in each importing country would be automatically returned to GATT.

The EC introduced the new concept of a "textile universe", which meant that the transitional agreement would cover all the items falling under chapters 50 to 63 of the HS Code. In addition to the items covered by the MFA,

these chapters included textile raw materials comprising cotton, wool, vegetable fibres, man-made staple fibres and filament yarn. This would extend the product range beyond the MFA coverage, and could inflate the total volume of imports by the inclusion of unrestricted products in order to reduce the impact of the "integration ratio" on the dismantling of existing restrictions.

*Transitional safeguards:* Developing countries recognized that liberalization of textile restrictions could not proceed without the adoption of a safeguard system to be applied during the transition period. Some of these countries were of the opinion that, during that period, safeguard measures should be permitted solely in accordance with GATT provisions. Others realized that these views were unlikely to receive general acceptance in the negotiations and adopted a more pragmatic approach. The developed countries based their proposals for safeguard measures taken during the transition period on the concept of "market disruption".

With respect to the duration of the safeguard transitional measures, developed importing countries suggested three years without further extension. Developing countries proposed one year with a possible extension to a maximum of two years.

*Strengthened GATT rules and disciplines:* The negotiating mandate provided that the modalities for negotiations should permit the eventual integration of the textile sector into GATT on the basis of strengthened GATT rules and disciplines. The emphasis of the developing countries on strengthened GATT rules and disciplines was prompted by their concern that, following integration, the MFA restrictions would be replaced by actions taken under other GATT provisions such as safeguards, anti-dumping and countervailing duties. Consequently, they proposed a pause of two years between the phase-out of restrictions and the invocation of GATT Article XIX. They also proposed the prohibition of anti-dumping and countervailing measures during the transition period on products that were integrated into GATT.

These views were not shared by the developed countries, which did not address the possibilities of misuse of the GATT system but concentrated on improved access to markets. They envisaged undertakings by all participants in these areas of negotiation and called upon

<sup>148</sup> See GATT document MTN.GNG/NG4/W/47 of 14 May 1990.

<sup>149</sup> See GATT documents MTN.GNG/NG4/W/37 of 5 February 1990 and MTN.GNG/NG4/W/46 of 14 May 1990.

<sup>150</sup> See GATT documents MTN.GNG/NG4/W/21 of 28 September 1988 and MTN.GNG/NG4/W/42 of 5 March 1990.

the developing countries to undertake additional commitments over and above those established in the GATT instruments. In the developed countries' view, strengthened GATT rules and disciplines essentially meant the opening of the textile and clothing markets of developing countries, the tightening of anti-dumping and subsidy rules, and the protection of intellectual property rights.

The EC even introduced the concept of multilateral verification of the implementation of commitments undertaken for the progressive elimination of restrictions and application of strengthened GATT rules and disciplines. It proposed in this regard the establishment of a monitoring body during the transition period to assist the GATT Council in reviewing the implementation of the transitional agreement.

*Duration of the transition period:* Concerning the time-frame of the transition period, many developing countries continued to stand by their earlier proposal of six years and five months, while the major developed countries suggested that the time-frame should be 15 years. However, with the delay in the

conclusion of the Round, this question became less important.

*New entrants, small suppliers, and cotton-producing and least developed countries:* The MFA had prescribed special treatment for new entrants and small suppliers, as well as for cotton-producing countries. Although this was rarely put into practice, developing countries proposed to the NGTC the removal of restrictions on new entrants and small suppliers, as well as on least developed countries from the very beginning of the process of integrating textiles and clothing into GATT. They provided a quantitative definition of small suppliers, i.e. suppliers whose share was one per cent or less of the total imports in a given market. They further requested that the transitional safeguard measures should not be applied to new entrants, small suppliers and the least developed countries. In addition, they proposed an enhancement factor for the cotton-producing countries in the application of progressive increases in growth rates. However, most of these proposals did not meet with a favourable response from developed importing countries.

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## C. The main elements of the Agreement

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The text of the Agreement on Textiles and Clothing, which is part of the Final Act signed at the Marrakesh Ministerial Meeting of 12-15 April 1994, consists of a preamble, nine articles and an annex. The Agreement, in general, adheres to the mandate of Punta del Este and the decision of the Mid-Term Review, and provides for the progressive phasing out of all MFA restrictions and other measures (unless they are justified under GATT rules), and the integration of this sector into GATT 1994 in four stages over a transition period of 10 years from the date of entry into force of the WTO Agreement. By the end of this transition period, with the full integration of the sector into GATT 1994, all restrictions will be terminated, and there will be no extension of the Agreement on Textiles and Clothing (Article 9).

### 1. Coverage of the Agreement

#### (a) Product coverage

This Agreement will govern the integration of textiles and clothing products into

GATT 1994 over the next 10-year period. As provided for in Article 1:7, the textile and clothing products to which this Agreement applies are set out in the Annex which contains approximately 800 HS tariff lines at six-digit level. The Annex consists of: (1) products within Section XI of the HS Code (textiles and textile articles except the lines of raw silk, raw wool and raw cotton); and (2) other products from certain other chapters of the HS Code which are currently included in the category systems of some of the MFA-restraining countries.

However, in the application of the transitional safeguards under Article 6 of the Agreement, paragraph 2 of the Annex states that actions should be imposed on particular products rather than on the basis of the HS lines *per se*. Paragraph 3 of the Annex further stipulates that no transitional safeguard actions should be imposed on certain handloom products, historically traded textile products such as jute bags and pure silk products, to which the provisions of Article XIX of GATT 1994, as interpreted by the Agreement on Safeguards, will apply.

**(b) Country coverage**

Since the Agreement is an integral part of the Final Act of the Uruguay Round, it will be applicable to all members to the WTO Agreement (including both MFA and non-MFA signatories). Thus, the membership of this Agreement will be more than 120 (assuming all GATT contracting parties will ratify the WTO Agreement) while the MFA has just over 40 signatories. Furthermore, this Agreement differs from the MFA in that the latter also governs the restrictions that are applied by GATT contracting parties against certain non-contracting parties, as MFA membership is open to both GATT contracting parties and non-contracting parties.<sup>151</sup>

**(c) Measures covered by the Agreement**

The provisions of this Agreement will be applicable to:

- all MFA restrictions maintained between GATT 1947 contracting parties and in place on the day before the entry into force of the WTO Agreement (Article 2:1);
- restrictions on textiles and clothing products maintained by the members (other than those under the MFA) or not justified under the provisions of GATT 1994 (Article 3); and
- actions taken by any members under the transitional safeguard mechanism to products covered by the Annex except those integrated into GATT 1994 under the integration programme (Article 6:1), or those already under restraint.

In this regard, the Agreement is unlike the MFA, which only applies to restrictions imposed by some developed countries on imports of textiles and clothing from certain developing country exporters.

Thus, as mentioned above, the major difference between the MFA and this Agreement is that this Agreement is applicable to all WTO members and all their trade in textiles and clothing will be subject to its provisions while the MFA is only applicable to those importing and exporting countries that choose to join it.

**2. Integration programme****(a) MFA restrictions**

Article 2:1 provides that all restrictions within bilateral agreements maintained between GATT 1947 contracting parties under the MFA and in place on the day before the entry into force of the WTO Agreement shall be notified in detail, including the restraint levels, growth rates and flexibility provisions, by the members maintaining such restrictions, to the newly established Textiles Monitoring Body (TMB) within 60 days following the entry into force of the WTO Agreement or shall otherwise be terminated forthwith.

Article 2:4 further provides that notified restrictions will be deemed to constitute the "totality" of such restrictions applied by the respective members on the day before the entry into force of the WTO Agreement. No new restrictions in terms of products or members will be introduced except under the provisions of this Agreement or relevant GATT 1994 provisions. However, the relevant GATT 1994 provisions will not include Article XIX in respect of products not yet integrated into GATT 1994, except the products as specifically provided for in paragraph 3 of the Annex.

*Stages of integration:* Products covered in the Annex of the Agreement, including those subject to MFA restrictions, will be integrated into GATT 1994 in four stages. The extent of integration at each stage is to be expressed as a percentage of the total volume of imports in 1990 of the products covered by the Annex. At each stage, the products to be integrated will encompass products from each of the following four groups: tops and yarns, fabrics, made-up textiles, and clothing. The four stages are defined as follows:

- Stage One - on the date of entry into force of the WTO Agreement, (assumed to be 1 January 1995), members shall integrate into GATT 1994 products which account for not less than 16 per cent of the total volume of 1990 imports of the products in the Annex, in terms of HS lines or categories.
- Stage Two - on the first day of the 37th month that the WTO Agreement is in effect (assumed to be 1 January 1998), pro-

<sup>151</sup> Under the Agreement on Textiles and Clothing, MFA restrictions applied by GATT contracting parties to non-contracting parties are not covered, such as those applied under bilateral agreements with China.

ducts which account for not less than a further 17 per cent of the total volume of the member's 1990 imports of the products in the Annex.

- Stage Three - on the first day of the 85th month that the WTO Agreement is in effect (assumed to be 1 January 2002), products which account for not less than a further 18 per cent of the total volume of the member's 1990 imports of the products in the Annex.
- Stage Four - on the first day of the 121st month that the WTO Agreement is in effect (assumed to be 1 January 2005), the textiles and clothing sector shall stand integrated into GATT 1994, all restrictions under this Agreement having been eliminated.

However, the integration ratios mentioned above are the minimum. Nothing in the Agreement shall prevent members from completing the integration programme at an earlier date or integrating products into GATT 1994 at rates higher than those provided for in the above-mentioned programme.

*Notification requirements for the respective stages of integration:* Article 2:7(a) requires that the members maintaining MFA restrictions (see table 7) shall integrate, in the first stage, 16 per cent of the total volume of their 1990 imports into GATT 1994, and shall notify the GATT Secretariat of the full details of the actions to be taken by them for such integration not later than 1 October 1994 as agreed by Ministers on 15 April 1994.

Members which were signatories to the MFA but have not maintained any MFA restrictions as of 31 December 1994, and wish to retain their rights to use the transitional safeguard, are required by Article 2:7(b) to notify the details of their actions under the integration programme to the TMB not later than 60 days following the date of entry into force of the WTO Agreement. Members which were not MFA signatories, but wish to retain the right to use the transitional safeguard, shall notify the details of their actions under the integration programme to the TMB not later than at the end of the 12th month that the WTO Agreement is in effect.

For the remaining stages, details of the actions under the integration programme, as required by Article 2:11, shall be notified to the TMB at least 12 months before their entry into effect.

*Growth rates and other flexibilities:* At each of the first three stages of the integration programme, an annual increase of the established growth rate (i.e. the growth rate from the former MFA restraints carried over into this Agreement) for the remaining restrictions is provided for as follows:

- for Stage One (from 1 January 1995 to 31 December 1997, inclusive) the level of each restriction under MFA bilateral agreements in force for the 12-month period prior to the date of entry into force of the WTO Agreement shall be increased annually by not less than the growth rate established for the respective restrictions, increased by 16 per cent;
- for Stage Two (from 1 January 1998 to 31 December 2001, inclusive), the growth rate for the respective restrictions during Stage One, increased by 25 per cent; and
- for Stage Three (from 1 January 2002 to 31 December 2004, inclusive), the growth rate for the respective restrictions during Stage Two, increased by 27 per cent (see tables 8 and 9).

However, nothing in the Agreement shall prevent a member from eliminating any restriction maintained under the MFA, effective at the beginning of any agreement year during the transition period, provided the exporting member concerned and the TMB are notified at least three months before the elimination comes into effect (Article 2:15).

Article 2:16 also provides for flexibility provisions (swing, carryover and carry forward) to be the same as those provided for in MFA bilateral agreements for the 12-month period prior to the entry into force of the WTO Agreement. No quantitative limits shall be placed or maintained on the combined use of swing, carryover and carry forward.

#### (b) *Other restrictions*

While quantitative restrictions maintained by the members under the MFA will be phased out over a 10-year transition period as referred to above, the Agreement also deals with other non-MFA quantitative restrictions on textiles and clothing products, including all unilateral restrictions, bilateral arrangements and other measures having a similar effect.<sup>152</sup>

<sup>152</sup> In general, non-MFA restrictions could be grouped into three categories as follows: (a) restrictions imposed, falling outside the MFA, by some developed countries, such as Japan and Switzerland, which are signatories to the MFA.

Table 8

**SPECIFIC LIMITS AND ANNUAL GROWTH RATES CONTAINED IN THE MFA  
BILATERAL AGREEMENTS OF MAJOR IMPORTING COUNTRIES, 1993**

Suppliers	Restricting importers					
	United States		European Communities		Canada	
	Specific limits (Number)	Growth rate (Per cent)	Specific limits (Number)	Growth rate (Per cent)	Specific limits (Number)	Growth rate (Per cent)
Argentina			3	4.3		
Bangladesh	20	7.0			8	7.0
Brazil	..	..	10	2.8	4	6.7
China	84	3.3	33	3.7	..	..
Colombia	2	6.0				
Costa Rica		5.9				
Czech Republic	..	..	23 <sup>a</sup>	4.4 <sup>a</sup>	4	5.0
Dominican Republic	8	..			1	6.0
El Salvador	..	..				
Egypt	4	6.3				
Guatemala	3	5.9				
Hong Kong	61	1.3	28	1.3	20	2.9
Hungary	8	5.6	17	4.8	1	4.0
India	18	5.9	15	2.8	..	..
Indonesia	34	6.0	8	4.8	11	6.0
Jamaica	..	..				
Macau	15	6.2	20	1.7	7	6.0
Malaysia	..	..	8	4.1	10	5.3
Mexico	12	5.4				
Pakistan	26	6.3	13	4.1	12	6.2
Panama	1	6.0				
Peru	..	..	2	5.7		
Philippines	39	4.8	12	5.3	11	6.5
Poland	9	5.1	17	4.7	10	5.0
Republic of Korea	66	1.2	44	2.9	..	..
Romania	18	4.6	28	4.6	15	5.1
Singapore	24	3.0	7	3.9	13	5.0
Slovak Republic	..	..			4	4.3
Sri Lanka	..	..	4	7.3	..	..
Thailand	37	5.7	16	4.4	16	4.9
Turkey	17	5.8			4	6.0
Uruguay	7	3.3			1	6.0

Source: Estimates by ITCB.

<sup>a</sup> Including also the Slovak Republic.

Under the provisions of Article 3, members are committed to notify in detail all their restrictions on textiles and clothing products (other than those maintained under the MFA),

whether consistent with GATT 1994 or not, to the TMB within 60 days following the date of entry into force of the WTO Agreement. Such notifications should also include information

For example, Japan's import restrictions on silk yarn against China and the Republic of Korea, and on cotton yarn against Pakistan (see GATT, *Trade Policy Review Report - Japan 1990*, pp. 241-242, and GATT document "Textiles and clothing in the world economy" (C/W/440 Spec(84) p. 108)); and the price surveillance system instituted by Switzerland on imports of textiles and clothing products (see GATT, *Trade Policy Review - Switzerland 1991*, p. 165)); (b) restrictions imposed by MFA signatories against non-MFA signatories. For example, the EC has applied restrictive measures against Morocco, Tunisia, Turkey, Malta, Japan, some Latin American countries and some countries in transition (see GATT, *Trade Policy Review - European Communities 1993*, pp. 73-75). The United States has applied restrictive measures against Bahrain, Mauritius, Haiti, Lesotho, etc. (see GATT, *Trade Policy Review - United States 1994*, p. 70); and (c) measures maintained by other countries, including developing countries, both MFA and non-MFA signatories, except those justified under the provisions of GATT 1994.

with respect to whether or not the restrictions are justified under GATT 1994 provisions. Any member may also make reverse notifications in this regard or concerning any restrictions that may not have been notified under the provisions of this Article.

All GATT-inconsistent, non-MFA restrictions shall be either: (1) brought into conformity with GATT 1994 within one year following the entry into force of the WTO Agreement; or (2) phased out progressively according to a programme, to be presented to the TMB within a period not exceeding the duration of this Agreement.

### 3. Transitional safeguards

Although Articles 2 and 3 require all members to phase out progressively both MFA and non-MFA quantitative restrictions (other than those justified under the provisions of GATT 1994) maintained by them over the 10-year transition period, Article 6 continues to permit the application of MFA-type selective safeguard actions during the transition period under the so-called "transitional safeguard".

Transitional safeguards can be applied to products covered by the Annex, except those integrated into GATT 1994 under the integration programme and those already under restraint. The application of such safeguards is available to all members. Members which are signatories to the MFA but do not maintain MFA restrictions may retain the right to use the transitional safeguards on condition that they notify the TMB of their intention within 60 days following the date of entry into force of the WTO Agreement. Members which were not signatories to the MFA since 1986 must make such a notification within six months following the entry into force of the WTO Agreement.

For the invocation of the transitional safeguards, Article 6 sets out the following procedures:

- (a) Before imposing the actions, the proposing member shall seek consultations with the affected member(s). The request for consultations shall be accompanied by up-to-date specific and relevant factual information, including: (i) the extent to which total imports of a product involve serious damage or the threat thereof; and (ii) identification of the member(s) to which serious damage, or the actual threat thereof, is attributed (based on a sharp and substantial increase in imports from a particular source, or selectivity). Furthermore, the information shall be closely related to identifiable segments of production and to the actual level of exports or imports during the 12-month period terminating two months preceding the month in which the request for consultation was made (paragraph 8).
- (b) To impose the action, the invoking member shall also propose the specific level at which imports from (a) particular member(s) will be restrained provided the level is not lower than in the above-mentioned 12-month period.
- (c) In seeking consultation, the invoking member shall communicate the necessary request to the member(s) concerned and to the TMB Chairman, accompanied by the relevant factual data and the proposed restraint level referred to in sub-paragraphs (a) and (b) above.
- (d) The member(s) in receipt of the request shall respond to it promptly with a view to the completion of the consultation within 60 days after the request was received.
- (e) If, in the consultations, there is mutual understanding that the situation calls for restraint on the exports of the particular product from the member(s) concerned, the restraint level shall be fixed not lower than the actual level of exports or imports from the member(s) concerned during the 12-month period terminating two months preceding the month in which the request for consultation was made.
- (f) Details of the agreed restraint measure shall be reported to the TMB within 60 days from the date of conclusion of the agreement. The TMB shall review all necessary information and determine whether the agreement is justified in accordance with the provisions of Article 6. In the light of its review, the TMB may make such recommendations as it deems appropriate to the member(s) concerned.

However, if no agreement can be reached within 60 days from the date on which the request for consultations was received, the invoking member may apply the restraint by date of import or date of export, in accordance with the provisions of Article 6, within 30 days following the 60-day period for consultations, and at the same time refer the matter to the TMB. Either member may refer the matter to the TMB before the expiry of the period of 60 days. In either case, the TMB shall review the case promptly, including the determination of serious damage, or actual threat thereof, and its

Table 9

## ILLUSTRATIVE INCREASES IN GROWTH RATES PROVIDED FOR IN THE AGREEMENT ON TEXTILES AND CLOTHING

(Percentages)

Increases envisaged in the Agreement										
Stage of integration	Year	Growth factor Per cent <i>a</i> (1)	Original growth rate 1 per cent <i>a</i> (2)	Increase in quota <i>b</i> (3)	Original growth rate 3 per cent <i>a</i> (4)	Increase in quota <i>b</i> (5)	Original growth rate 5 per cent <i>a</i> (6)	Increase in quota <i>b</i> (7)	Original growth rate 6 per cent <i>a</i> (8)	Increase in quota <i>b</i> (9)
<b>A. In accordance with paragraphs 13 and 14 of Article 2</b>										
I	1	16	1.16	101.16	3.48	103.48	5.80	105.80	6.96	107.00
	2		1.16	102.33	3.48	107.08	5.80	112.99	6.96	114.40
	3		1.16	103.52	3.48	110.81	5.80	119.54	6.96	122.40
II	4	25	1.45	105.02	4.35	115.63	7.25	128.21	8.70	133.00
	5		1.45	106.54	4.35	120.52	7.25	137.50	8.70	144.57
	6		1.45	108.08	4.35	125.76	7.25	147.47	8.70	157.15
	7		1.45	109.65	4.35	131.23	7.25	158.16	8.70	170.82
III	8	27	1.84	111.67	5.52	138.47	9.21	172.70	11.05	189.70
	9		1.84	113.72	5.52	146.11	9.21	188.61	11.05	210.66
	10		1.84	115.81	5.52	154.18	9.21	205.98	11.05	233.94
<b>B. In accordance with paragraph 18 of Article 2.</b>										
I	1	25	1.25	101.25	3.75	103.75	6.25	106.25	7.50	107.50
	2		1.25	102.52	3.75	107.64	6.25	112.89	7.50	115.56
	3		1.25	103.80	3.75	111.67	6.25	119.95	7.50	124.23
II	4	27	1.59	105.45	4.69	116.91	7.94	129.47	9.53	136.07
	5		1.59	107.13	4.69	122.39	7.94	139.75	9.53	149.04
	6		1.59	108.83	4.69	128.13	7.94	150.85	9.53	163.24
	7		1.59	110.56	4.69	136.97	7.94	162.83	9.53	178.80
III	8	27	2.02	112.79	5.96	145.13	10.08	179.24	12.10	200.43
	9		2.02	115.07	5.96	153.78	10.08	197.31	12.10	224.68
	10		2.02	117.39	5.96	162.95	10.08	217.20	12.10	251.87

Source: Calculations by the UNCTAD secretariat based on data in GATT document COM.TEX/SB/1799/Add.1, and ITCB data base.

*a* The rate foreseen in the bilateral agreement under the MFA.

*b* Obtained by applying to the original bilateral growth rate the additional increase (growth factor) provided for in the Agreement on Textiles and Clothing (see column (1)).

causes, and make appropriate recommendations to the members concerned within 30 days.

In special circumstances (such as under the normal safeguard mechanism), in which delay would cause damage that would be difficult to repair, provisional action may be taken under paragraph 10 provided that the request for consultations and notification to the TMB is effected within no more than five working days after taking the action. If no agreement is reached as a result of the consultations, the TMB is to be notified within 60 days from the date of the implementation of the action. It shall promptly examine the matter and make appropriate recommendations to the members concerned within 30 days. If agreement is reached, the TMB shall be notified within 90 days from the date of the implementation of the action, and make such recommendations as it deems appropriate to the member(s) concerned.

With respect to the duration of transitional safeguard actions, Article 6:12 stipulates that no such measure shall be extended after three years of its invocation.

When a transitional safeguard action remains in force for a period exceeding one year, Article 6:13 requires growth rates and other flexible possibilities (swing, carryover, carry forward) to be established along the same lines as these contained in Annex B of the MFA.

If a transitional safeguard action is applied to a product for which a restraint was previously in place under the MFA during the 12-month period prior to the entry into force of the WTO Agreement, or pursuant to the provisions of this Agreement (Articles 2 or 6), the level of the new restraint shall be the level of exports or imports from the member(s) concerned during the 12-month period terminating two months preceding the month in which the request for consultations was made (as provided for in Article 6:8), unless the new restraint comes into force within one year of: (a) the date of notification for the elimination of the previous restraint (as referred to in Article 2:15); or (b) the date of removal of the previous restraint put in place pursuant to the provisions of this Article or of the MFA. In the case of (b), the level shall not be less than the higher of (i) the level of restraint for the last 12-month period during which the product was under restraint, or (ii) the level of restraint provided for in Article 6:8.

When a member not maintaining any MFA restrictions under Article 2 decides to impose a transitional safeguard action, it shall

make appropriate arrangements based on normal commercial practices and avoid over-categorization.

#### 4. Relationship with the Agreement on Safeguards

Before any integration takes place, all the products covered in the Annex will be subject to the provisions of the Agreement on Textiles and Clothing. However, once products are integrated into GATT 1994, only the provisions of GATT Article XIX and the Agreement on Safeguards will be applicable to them.

In the event that a GATT Article XIX safeguard measure is initiated by a member against a product during a period of one year immediately following the integration of that product into GATT 1994 under the integration programme of this Agreement, the provisions of Article XIX, as interpreted by the Agreement on Safeguards, shall apply on condition that:

- the importing member concerned shall apply the measure (other than in the form of a tariff) in such a manner that the applicable level shall not be lower than the average level of exports from the member concerned in the last three representative years (as set forth in Article XIII:2(d) of GATT); and
- the exporting member concerned shall administer such a measure.

When a GATT Article XIX safeguard measure is imposed for more than one year, the applicable level shall be progressively liberalized at regular intervals during the period of application. In such cases the exporting member concerned may not exercise the right of suspension of obligation or withdrawal of concession (as provided for in Article XIX:3(a) of GATT).<sup>153</sup>

#### 5. Quota administration

As in the MFA, all the restrictions maintained under this Agreement, including those applied in accordance with the transitional safeguards provisions, are required by Article 4 of the Agreement to be administered by the exporting members. Importing members shall

<sup>153</sup> GATT Article XIX as interpreted by the Agreement on Safeguards.



not be obliged to accept shipments in excess of the levels of restriction.

Any changes with respect to the restraint level, practices, rules, procedures and product categorization in the implementation or administration of the restrictions under this Agreement may not upset the balance of rights and obligations between the members concerned under the Agreement.

When such changes are necessary, the member initiating them shall inform and initiate consultations with the affected member(s) prior to the implementation of such changes, with a view to reaching a mutually acceptable solution regarding appropriate and equitable adjustment. If such consultation prior to implementation is not feasible, the member initiating the said changes will, at the request of the affected member(s), consult, within 60 days if possible, with the member(s) concerned with a view to reaching a mutually satisfactory solution regarding appropriate and equitable adjustments. If a mutually satisfactory solution is not reached, any member involved may refer the matter to the TMB for its recommendations as provided in Article 8. Should the TSB not have had the opportunity to review a dispute concerning such changes introduced prior to the entry into force of the WTO Agreement, the matter under dispute will be reviewed by the TMB in accordance with the rules and procedures of the MFA applicable to such a review.

## 6. Circumvention

The problem of circumvention has attracted considerable attention in recent years. In order to tackle the problem, Article 5 of the Agreement requires members to "establish the necessary legal provisions and/or administrative procedures to address and take action against such circumvention", and to cooperate fully in this regard consistent with their domestic laws and procedures. It also contains detailed provisions with respect to appeal, consultation, cooperation among members in investigating circumvention practices, and the role of the TMB.

When allegations of circumvention are made, the members concerned are required to consult immediately. They should cooperate fully in the investigation of the alleged practice in order to establish the facts, by the exchange of documents and information, and by plant visits and contacts.

When the fact of circumvention has been established after investigation, the entry of the circumvented goods into the importing country may be denied. If the goods have already entered, they may be debited to the quota of the true country of origin. If circumvention has occurred through a country of transit, action may also be taken against such a country by applying a restriction on it.

False declarations are penal offences. When such offences have been committed members should take action against the exporters or importers under their domestic laws.

The procedures under Article 5 require the members concerned to consult with one another. The actions taken should be reported to the TMB. If there is any disagreement between the parties, the matter should be referred to the TMB which will review the situation and make recommendations.

## 7. Additional obligations

Although the results of the Uruguay Round constitute a single undertaking, the Agreement on Textiles and Clothing forms an integral part of the Final Act, the acceptance of which is required to implement it in its entirety. Article 7 of the Agreement establishes the linkage between the integration process and the fulfilment of certain commitments under other Uruguay Round agreements, whereby the members are required to:

- achieve improved market access for textiles and clothing products by tariff reductions and bindings, or through liberalization of other non-tariff measures;
- strengthen the rules and disciplines with respect to anti-dumping practices, subsidies and countervailing measures, and protection of intellectual property rights; and
- avoid discrimination against textiles and clothing imports when taking measures for general trade policy reasons.

In this regard, members are obliged to make notifications and reverse notifications to the TMB.

In the event of a dispute deriving from the imbalance between the integration process and the above-mentioned actions, members may bring it before the relevant WTO bodies and so inform the TMB. Any subsequent

findings or conclusions by the WTO bodies concerned shall form part of a comprehensive report to be made by the TMB.

## 8. *Special treatment for certain categories of members*

Special treatment for certain categories of members is provided for in Articles 1, 2 and 6. While the special treatment provisions contained in Article 1 are of a best endeavour nature (such as paragraph 3 for non-MFA members), the categories concerned are provided in Article 2 with a specific threshold and in Article 6 particular elements are emphasized.

### (a) *Under the integration programme*

Article 2:18 provides a quantified definition of small suppliers (see tables 9 and 10). Under such definition, those members whose exports subject to restrictions represent 1.2 per cent or less of the total volume of the restrictions applied by an importing member as of 31 December 1991 will be granted meaningful improvement in access for their exports during the duration of this Agreement, through:

- advancement by one stage of the growth rates set out in Article 2, paragraphs 13 and 14 (their growth rates will be increased at the beginning of each stage by 25, 27 and 27 per cent respectively instead of 16, 25 and 27 per cent); or
- at least equivalent changes, as may be mutually agreed, with respect to a different mix of base levels, growth and flexibility provisions.

### (b) *Under the transitional safeguard mechanism*

In the application of the transitional safeguard mechanism, Article 6:6 requires the interests of the following exporting members to be taken into account:

- least-developed country members shall be accorded significantly more favourable treatment than that provided to the other members, preferably in all its elements but, at least, on overall terms;

- small suppliers shall be accorded differential and more favourable treatment in terms of restraint level, growth and other flexibility provisions (as provided in Article 6, paragraphs 8, 13 and 14). Due account will also be taken (pursuant to paragraphs 2 and 3 of Article 1) of the possibilities for the development of their trade and the need to allow commercial quantities of imports from them;
- wool-producing developing country members, in view of their dependence on the wool sector and the fact that their exports consist almost exclusively of wool products, shall be given special consideration as regards their export needs when quota levels, growth rates and flexibility are being considered; and
- more favourable treatment shall be accorded to the outward processing trade.

## 9. *Textiles Monitoring Body (TMB)*

In order to supervise the implementation of this Agreement, a Textiles Monitoring Body (TMB) will be established as a standing body within the framework of the WTO, reporting directly to the Council for Trade in Goods. While the TMB will be similar to the Textiles Surveillance Body (TSB) of the MFA in many areas, the main differences between the two bodies will be in their functions and membership. Owing to the dismantling of the bilateral agreements under the MFA upon the entry into force of the WTO Agreement, the role of the TMB will focus on resolving disputes deriving from the implementation of the Agreement and reviewing product-specific restrictions imposed under the transitional safeguards. The TMB will consist of a Chairman and 10 members chosen from among the WTO members on an ad personam basis, and will thus have a much broader representation than the TSB. It is understood that consensus within the TMB does not require the assent or concurrence of the TMB members appointed by members of the WTO involved in an unresolved issue under review by the TMB.

The main functions of the TMB, as required under this Agreement, are the following:

- to examine all measures taken under this Agreement and their conformity;
- to take the actions specifically required of it by this Agreement;

Table 10

SMALL SUPPLIERS OF TEXTILES AND CLOTHING <sup>a</sup>

Importer	Canada	European Communities	Finland	United States <sup>b</sup>
Supplier	Colombia	Peru	Sri Lanka	Argentina
	Macau	Sri Lanka		Costa Rica
	Uruguay			Jamaica
				Macau
				Peru
				Uruguay
				Yugoslavia

**Source:** ITCB estimates, based on specific limits in the bilateral agreements under the MFA.

**a** Suppliers whose restrictions represent 1.2 per cent or less of the total volume of the restrictions applied by an importing member as of 31 December 1991 (see Article 2:18 of the Agreement on Textiles and Clothing).

**b** Allows for group limits in the bilateral agreement.

- to rely on notifications and information supplied by the members under the relevant Articles of this Agreement, supplemented by any additional information or necessary details they may submit or it may decide to seek from them. It may also rely on notifications to and reports from other WTO bodies and from such other sources as it may deem appropriate;
- to ensure that members shall afford each other adequate opportunity for consultations with respect to any matters affecting the operation of this Agreement;
- to make recommendations to the members concerned, in the absence of a mutually agreed solution, in the bilateral consultations provided for in this Agreement;
- to review promptly, at the request of any member, any particular matter which that member considers to be detrimental to its interests under this Agreement, on which consultations between the TMB and the member(s) concerned have failed to produce a mutually satisfactory solution. On such matters, the TMB may make such observations as it deems appropriate to the member(s) concerned and for the purposes of the major review (provided for in Article 8:11);
- to invite the participation of the members which may be directly affected by the matter in question before formulating its recommendations or observations;
- to make recommendations or findings, whenever called upon to do so, preferably within a period of 30 days unless a different time-period is specified in this Agreement. All such recommendations or findings shall be communicated to the members directly concerned. All such recommendations or findings shall also be communicated to the Council for Trade in Goods for its information;
- to exercise proper surveillance of the implementation of its recommendations while members shall endeavour to accept them in full; and
- to assist the Council for Trade in Goods to conduct a major review before the end of each stage of the integration process. In doing so, it shall, at least five months before the end of each stage, transmit to the Council for Trade in Goods a comprehensive report on the implementation of this Agreement during the stage under review, in particular in matters with regard to the integration process, the application of the transitional safeguard mechanism, and the application of GATT 1994 rules and disciplines (as defined in Articles 2, 3, 6 and 7 respectively). Its comprehensive report may include any recommendation it deems appropriate to the Council for Trade in Goods.

## 10. Relationship with the Dispute Settlement Body and the Council for Trade in Goods

### (a) Dispute Settlement Body

If a dispute remains unresolved by the TMB, either member, as provided for in Article 8:10, may bring the matter before the Dispute Settlement Body, invoking Article XXIII:2 of GATT<sup>154</sup> and the relevant provisions of the Dispute Settlement Understanding.

In order to resolve any disputes that may arise with respect to the imbalance between the integration process and the obligations referred to in Article 7, the Dispute Settlement Body may authorize, without prejudice to the final date of termination of this Agreement and all

restrictions thereunder, an adjustment to the integrating ratios (as provided for in Article 2:14), for the stage subsequent to the review with respect to any member found not to be complying with its obligations under this Agreement.

### (b) Council for Trade in Goods

In order to oversee the implementation of this Agreement, Article 8:11 stipulates that the Council for Trade in Goods shall conduct a major review before the end of each stage of the integration process.

In the light of its review the Council for Trade in Goods shall by consensus take such decisions as it deems appropriate to ensure that the balance of rights and obligations embodied in this Agreement is not being impaired (Article 8:12).

## D. Implications

The inclusion of a transitional agreement on textiles and clothing in the final results of the Uruguay Round represents an essential step towards achieving trade liberalization in this sector of vital interest to developing countries. As a delicate compromise between the interests of developing exporting countries and developed importing countries, the Agreement provides for trade in textiles and clothing to be gradually subjected to GATT rules and disciplines within a 10-year transition period and for the MFA restrictions to be phased out through a four-stage integration process. Over the transition period, the existing annual growth rates for the respective restrictions under the bilateral agreements will also be increased. The increases in the growth rates can be considered as an important improvement compared to the MFA. In particular, they could mean significant quota increases for countries that currently enjoy relatively higher growth rates, generally medium-sized and small exporters. However, for products where the growth rates are low, the increases (which are calculated as a percentage of a product) will be of minimal significance (see table 9). Small suppliers will

also enjoy specific improvements in access (e.g. in respect of base levels, growth and flexibility provisions) when products exported by them and subject to restrictions represent 1.2 per cent or less of the total volume of the restrictions applied by an importing member (see table 10). The Agreement also includes special provisions for least developed countries, non-MFA members, cotton producers, wool producers and the outward processing trade, but without any specific threshold. With respect to the Uruguay Round tariff concessions for textiles and clothing in selected countries see chart 3 and table 11.

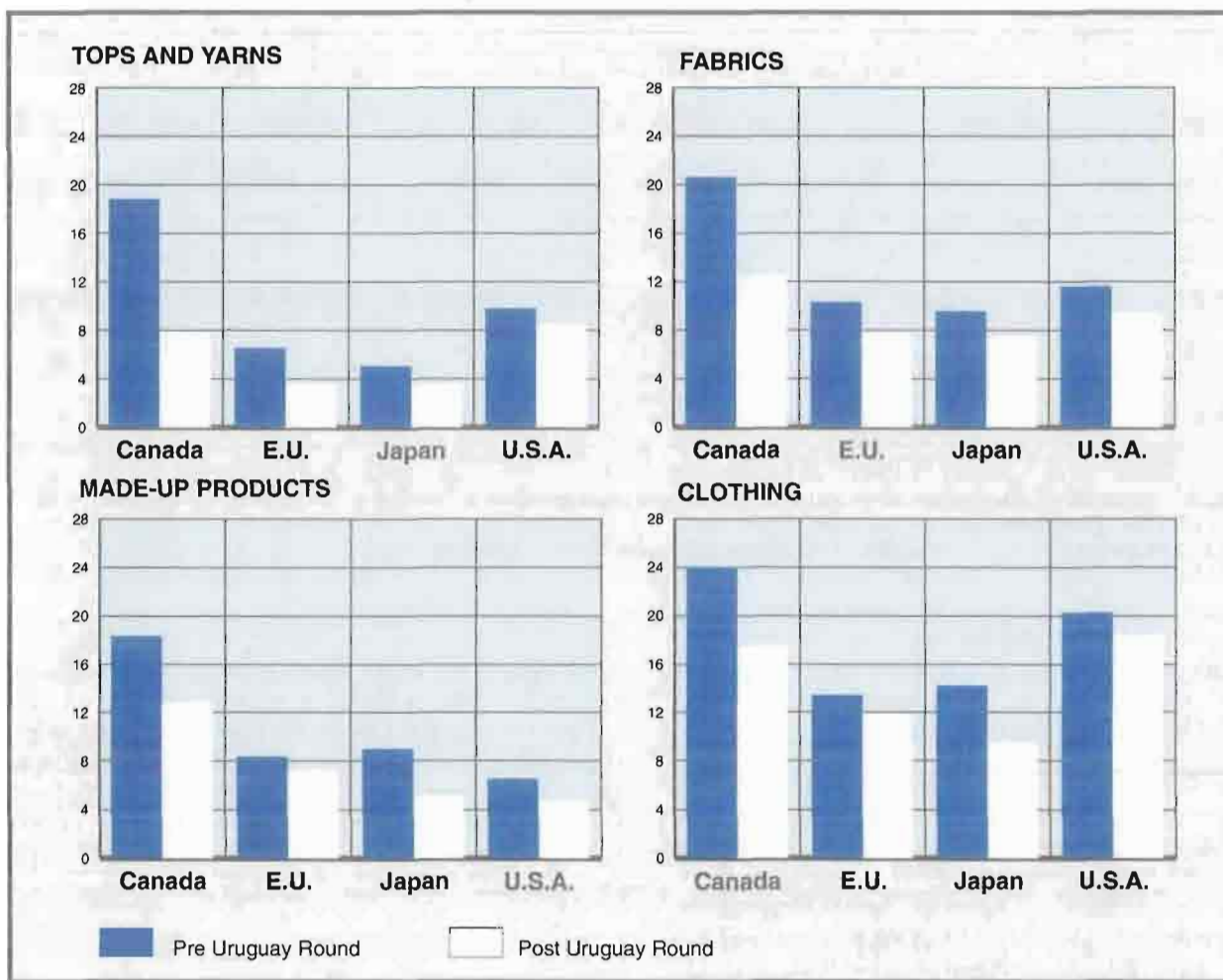
Apart from the economic package, the Agreement has successfully managed to discard some of the disturbing features of the MFA, for example: (i) the elimination of the provision of "exceptional circumstances", which enables importing countries to escape from the obligations of Annex B of the MFA; (ii) the abolition of the concept of "minimum viable production", through which the small importing countries are able to evade their obligations and transfer the burden of import adjustment

<sup>154</sup> As interpreted by the Understanding on Dispute Settlement of the Final Act.

Chart 3

URUGUAY ROUND TARIFF CONCESSIONS IN 'QUAD' COUNTRIES

(Percentages)



Source: Calculations by the UNCTAD secretariat, based on data in its Trade Control Measures Information System.

from dominant to less significant suppliers; and (iii) the deletion of the so-called "mutually acceptable terms", which serve as a vehicle for developed importing countries to deviate from their obligations under the MFA in negotiating bilateral textile agreements with developing exporting countries. The Agreement has succeeded in abolishing the system of bilateral agreements based on the concept of avoiding "real risks" of market disruption.

The most important feature of the Agreement, however, is the commitment, set out in Article 9, that it is not renewable. Thus, the discriminatory MFA regime, which has been the most notorious characteristic of the

textile trade for three decades, will be brought to an end at the expiry of the transition period.

On the other hand, since each importing member will select the products to be integrated into GATT unilaterally, it is difficult to foresee which of the MFA restrictions will be phased out in the early stages, although it can be expected that the most sensitive products, in which growth rates are lowest and quota levels consistently filled, will be left to the final stage. As the Annex to the Agreement incorporates a number of tariff lines not at present specifically restricted under the MFA, the importing countries can use this inflated volume to avoid integrating currently restricted product areas at the earlier stages. Many developing exporting

Table 11

**PRE- AND POST-URUGUAY ROUND TARIFFS FOR TEXTILES AND CLOTHING  
IN SELECTED COUNTRIES**

(Percentages)

	<i>Pre-UR tariff</i>	<i>Post-UR tariff</i>	<i>Reduction</i>	<i>Pre-UR<sup>a</sup> bound</i>	<i>Post-UR<sup>a</sup> bound</i>
United States	19.6	17.5	10.9	98.9	98.9
EC	9.9	8.3	16.5	100.0	100.0
Japan	10.4	6.8	34.3	100.0	100.0
Republic of Korea	28.1	19.9	29.0	1.4	87.1
Brazil	78.5	36.7	53.2	0.3	100.0

**Source:** Information supplied by the Office of the United States Trade Representative, Washington, D.C.

**Note:** These data reflect a preliminary analysis of information received from the GATT Secretariat as of 1 May 1994, based on GATT Schedules.

<sup>a</sup> Proportion of trade in textiles and clothing for which tariffs are bound.

countries therefore do not expect to benefit from meaningful trade liberalization in this sector in the immediate future.

Moreover, while the existing MFA restrictions are being gradually phased out, new quantitative restrictions can be imposed by the importing countries, under the so-called "specific transitional safeguard" provisions of the Agreement during the 10-year transitional period, to products covered by the Annex to the Agreement (other than handloom products, historically traded textile products and pure silk products). Measures applied under the transitional safeguard provisions can, like the MFA, continue to be selective "on a member-by-member basis". The criteria and procedures for such actions have retained most of the elements of the so-called "market disruption" provisions of Annex A and Article 3 of the MFA. In addition, the MFA-type quantitative restrictions can now be applied to non-MFA signatories as well under the transitional safeguard provisions of the Agreement.

Owing to the fact that all the MFA and non-MFA restrictions maintained by the members will be notified to the Textiles Monitoring Body only after the entry into force of the WTO Agreement, and the products to be integrated into GATT 1994 at the first stage will only be known on 1 October 1994, it is difficult to assess at the moment how developing countries will benefit from this transitional Agreement, particularly in terms of the economic

package. Although such an assessment cannot be made until information is available on the scope of the current restrictions and the products that will be integrated in the first stage, the following paragraphs propose to highlight some of the concerns of the developing countries regarding the implementation of the Agreement.

### 1. *The influence of the MFA*

The Agreement has managed to remove certain disturbing features of the MFA and to abolish some of the provisions that have been impossible to define in contractual terms (such as "exceptional circumstances", "minimum viable production", etc.) and that have contributed to the kind of arbitrary bilateralism that developing exporting countries have long opposed. In many respects, however, it is a further extension of the MFA, which will continue to influence trade in this sector over the transition period, and the MFA restrictions contained in the bilateral agreements will remain until the restrained products are integrated into GATT 1994. Moreover, the provisions of the transitional safeguards bear a strong resemblance in criteria and procedures to the MFA. The monitoring system of the Agreement also follows the same pattern as that of the TSB under the MFA.

## 2. Coverage

The Annex to the Agreement defines the product coverage. It covers the whole universe of textile and clothing products in Section XI of the HS Code (excluding fibres), including many products that have never been specifically restricted under the MFA in any importing country. These products are in chapters 53, 56, 57 and 59 of Section XI of the HS Code, where there are hardly any significant imports from the restricted sources.

In addition, the Annex includes items from certain other Sections of the HS Code. These products are not, strictly speaking, textile products, but have some textile components, e.g. soft luggage, footwear uppers, umbrellas, seat belts, etc. Some of these products have found their way into the textile category system of the United States and are covered by its bilateral textile restraint agreements under the MFA. The EC also applies non-MFA restrictions to some of these items. According to ITCB estimates,<sup>155</sup> these products would account for more than 35 per cent of the total volume of imports in the EC and the United States. The inclusion of unrestricted items inflates the volume of total imports which forms the base for the integration programme. This will enable the developed importing countries to meet the integration percentage required by the Agreement with the inflated volume of imports, and to avoid liberalizing the existing MFA restrictions during the earlier stages of the integration.

## 3. Integration programme

As pointed out earlier, the programme of integration of the Agreement allows each restraining country to choose the range of textile and clothing products it prefers to integrate at each of the first three stages. Given the complexity of, and differences in, the system of major importing countries' categorization for textiles and clothing, it will be very difficult for members to monitor the integration programme effectively. For example, the EC have 114 categories in which textile and clothing products are classified, based on the degree of processing; the United States has nearly 200

categories (including part-categories) under five category series which are classified on the basis of fibres.

According to the integration ratio, as laid down in the Agreement, only 51 per cent of the products covered in the Annex will be integrated into GATT 1994 over the 10-year transition period in three stages, leaving the balance of 49 per cent to be integrated on the very last day of the Agreement. This programme evokes some doubts as to its credibility, as the restraining countries can easily evade the phasing out of the most sensitive MFA restrictions until the later stages, and the problems of industrial adjustment cannot be mitigated when such a large bulk of restrained products covered by the Annex will be left in abeyance for integration until the very last minute.

## 4. "Market disruption" and the transitional safeguards

Although the term "market disruption" is not mentioned in the text, the concept is still a basic premise of the transitional Agreement. In particular, it is reflected in the basic elements of the transitional safeguards. For example, the criteria for transitional safeguard actions under the Agreement are, in many respects, along the same lines as "market disruption" as described in Annex A of the MFA, under which discriminatory measures can be applied on a member-by-member basis against both MFA and non-MFA signatories to whom serious damage, or the actual threat thereof, is attributed. The serious damage, or actual threat thereof, will be "determined on the basis of a sharp and substantial increase in imports, actual or imminent".<sup>156</sup> Furthermore, transitional safeguard action can be taken either by mutual agreement, following consultations, or unilaterally, subject to examination by the TMB.

In terms of the other factors employed in determining "serious damage", the Agreement may have negative effects on developing exporting countries as some new factors such as wages and domestic prices have been added to the list determining serious damage.<sup>157</sup>

Compared to Annex A of the MFA, there are also some changes in the provisions of Ar-

<sup>155</sup> See ITCB document CR/XIX/(ARQ) 03, June 1994, p. 3.

<sup>156</sup> "Such an imminent increase shall be a measurable one and shall not be determined to exist on the basis of allegation, conjecture or mere possibility arising, for example, from the existence of production capacity in the exporting countries." (Annex A, II(i)).

<sup>157</sup> Under the MFA, the existence of serious damage will be determined on the basis of factors such as turnover, market

ticle 6. For instance, under the transitional safeguards, action can only be applied in situations where imports have caused serious damage. There is no possibility of taking preventive action to avoid "real risks" of serious damage, as is the case under the MFA. This could be viewed as a means to prevent the misuse of the transitional safeguard mechanism in practice.

Furthermore, as a new positive element in determining serious damage, the country imposing the action, as required by the Agreement, should also examine "on the basis of the level of imports as compared with imports from other sources" whether the serious damage has been caused to the domestic producers of the product concerned as a result of the totality of imports from all sources. Given the fact that the MFA requires serious damage to be caused by a sharp and substantial increase in imports from a particular source at prices substantially below those prevailing in the market of the importing country, this development can be seen as an important step towards the dismantling of the MFA.

However, the new concept of cumulation of damage caused by increased imports from more than one source (or the totality of imports), as referred to above, implies that more than one member could be held responsible for the serious damage, and a transitional safeguard measure could therefore be imposed on several members at the same time.

With respect to other elements such as the procedures for the application of transitional safeguards, the basic obligations concerning the base levels, growth rates and flexibility of quotas are similar to those provisions in Article 3 and Annex B of the MFA.

### **5. Relationship with the commitments under other agreements**

The provisions of Article 7 of the Agreement establish a special direct link between the benefits of the economic package of the Agree-

ment and some of the obligations under other agreements, which include the specific commitments: to achieve improvements in market access; to ensure the application of policies fairly and equitably in respect of dumping, subsidies and intellectual property protection; and to avoid discrimination against imports of textile and clothing products.

However, the unclear language and intent of the provisions of this Article may give rise to difficulties with respect to its application. Some importing countries appear to interpret this provision as linking the integration process with further tariff concessions on textiles by certain exporting countries.<sup>158</sup> However, developing exporting countries have argued that the concessions that they have made in this area are compatible with their development, finance and trade needs and that, as a matter of principle, are not prepared to pay for the phasing out of what constitutes a derogation from GATT.

### **6. Non-MFA signatories**

As mentioned earlier, one of the major differences from the MFA is that this Agreement will apply to the trade in textiles of all WTO members, including non-MFA signatories. While, under the Agreement, members that are signatories to the MFA are obliged to liberalize their restrictions in accordance with the integration programme, non-MFA signatory members are required to notify the TMB, within six months after the entry into force of the WTO Agreement, of whether or not they wish to retain the right to use the transitional safeguards. If they choose not to do so, their trade in textiles will be deemed to have been integrated into GATT 1994 at a stroke. If, however, they decide to retain the right to use the transitional safeguards, they must notify the TMB, within 12 months after the entry into force of the WTO agreements, as to which products will be integrated into GATT 1994 during the first phase.

share, profits, export performance, employment, volume of disruptive and other imports, production, utilization of capacity, productivity and investments. See Annex A to the MFA.

<sup>158</sup> The additional United States note to Section XI of its Tariff Schedule provided that the concessions in its schedule "on all textiles and clothing products covered by the Agreement on Textiles and Clothing, as specified in the Annex to that Agreement, are established based upon the fundamental understanding that the maintenance of the balance of rights and obligations under the Agreement on Textiles and Clothing, in particular Article 7 thereof, means Members will provide effective market access to textiles and clothing entering their territory from the United States. An assessment of effective market access is based upon the following criteria: (i) the reduction and binding of tariff rates at levels no higher than 35 per cent for apparel, 30 per cent for fabric and made-ups, 15 per cent for yarns, and 7.5 per cent for fibres; and (ii) the elimination of all non-tariff barriers within three years and a commitment that no new non-tariff barriers will be established". See Schedules XX - United States, Uruguay Round of Multilateral Trade Negotiations, *Legal Instruments Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations Done at Marrakesh on 15 April 1994*, published by the GATT secretariat, p. 6768.



Developing countries, which have maintained restrictions on textiles and clothing products that might not be justified under the other provisions of GATT 1994, can phase them out progressively, like MFA restrictions, within the 10-year transition period by retaining the right to invoke the transitional safeguards.

Given the fact that this Agreement is, in many respects, a further extension of the MFA, and that many non-MFA signatory members are not familiar with the practices employed in the MFA, it is important for technical assistance to be provided to these members, many of which are developing countries. ■

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## TRADE-RELATED INVESTMENT MEASURES

### A. The nature and effects of TRIMs

The measures adopted by Governments to attract and regulate foreign direct investment in their territories include both incentives designed to attract investment, such as fiscal incentives, loans, tax rebates, provision of services on preferential terms, etc., as well as a series of requirements or conditions designed to encourage the use of the investment according to national priorities. The latter category can take the form of local content requirements, manufacturing requirements, export performance requirements, and technology transfer or licensing requirements, etc. The use of these two kinds of measures constitutes the terms and conditions for the entry of investment into the host country. Where such investment measures are related to trade in goods they are defined as TRIMs. Investment incentives, increasing the after-tax return on the owner's equity, enable countries to attract foreign direct investment in specific fields, and are a means for attracting investment to sectors, regions or countries where it might otherwise not have occurred. Performance requirements, on the other hand, ensure that the operations of the firm are consonant with the policy objectives of the host country, and that they form part of an overall strategy aimed at the country's development. The latter is particularly important

for developing countries, where TRIMs are conceived as part of a strategy supportive of transfer of technology, industrialization, and economic growth. An additional motive for employing TRIMs has been to control anti-competitive and trade-restrictive business practices; developing countries considered it more practical to pre-empt such practices through TRIMs rather than to attempt to detect such practices later and to prosecute TNCs under competition law. Therefore the combination of a variety of incentives and performance requirements is aimed at securing a balanced regulation and enhancement of foreign direct investment in the host country.<sup>159</sup> Furthermore, the same mixture can ensure an adequate compromise between the interests of the host country and those of the investor.<sup>160</sup>

The availability of a diverse set of incentives and conditions provides flexibility in negotiations with potential investors, and may allow a bargain to be struck in which an incentive with high value to the investor and low marginal cost to the host country (such as access to the benefit of an existing free-trade zone) is traded for a performance requirement of low marginal cost to the investor but high real or perceived value to the host country (e.g. an agreed commitment for local expenditure on

<sup>159</sup> United States Department of Commerce, *The Use of Investment Incentives and Performance Requirements* (Washington, D.C.: 1977), pp. 1-2. The 1977 benchmark survey of the United States Department of Commerce, which provided elements for the formulation of a United States negotiating position on this issue, found that 27 per cent of United States affiliates in the developing countries received one or more incentives to invest, while the figure was 25 per cent for developed countries. However, developing countries imposed performance requirements on United States firms more often than other developed countries - 29 per cent as against 6 per cent.

<sup>160</sup> Hardeep Puri and Delfino Bondad, "TRIMs, development aspects and the General Agreement", *Uruguay Round: Further Papers on Selected Issues* (UNCTAD/ITP/42), 1990, p. 55.

research and development).<sup>161</sup> TRIMs are not unique in imposing conditions of performance. A "pure" investment incentive involving, for example, a tax rebate depending on the size of local operations, or including labour-training grants depending on the size of the labour force at the local plant, behaves like a performance requirement.<sup>162</sup> These kinds of *quid pro quo* can be found in several countries, both developed and developing.<sup>163</sup> Differences between developed and developing countries with regard to performance requirements may be traced to variations in underlying factors such as country size and the intensity of competition in the markets for FDI in which the countries operate; performance requirements may be more frequent in those developing countries where "the requirements for a successful application of performance requirements - a large, protected internal market" were found.<sup>164</sup> Some analysts have pointed out "that developed countries achieve much the same results using implicit performance requirements imposed through selective incentive granting that developing countries achieve through explicit performance requirements; there has been no clear finding as to whether the trade-distorting effects of government interventions to increase exports and reduce imports were more pronounced in developed or developing countries".<sup>165</sup>

Some economists have argued that TRIMs may lead to welfare losses, both for the country of origin and for the host country. However, it has been questioned whether the removal of TRIMs may not lead to other distortions in trade, as their removal could result in other policy adjustments whose effect on

trade would be hard to predict.<sup>166</sup> The empirical investigations of the trade effects of TRIMs are methodologically problematic, since at best they compare "actual operations of firms with a hypothetical world in which target countries have no performance requirements, while all other countries are allowed to retain investment incentives".<sup>167</sup> The motive behind many TRIMs has been to correct certain distortions in international trade, such as "the fact that the international trade of foreign-controlled firms is relatively unresponsive to differentials in international prices" and to "compensate for the pro-import and anti-export bias" of TNCs.<sup>168</sup> TRIMs may speed up the progress of a firm along a path that the management would have followed anyway, and result in firms expanding small projects to full competitive scale. Therefore, TRIMs can be used for channeling FDI to bring infant industries to maturity.

Recent surveys of FDI regimes around the world help to throw light on the incidence of some of the main types of TRIMs. For example, a review of the FDI regimes of 30 developing countries, 5 Central and Eastern European countries and 21 developed countries covering the period 1992-1993 leads to the following conclusions on the incidence and characteristics of local content requirements:<sup>169</sup>

- While a number of countries have de-emphasized the use of local content requirements, these continue to be imposed in both developed and developing countries. However, they are clearly targeted at specific industries. The overwhelming majority of local content requirements were found in the automobile and its components industries. Some require-

<sup>161</sup> Theodore H. Moran and Charles S. Pearson, "Tread carefully in the field of TRIP (Trade-Related Investment Performance) measures", *The World Economy*, Vol. 11, No. 1 (1988), p. 121.

<sup>162</sup> *Ibid.*

<sup>163</sup> The Office of the United States Trade Representative, in its *1994 National Trade Estimate Report on Foreign Trade Barriers*, identified 24 developed and developing countries that use at least one TRIM (Washington, D.C.: 1994). A UNCTC/UNCTAD study reported that European Governments offer cash grants up to 60 per cent of the cost of the entire investment; state governments in the United States have given as much as \$325 million per project (or \$108,000 per job) to foreign firms. While no explicit domestic content or export-performance regulations are involved, it would be disingenuous to argue that such efforts were not trade-related investment measures. The Federal Reserve Bank of St. Louis found a positive statistical correlation between the expenditures of individual states in the United States on investment promotion, on the one hand, and exports from those states, on the other. No less real is the import-substitution dimension of such policies among the developed nations. The trend, moreover, is worrisome. Average state expenditures in the United States to induce inward investment and to promote exports have grown over the past decade by more than 600 per cent. *The Impact of Trade-Related Investment Measures on Trade and Development* (United Nations publication, Sales No. E.91.II.A.19), 1991, p. 9.

<sup>164</sup> Stephen Guisinger, *Investment Incentives and Performance Requirements*, Report to the World Bank (July 1983), p. vii.

<sup>165</sup> *Ibid.*

<sup>166</sup> Moran and Pearson, *op. cit.*, p. 122.

<sup>167</sup> *Ibid.*, p. 126.

<sup>168</sup> *Ibid.*, p. 123.

<sup>169</sup> Based on reports by the Economist Intelligence Unit for various years; *World Investment Report: Transnational Corporations and Integrated International Production* (United Nations publication, Sales No. E 93.II.A.14), 1993; *World Investment Directory*, Vols. I, II, III and IV (1992 and 1994).

ments were also found in the audiovisual, computer equipment, pharmaceuticals and tobacco industries and in food processing activities. By contrast, none of the Central and Eastern European countries examined appeared to impose local content.

- In addition to, or instead of, direct requirements on local content, a number of countries impose indirect requirements through rules of origin which determine the level of local or regional value-added content necessary to qualify for preferential treatment under a regional integration scheme, for example NAFTA, EC, CACM.
- There is evidence that countries that have discontinued formal application of local content requirements continue to "encourage" their use in the negotiation of incentives agreements. Although this practice is quite common, even in developed countries, it is not easy to capture it in surveys of legal instruments.
- Local content continues to be a significant requirement to qualify for public procurement/public works bids, at the federal, state, province and city levels.

The proponents of negotiations in this area considered that TRIMs can have a "strong dampening and distorting effect on world trade", by distorting the pattern of trade and investment flows and that TRIMs prevented TNCs from adopting a coherent global competitive strategy. As discussed below, their removal became a main negotiating objective of the United States and some other developed countries. The 1988 Omnibus Trade and Competitiveness Act, which provided the United States with negotiating authority for the Uruguay Round, also gave the President extended power to review and block foreign takeovers of United States firms. As stated in the Act, the principal negotiating objectives of the United States regarding foreign direct investment were (i) to reduce or to eliminate artificial or trade-distorting barriers to foreign direct investment, to expand the principle of national treatment, and to reduce unreasonable barriers to establishment; and (ii) to develop internationally agreed rules, including dispute settlement procedures, which (a) will help ensure a free flow of foreign direct investment, and (b) will reduce or eliminate the trade-distortive effects of certain trade-related investment measures.<sup>170</sup>

## B. Investment and the trading system

Unsuccessful efforts were made by the developed countries, particularly since the Second World War, to establish an international regime for the protection of international investment. In the late eighteenth and nineteenth centuries, the European powers and the United States set minimum standards for the protection of foreign investment based on treatment superior to national treatment, according to which the host countries were not permitted to interfere with foreign assets and seizure and expropriation were prohibited. The standards of treatment were established in a number of commercial treaties, and were often enforced through political pressure or military intervention. These standards diverged from the general principles of international law, under which foreigners were subject to local laws and not entitled to a higher standard of justice than nationals. Interference with the property of

foreigners was permissible subject to independent judicial review and full compensation.

The Latin American countries were the first to challenge the enforcement of such favourable treatment for foreign investors in the nineteenth century, through the Calvo Doctrine (1868), which provided that an alien established in a State had the same rights as a national of the State but was not entitled to count on his home State or foreign courts for protection. The Doctrine also provided that no State might intervene, diplomatically or otherwise, to enforce one of its citizen's private claims in a foreign country. During the inter-war period, League of Nations conferences were stalemated on the issue of investor rights and host country obligations. Developing and Eastern European countries collectively succeeded in preventing attention from being exclusively focused on their obligations to

<sup>170</sup> Sect. 1101 (b)(11), 102 Stat.1107 (codified at 19 U.S.C. sect. 2901 (1988)),

foreigners and sought a collective approval for their acts to limit foreign investors rights.

After the Second World War, the United Nations Conference on Trade and Employment in 1947-1948 considered the issue of investment. In the discussions on the expansion of international trade, investment measures formed part of a wider discussion of restrictive business practices. The Havana Charter for an International Trade Organization<sup>171</sup> contained provisions on such measures. The Final Act of the Conference included the encouragement of the international flow of capital for productive investment among the objectives of the International Trade Organization (Article 1:2). Chapter III, Article 12, on "International Investment for Economic Development and Reconstruction" stated, *inter alia*, that "The Members recognize that, international investment, both public and private, can be of great value in promoting economic development and reconstruction and consequent social progress... a Member has the right to take any appropriate safeguards necessary to ensure that foreign investment is not used as a basis for interference in internal affairs or national policies; to determine whether and to what extent and upon what terms it will allow future foreign investment ...". It was recognized that such development would be facilitated if members were to offer, for international investments acceptable to them, reasonable opportunities on equitable terms to the nationals of other members and adequate security for existing and future investments. However, they also recognized the right to prescribe and give effect to reasonable requirements, including those relating to ownership, in order to safeguard national interests. The Charter also contained a chapter on Restrictive Business Practices (chap. V) which stipulated in Article 50 that "Each Member shall take all possible measures by legislation or otherwise, in accordance with its constitution or system of law and economic

organization, to ensure within its jurisdiction, that private and public commercial enterprises do not engage in practices which are as specified in paragraphs 2 and 3 of Article 46 and have the effect indicated in paragraph 1 of that Article, and it shall assist the Organization in preventing these practices".<sup>172</sup>

The negotiations which led up to the Havana Charter, and eventually to GATT, demonstrated that governments were not prepared to subject their investment policies to international rules and disciplines.<sup>173</sup> During that period, following the failure to establish an international regime for the protection of international investment, the developed countries pursued the same policies bilaterally through the conclusion of Friendship, Commerce and Navigation (FCN) Treaties and Investment Promotion and Protection agreements with host countries. The purpose of such treaties was to ensure that the property of investors would not be expropriated without prompt, adequate and effective compensation, non-discriminatory treatment, transfer of funds and dispute settlement procedures.

The issue of international investment resurfaced at the United Nations, where the developing countries sought international approval for their sovereign aspirations and endeavoured to alter the traditional international investment standards. The United Nations General Assembly passed its first resolution on Permanent Sovereignty over Natural Resources in 1962 and the Charter of Economic Rights and Duties of States in 1974. The Permanent Sovereignty resolution recognized the inalienable right of all States freely to dispose of their natural wealth and resources in accordance with their national interests and affirmed that foreign investment agreements freely entered into by sovereign States shall be observed in good faith. The Charter contained much stronger language on foreign investment; in particular Article 2 provides for the right of

<sup>171</sup> See United Nations Conference on Trade and Employment, held at Havana, Cuba, from 21 November 1947 to 24 March 1948, *Final Act and Related Documents* (Lake Success, N.Y., Interim Commission for the International Trade Organization, 1948), United Nations document E/Conf. 2/78.

<sup>172</sup> The practices are the following: fixing prices, terms or conditions to be observed in dealing with others in the purchase, sale or lease of any product; excluding enterprises from or allocating or dividing any territorial market or field of business activity, or allocating customers or fixing sales quotas or purchase quotas; discriminating against particular enterprises; limiting production or fixing production quotas; preventing by agreement the development or application of technology or invention whether patented or unpatented; extending the use of rights under patents, trademarks or copyrights granted by any member to matters which, according to its laws and regulations, are not within the scope of such grants, or to products or conditions of production, use or sale which are likewise not the subjects of such grants.

<sup>173</sup> An evaluation of restrictive business practices was carried out after 1958 by a GATT Group of Experts. The discussions of the Group were focused on the activities of international cartels and trusts which might hamper the expansion of world trade and interfere with the objectives of GATT. See *Restrictive Business Practices*, GATT Resolution of 5 November 1958, reprinted in GATT, *BISD*, Seventh Supplement, 1959, p. 29, and GATT document No. L/1015, reprinted in *BISD*, Ninth Supplement, 1961, p. 171. The contracting parties also included a general statement on the importance of international investment for economic development. See *BISD*, Third Supplement, 1955, pp. 49-50.

each State to regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities and that no State shall be compelled to grant preferential treatment to foreign investment. The draft Code of Conduct on Transnational Corporations of the United Nations Commission on Transnational Corporations addressed a wide range of issues such as respect for national sovereignty, observance of national laws, adherence to socio-economic objectives of host States, restrictive business practices, transfer pricing, treatment of transnational corporations, nationalization, appropriation and compensation. Most developed countries were opposed to a legally binding status for the code. The Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices,<sup>174</sup> and the OECD Declaration and Decisions on International Investment and Multinational Enterprises and Codes on Liberalization of Current Invisible Operations and Capital Movements<sup>175</sup> deal with some aspects of the behaviour and treatment of transnational corporations as did provisions included in the UNCTAD draft code of conduct on transfer of technology.

At the regional level efforts have also been made to deal with investment issues, for example the Treaty of Rome establishing the EEC provided for freedom of movement for persons, services and capital. Articles 52 to 58 on right of establishment stipulate, *inter alia*, that freedom of establishment includes the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms, under conditions of national treatment. The North American Free Trade Agreement provides for national treatment, MFN, non-discriminatory treatment, and minimum standards of treatment in accordance with international law for investors and investments of another signatory State. The Agreement also prohibits a number of performance requirements.

After the conclusion of the Tokyo Round of Multilateral Trade Negotiations in 1979, there have been attempts to bring under the purview of the General Agreement a more focused consideration of a limited number of

performance requirements introduced by host countries with regard to foreign investors, particularly in relation to the use of local content and to export performance. However, several contracting parties, especially developing countries, resisted those attempts, maintaining that the issue of foreign direct investment was beyond the jurisdictional competence of GATT. On the other hand, the United States and some other developed countries argued that such requirements have effects clearly related to trade and should be addressed by the contracting parties through a detailed examination of GATT articles. The issue of investment could not be successfully pursued at the 1982 GATT Ministerial Meeting.

The dispute brought by the United States against Canada on FIRA (Administration of the Foreign Investment Review Act) in 1982 was a significant step in defining the extent to which investment measures were covered by multilateral trade obligations. The United States claimed that the requirements imposed on the foreign investor by FIRA to purchase goods of Canadian origin in preference to imported goods, to manufacture goods in Canada which would otherwise have to be imported and to export specified quantities of production were inconsistent with Articles III:4, III:5, XI and XVI:1(c). A large number of delegations had expressed doubts as to whether the dispute between the United States and Canada was one for which GATT had competence since it involved investment legislation, a subject not covered by GATT. The Council finally decided to allow the panel to proceed with its work, with the terms of reference as agreed, on the presumption that the report of the panel would be limited in its activities and findings to within the boundaries of GATT and the legislation as such would not be called into question.

The FIRA panel found that Canada's practice of allowing certain foreign direct investments under FIRA on condition that the investors provide written undertakings to purchase goods of Canadian origin or from Canadian sources was inconsistent with Article III:4 of GATT, which stipulates that imported products shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.

<sup>174</sup> Philippe Brusick, Murray Gibbs and Mina Mashayekhi, "Anti-competitive practices in the services sector", *Uruguay Round: Further Papers on Selected Issues* (UNCTAD, ITP/42), 1990, p. 129.

<sup>175</sup> The Declaration contains a recommendation to multinational enterprises operating in member States to observe a set of annexed Guidelines, a commitment by the signatories to accord national treatment to foreign-controlled enterprises operating in their States and some consultation provisions. The OECD Codes on Liberalisation of Current Invisible Operations and on Capital Movements aim at removing barriers to capital movement between OECD member countries and contain a commitment to accord national treatment to foreign investments.

On the other hand, the undertakings to purchase Canadian goods did not prevent the importation of goods as such and were therefore found not to be inconsistent with Article XI:1 of the General Agreement on the prohibition of quantitative restrictions, nor were Canadian requirements that investors provide written undertakings that they would export a specified amount or proportion of their production in violation of Article XVI:1.<sup>176</sup>

Argentina made a submission to the panel noting that the dispute involved two developed countries and could not be invoked as a precedent against similar measures applied by developing countries, given the provisions in GATT that provided greater flexibility for such countries, particularly Article XVIII. In response, the panel recognized that in any dispute involving developing countries full account should be taken of the special provisions of GATT for such countries.<sup>177</sup>

The FIRA Panel Report provided the basis for a more effective challenge of TRIMs at the multilateral level. The United States trade legislation was amended to address investment measures more directly. Section 301 of the 1974 Trade Act, as amended in 1984, and sections 305 and 307 of the 1984 Trade and Tariffs Act confer on the relevant authorities in the United States the required legislative authority on the issue of foreign direct investment. Section 307 defines international trade so as to include both goods and services and foreign direct investment by United States persons, especially if such investment has implications for trade in goods and services. It further provides that if the United States Trade Representative (USTR) determines that action by the United States is appropriate to respond to any export performance requirements of any foreign country or instrumentality that adversely affect the economic interests of the United States, the USTR shall seek to obtain the reduction and elimination of such export performance requirements and may impose duties or other import restrictions on the products or services of such entities for such time as is determined appropriate, including the exclusion from entry into the United States of products subject to such requirements. During the preparatory process for the Uruguay Round, the

United States proposed<sup>178</sup> that the negotiations should (i) seek to increase discipline over government investment measures which divert trade and investment flows at the expense of other contracting parties; (ii) explore a broad range of investment issues in the negotiations, including national/MFN treatment for new and established direct investment and the right to establish an investment; and (iii) examine various types of trade-related investment measures such as local content requirements, export performance requirements, incentives and product mandating, which should be controlled and reduced in the light of specific articles of GATT as well as its overall objectives.

The scope and limits of the negotiations on TRIMs in the Uruguay Round were spelt out in the Punta del Este Ministerial Declaration as follows:

Following an examination of the operation of GATT Articles related to the trade restrictive and distorting effects of investment measures, negotiations should elaborate, as appropriate, further provisions that may be necessary to *avoid such adverse effects on trade*.<sup>179</sup>

The Mid-Term Review Decision of the Trade Negotiations Committee, which met at Montreal in December 1988, expressed this negotiating objective in terms of procedure, in the form of a series of elements:

- Further identification of the trade restrictive and distorting effects of investment measures that are or may be covered by GATT Articles, specifying those Articles.
- Identification of other trade restrictive and distorting effects of investment measures that may not be covered adequately by existing GATT Articles but are relevant to the mandate of the Group given by the Punta del Este Ministerial Declaration.
- Development aspects that would require consideration.
- Means of avoiding the identified adverse trade effects of trade-related investment measures including, as appropriate, new provisions to be elaborated where existing

<sup>176</sup> The FIRA panel did not examine the following measures, thereby leaving their GATT legal status unresolved: undertakings to set up a purchasing division within a Canadian subsidiary; undertakings to consult Canadian industry specialists in drawing up tender lists; undertakings to manufacture goods or components that would otherwise be imported; undertakings regarding Canadian participation in the enterprise. There are no other GATT dispute settlement rulings on these issues.

<sup>177</sup> See *BISD*, Thirtieth Supplement, pp. 140-166.

<sup>178</sup> GATT document PREP.COM(86):W/35, 11 June 1986.

<sup>179</sup> "Ministerial Declaration on the Uruguay Round", *Uruguay Round: Papers on Selected Issues* (UNCTAD/ITP/10), 1989, Annex I, p. 376. Emphasis added.



GATT Articles may not cover them adequately.

- Other relevant issues, such as the modalities and implementation.<sup>180</sup>

Neither the mandate nor the Mid-Term Review Decision implied that investment measures could be presumed to have trade-restrictive effects *per se*. The negotiations were expected to investigate whether such measures had effects that distorted or restricted

international trade. During the course of the negotiations on TRIMs, however, there were attempts to go beyond the carefully balanced nature of these texts and to evolve what appeared to be a regime for investment in general, including right of establishment and national treatment. Developed countries, arguing that the effects could not be separated from the measures themselves, called for the elimination of TRIMs altogether rather than for minimizing and avoiding the adverse effects of these measures on trade.

### C. Different negotiating approaches

Two basic issues separated the participants in the negotiations: The first was whether the disciplines developed in this area should be limited by existing GATT Articles or expanded to develop an investment regime, while the second was whether some or all actionable TRIMs should be prohibited or should be dealt with on a case-by-case basis demonstration of direct and significant restrictive and adverse effects on trade.

The United States and Japan were in favour of an international investment regime that would establish rights for foreign investors and reduce constraints on transnational corporations. They believed that TRIMs could and did have adverse trade effects and that this was a sufficient reason to make the case for applying general principles and disciplines to control them. The submissions by these countries<sup>181</sup> enumerated a number of regulatory performance requirements adopted by governments of

host countries, which were alleged to have trade-distorting and inhibiting effects, such as requirements for local content, export performance, trade balancing, domestic sales, manufacturing, product mandating, remittance restrictions, technology transfer, licensing and local equity. In a separate category, incentives granted by governments were included because they allegedly led to distortions of trade flows, for example, when they result in creation of trade or subsidized trade flows. For each of the TRIMs mentioned above, a large number of GATT Articles were cited as being of relevance, and it was suggested that these articles be reviewed in depth in order to assess their relevance and establish, where necessary, additional disciplines. The United States position was that GATT already covered trade-related investment measures but that these should be addressed more explicitly through the elaboration of additional disciplines.<sup>182</sup> The

<sup>180</sup> GATT document MTN.TNC/11.

<sup>181</sup> See submissions by the United States, documents MTN.GNG/NG12/W/1, W/2, W/4, W/5, W/9, W/11, W/14, W/15, and W/24. See submissions by Japan, documents MTN.GNG/NG12/W/7, W/12 and W/20. See submission by Switzerland MTN.GNG/NG12/W/16, 7 July 1989. The Swiss proposal also called for comprehensive disciplines on TRIMs based on categorization of such measures in three groups namely, (i) Category A: prohibited investment measures i.e. those that influence the business behaviour of the investor during the production process and are thus inherently trade distorting e.g. local content, trade balancing, manufacturing, product mandating, and export requirements; (ii) Category B: permitted investment measures: i.e. all investment decisions *per se*, that influence decisions to invest, such as limitations to foreign investment and investment incentives for regional development; (iii) Category C: actionable measures, i.e. measures on which agreement could not be reached and ways and means to be agreed on to reduce their number. The proposal established formal methods and criteria for treating a given TRIM under a specific category based first on a classification by each country in the light of macroeconomic and trade conditions, and subsequently on multilateral negotiations. For category C, Switzerland proposed a request/offer exchange of concessions.

<sup>182</sup> The United States attempted to categorize the effects of TRIMs as those which: (i) prevent, reduce or divert imports by limiting the sale, purchase and use of imported products; (ii) restrict the ability to export of home and third country producers; and (iii) artificially inflate exports from a host country, thereby distorting trade flows in world markets. It also requested that the applicability of some trade policy concepts to TRIMs should be considered, namely non-discrimination (MFN and national treatment), prohibition (as implicit in Articles I, II, XI, and XVI), transparency, and dispute settlement.

main elements of the United States proposal were that certain TRIMs should be categorically prohibited, that a test should be established to evaluate the adverse trade effects of other TRIMs, that a framework should be developed to phase out prohibited TRIMs, that a notification procedure should be developed, and that an oversight committee should be established to review the work of the Agreement. As far as development issues were concerned the United States proposed that effective disciplines against TRIMs should first be established and that arrangements for a transitional period during which developing countries would eliminate the prohibited TRIMs should then be considered.

The proposal by Japan also drew attention to the need for inclusion of both national and local government measures, apparently in order to cover policies introduced at the state rather than the federal level in the United States. Another important feature of the proposal concerned the methodology to facilitate examination of the effects of TRIMs by classifying them into those that were clearly inconsistent with GATT (type A) and those that were consistent with GATT but were relevant to its provisions (type B). The intention was that type A measures (i.e. local content, export performance, trade balancing, domestic sales, technology transfer, manufacturing, product mandating requirements) should be prohibited while further general disciplines would be elaborated for type B measures. Unlike the United States, Japan did not include investment incentives.

The EC and the Nordic countries<sup>183</sup> focused on measures that had a direct and significant restrictive impact on trade and a direct link to existing GATT rules. They drew a clear distinction between the general issue of foreign direct investment and the more specific issues of trade-related investment measures and

therefore opposed the inclusion of right of establishment and transfer of resources in the negotiations. They believed that direct and indirect trade effects of investment measures should be evaluated separately. Indirect trade effects in their opinion were caused by TRIMs related to licensing, local equity and technology transfer requirements, remittances and exchange restrictions, and investment incentives. TRIMs with indirect effects would be subject to consultation and dispute settlement procedure. The Nordic countries identified two TRIMs i.e. local content and export performance requirements, that should be phased out in accordance with a notification process, then undergo a binding period based on the results of the notifications, and finally an adjustment period in the light of the situation of developing and least developed countries. The EC, on the other hand, identified eight TRIMs that met the criterion of being directed at the exports and imports of a company with the immediate objective of influencing its trading patterns. These requirements were local content, manufacturing, export performance, product mandating, trade balancing, exchange restrictions, domestic sales, and manufacturing limitations concerning components of the final product. On the question of exceptions such as those for the developing countries, the EC believed that the question of exceptions could not be examined until the TRIMs and relevant GATT provisions had been identified.

Developing countries called for strict adherence to the mandate and for limiting the negotiating exercise to the effects of investment measures or regulations that had a direct and significant negative effect on trade.<sup>184</sup> Whilst highlighting their need for foreign direct investment, they maintained that certain investment measures or performance requirements were necessary to channel foreign investment according to their national development policy objectives. Developing countries argued that

<sup>183</sup> See submissions by the EC, documents MTN.GNG/NG12/W/8, W/10 and W/22, and the submissions by the Nordic countries, documents MTN.GNG/NG12/W/6 and W/23.

<sup>184</sup> See Meeting of 30 October - 2 November 1987, document MTN.GNG/NG12/4, pp. 11-12, where some developing countries' positions have been summarized as follows: "the delegation could not accept the view that the objective of negotiations was to establish within GATT a new system to regulate trade-related investment measures or to provide for a smooth development of the international exchange of investment, as had been stated in the submission by the Japanese Government (MTN.GNG/NG12/W/7). The objective of the Group's work was to clarify the operation of GATT Articles and to elaborate such further provisions as may be necessary. This could not be construed as a license to create a new regime or agreement. It was clear that the negotiating mandate could not provide a basis to question the sovereign right of governments to regulate foreign direct investment and lay down conditions of establishment for foreign enterprises. Nor could it allow national policies on investment, industrialization and treatment of foreign capital to be questioned on the grounds that these were trade-related" and the "Second of these participants stated that the focus of discussions should be the examination of direct, significant, negative effects on trade caused by investment measures. In order to make GATT Articles applicable, such effects must necessarily bring about a concrete negative result on trade since investment measures *per se* were not covered by the General Agreement. The absence of a real link to trade for some effects of investment measures was leading some countries to apply subjective elements of presumption of eventual harm to trade flows. This was the case of such measures such as remittance restrictions, technology transfer requirements, licensing requirements and others. Measures of this kind related to issues of foreign capital treatment, in the scope of industrial policies, which were not of GATT's competence."

they used TRIMs to offset the anti-competitive practices of the transnational corporations, and that these should be addressed, particularly the restrictive business practices which in themselves would have trade-distorting effects in any solution decided upon (see box 13). Such measures were considered outside the scope of the negotiating mandate by the United States and the EC.

The developing countries have also stressed the necessity of differential and more favourable treatment in their favour. In this context they cited the FIRA Panel's recognition that in disputes involving less-developed (i.e. developing) contracting parties, full account should be taken of the special provisions of the General Agreement relating to these countries (such as Article XVIII:C). Malaysia linked TRIMs to the provisions of Part IV, in particular Articles XXXVI:3, XXXVI:5, XXXVI:9 and XXXVII:3(c). As mentioned above, the developed countries believed that, following the establishment of disciplines on TRIMs containing obligations for all participants, considerations relating to development could be addressed. India's comprehensive proposal on TRIMs included, *inter alia*, a part on specific investment measures and their trade effects, in which it was stated that there were two performance requirements that could have trade effects: export performance requirements and local content/manufacturing. These measures, however, did not have adverse trade effects in all circumstances; their developmental dimensions far outweighed their trade effects in the case of developing countries and they were used to counter restrictive business practices of TNCs.

The submissions of the group of developing countries outlined, *inter alia*, the methodological approach they advocated in determining the effects of TRIMs as follows: (i) there could be no *a priori* presumption that investment measures were inherently trade restrictive or distorting; (ii) if it were demon-

strated in the group that, in certain circumstances and on a case-by-case basis, some investment measures did indeed have a direct and significant adverse effect on trade, a clear causal link would need to be established between the measure and the alleged effect; (iii) if such a link was established, the nature and impact on the interests of the affected party would have to be assessed; (iv) once the above-mentioned steps had been undertaken, appropriate ways and means would have to be found to deal with the demonstrated adverse effects; and (v) the foregoing meant that it was the effects and not the measures themselves that needed to be addressed.<sup>185</sup>

After May 1990 the Chairman of the TRIMs Negotiating Group issued several drafts<sup>186</sup> designed to integrate the different approaches mentioned above.<sup>187</sup> The Chairman's drafts encountered considerable opposition on all sides, particularly on the following questions: (i) on coverage, whether the agreement would cover measures imposed only when the investment was made, or also measures applied to established firms, and whether TRIMs that were enforceable through a government offering or the withdrawal of advantages and particularly subsidies should be covered or only TRIMs that were legally enforceable; (ii) on prohibition, the divergences of view related to whether TRIMs should be avoided on a case-by-case basis through trade remedies only, or in certain cases by prohibition as well (e.g. those already prohibited by Articles III and XI); (iii) whether the developing countries should be given additional flexibility, e.g. through an extended transitional arrangement; and (iv) whether restrictive business practices should be addressed. As a result, the Brussels text of the Final Act did not contain any text on TRIMs. The Draft Final Act submitted by the Director-General of GATT in December 1991 tackled the above-mentioned issues by proposing compromise texts. The TRIMs Agreement adopted at Marrakesh is identical to that contained in the 1991 Draft Final Act.

<sup>185</sup> See submissions by Malaysia (MTN.GNG/NG12/W/13), Singapore (MTN.GNG/NG12/W/17), India (MTN.GNG/NG12/W/18), Mexico (MTN.GNG/NG12/W/19), and Bangladesh (MTN.GNG/NG12/W/21). Mexico proposed that the effects of two TRIMs (export requirements and local equity requirements) be empirically tested. See the joint submission by developing countries (Argentina, Brazil, Cameroon, China, Colombia, Cuba, Egypt, India, Tanzania (United Rep. of) and Yugoslavia) (MTN.GNG/NG12/W/25), and draft Declaration on TRIMs submitted by Bangladesh, Brazil, Colombia, Cuba, Egypt, India, Kenya, Nigeria, Pakistan, Peru, Tanzania (United Rep. of) and Zimbabwe) (MTN.GNG/NG/W/26).

<sup>186</sup> The Chairman's first to fifth drafts were dated 18 May 1990, 29 June 1990, 19 July 1990 (MTN.GNG/NG12/W/27), 24 October 1990 and 20 November 1990. The latter, known as the Hong Kong draft, was prepared by Hong Kong on behalf of the Chairman of the Trade Negotiations Committee (TNC) in consultation with several delegations.

<sup>187</sup> The drafts originally included a submission written by the Chairman which became the "A" text, document MTN.GNG/NG12/W/24 from the United States was known as the "B" text, and document MTN.GNG/NG12/W/26 from developing countries became the "C" text. Subsequently, the texts were merged.

## Box 13

**RESTRICTIVE BUSINESS PRACTICES BY TNCs IN DEVELOPING COUNTRIES,  
THEIR POSSIBLE OUTCOME AND TRIMS DESIGNED TO DEAL WITH THEM<sup>1</sup>**

RBPs	Possible outcome	Associated TRIMs
<i>A. Horizontal RBPs</i>		
Market allocation	Export prohibition; specific market allocation	Trade-balancing requirement; export requirement
Refusal to deal (boycott)	Refusal to supply	Manufacturing requirement
Price fixing	Excessive pricing for imports; low pricing for exports	Local content requirement; local equity requirement; joint venture with government participation
Collusive tendering	Excessive pricing for imports	Local content requirement; domestic sales requirement.
<i>B. Vertical RBPs</i>		
Refusal to deal	Import refusal or prohibition	Local content requirement
Exclusive dealing	Export prohibition	Export requirement
Differential pricing	Excessive pricing for imports	Local content requirement; domestic sales requirement
Resale price maintenance	Excessive pricing for exports and imports	Export requirement; local equity requirement
Tied selling	Excessive conditions for imports	Domestic sales requirement; licensing and technology transfer requirement
Predatory pricing	Predatory pricing for imports	Manufacturing requirement
Transfer pricing	Predatory pricing for imports or excessive pricing resulting in remittance evasion	Remittance and exchange restrictions; manufacturing requirement; domestic sales requirement

<sup>1</sup> Hardeep Puri and Philippe Brusick, "Trade-related investment measures: Issues for developing countries in the Uruguay Round", *Uruguay Round: Papers on Selected Issues* (UNCTAD/ITP/10), 1989, p. 219.

## D. Agreement on Trade-Related Investment Measures (TRIMs)

The TRIMs Agreement establishes the extent to which multilateral trade obligations cover investment measures. It prohibits those measures which are prohibited by GATT Articles III and XI. The developing countries were thus successful in preventing the extension of

trade obligations into the field of investment, and the incorporation of principles such as "right of establishment" and "national treatment" for investors into the trading system. Countries maintain their sovereign rights to regulate foreign direct investment so long as the

TRIMs Agreement is not infringed. The Preamble of the TRIMs Agreement recognizes that certain investment measures can cause trade-restrictive and distorting effects. The scope and coverage of the Agreement is circumscribed by Article 1 which stipulates that it relates to trade in goods only. It should be noted that the General Agreement on Trade in Services (GATS) covers investment liberalization as it includes commercial presence as one of the modes of supply of services, defined in Article XXVIII of GATS as "any type of business or professional establishment, including through the constitution, acquisition or maintenance of a juridical person, or the creation or maintenance of a branch or a representative office within the territory of a Member for the purpose of supplying a service".<sup>188</sup>

Article 2 on National Treatment and Quantitative Restrictions in the TRIMs Agreement limits the prohibited TRIMs to those inconsistent with the provisions of GATT Article III on National Treatment on Internal Taxation and Regulation and Article XI on General Elimination of Quantitative Restrictions. The Agreement therefore recognizes that certain measures do violate GATT Articles but does not expand on the existing disciplines. The Annex to the Agreement contains an illustrative list of such TRIMs which are mandatory or enforceable under domestic law or under administrative rulings, or compliance with which is necessary to obtain an advantage,<sup>189</sup> as follows (i) under the national treatment obligation TRIMs include those that require: (a) the purchase or use by an enterprise of products of domestic origin or from any domestic source (i.e. local content requirement); or (b) that an enterprise's purchases or use of imported products be limited to an amount related to the volume or value of local products that it exports (i.e. trade balancing requirement); (ii) TRIMs that are inconsistent with the obligation of Article XI:1 are those which restrict (a) the importation of products to an amount related to the quantity or value of local products exported (i.e. trade balancing); (b) the importation of products by restricting an enterprise's access to foreign exchange to the

amount of foreign exchange inflows attributable to the enterprise (i.e. exchange restrictions); or (c) the exportation of products specified in terms of volume or value of local production (i.e. domestic sales requirement). These two Articles and the illustrative list basically codify the findings in the FIRA case mentioned above. The TRIMs Agreement does not give a definition of a TRIM or an objective test for identifying such measures. It seems, therefore, that it is for the notifying country to judge which of its TRIMs are illegal under the Agreement. It is only after the TRIMs Committee has entered into operation that some guidance could be given on which measures are, strictly speaking, prohibited. Until such time, countries will have to notify the measures that they believe are not in conformity with Article 2. This is naturally subject to interpretation and differences of opinion. It can be expected that the countries most opposed to TRIMs will initiate litigation in order to determine the frontiers of the Agreement.

However, it is clear that export performance requirements remain permissible under the WTO Agreements.<sup>190</sup> Most developing countries have export requirements and they are normally mandatory for most investments in free trade zones or exclusive economic zones. Several other measures which may appear controversial can be maintained by host countries because there are no explicit legal prohibitions against them.

Since neither GATT case history nor the WTO rules address the wide range of investment policy measures currently in effect in many countries, the status of several of these is unclear. A narrow interpretation of the rules would imply that any measure that is not covered in the TRIMs text, or the Agreement on Subsidies and Countervailing Measures and is not inconsistent with basic GATT principles, would be acceptable or legitimate. But the question is particularly complicated for voluntary programmes since the TRIMs Agreement specifies measures that are "mandatory or enforceable under domestic law or administrative rulings", but it also refers to obtaining an advantage. This "advantage" may not be formally

<sup>188</sup> See chapter VII.

<sup>189</sup> An "advantage" is not defined in the Agreement and therefore its scope could be wide including, *inter alia*, subsidies. The Agreement on Subsidies and Countervailing Measures is also of interest in this respect as it disciplines trade-promoting investment measures or incentives. Moreover, it refers specifically to subsidies tied to export performance and domestic sourcing requirements in Article 3, paragraph 3.1: "Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1 above, shall be prohibited:

(a) subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex 1;

(b) subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods.

<sup>190</sup> Although subsidies linked to such requirements would be covered by the discipline of the Agreement on Subsidies and Countervailing Measures.

linked to the investment measure concerned.<sup>191</sup> However, Article 6 provides strengthened obligations on transparency in the administration of TRIMs, and TRIMs that are not transparent are likely to face challenges from trading partners.

There is no reference to a case-by-case effects test or measures of sub-national levels of government. Article 6, however, does provide for the notification to the WTO secretariat of the publications in which TRIMs may be found, including those applied by regional and local governments and authorities within their territories.

All exceptions under GATT apply, as appropriate, to the TRIMs Agreement (public morals, environmental protection, national security, etc.). Developing countries are free to deviate temporarily from the provisions prohibiting certain TRIMs (Article 2) to the extent that Article XVIII of GATT, the Understanding on Balance-of-Payments Provisions of GATT, and the Declaration on Trade Measures Taken for Balance-of-Payments Purposes adopted on 28 November 1979 permits them to deviate from Articles III and XI. In accordance with Article 5 on Notification and Transitional Arrangements, members should, within 90 days of the date of entry into force of the WTO Agreement, notify the Council for Trade in Goods of all TRIMs of general or specific application which they are applying that are not in conformity with the provisions of this Agreement. The TRIMs so notified should be eliminated within two years of the date of entry into force of the WTO Agreement by developed country members. Developing countries are allowed five years and the least developed countries a seven-year transitional period for eliminating the prohibited TRIMs, which could be extended if they demonstrate particular difficulties in doing so, and taking into account the individual development, financial and trade needs of the members in question. TRIMs introduced less than 180 days before the entry into force of the WTO will not benefit from the transitional arrangements, and members should not modify the terms of any notified TRIM so as to increase the degree of inconsistency with Article 2. Such provisions amount to a standstill on the prohibited TRIMs. The TRIMs

text, however, permits TRIMs to be levied on new investors in the transition period to protect existing investors. This addresses a major concern of current investors, particularly in the automotive sector, regarding possible serious disadvantages vis-à-vis new investors. Local content requirements and domestic sourcing are most prevalent in the automotive industry.

The Agreement establishes a Committee on Trade-Related Investment Measures to monitor its operation and implementation. Disputes arising under the Agreement will be subject to the integrated dispute settlement mechanism of the WTO.

In the final analysis, the Agreement on TRIMs does not burden member States with any new obligations. Compared to the range of policy instruments at a government's disposal, the TRIMs Agreement does not significantly constrain the ability of any government to regulate foreign direct investment in its territory. However, the import-substituting measures of many developing countries are now more explicitly prohibited. In any event, the above investment measures were inconsistent with GATT principles and could have been challenged in a dispute; the TRIMs Agreement simply codifies what had already been enunciated in the Canadian FIRA case. The WTO and the single undertaking clarify the application of these obligations to developing countries and transition economies, but challenges will no doubt be made to establish the exact "frontier" of the prohibition beyond the scope of the "illustrative list". Although the developing countries managed to limit the scope of the Agreement on TRIMs during the Uruguay Round, Article 9 on the review of the operation of the Agreement no later than five years after the date of entry into force of the WTO Agreement provides for consideration as to whether the Agreement should be complemented with provisions on investment policy and competition policy.

In the latter instance it should be noted that the TRIMs Agreement does not contain provisions on restrictive business practices. It would appear that any extension of multilateral trade rules to cover investment measures would be related to the negotiation of multilateral rules on competition policy. ■

<sup>191</sup> The 1990 Panel on EEC-Regulation on Imports of Parts and Components suggested a broad scope for the application to Article III. The Panel ruled that the comprehensive coverage of all laws, regulations or requirements affecting the internal sale, etc., of imported products suggests that not only requirements which an enterprise is legally bound to carry out, such as those examined by the FIRA Panel, but also those which an enterprise voluntarily accepts in order to obtain an advantage from the government constitute requirements within the meaning of that provision. The Panel noted that the EEC made the grant of an advantage, namely the suspension of proceedings under the anti-circumvention provision, dependent on undertakings to limit the use of parts or materials of Japanese origin without imposing similar limitations on the use of like products of EEC or other origin, hence dependent on undertakings to accord treatment to imported products less favourable than that accorded to like products of national origin in respect of their internal use. GATT, *BISD*, Thirty-seventh Supplement, pp. 132, 197.

## GENERAL AGREEMENT ON TRADE IN SERVICES

### A. The background to the debate on services

The United States Administration possessed a sufficient mandate in the Tokyo Round to negotiate on services agreements under Section 102 (g) of the Trade Act of 1974. However, the United States did not press for concessions in the services sector, given its preoccupation, and those of its main trading partners, with other issues. Nevertheless, provisions dealing with certain services were incorporated in the Tokyo Round results in the context of the Codes on Customs Valuation and on Government Procurement. During the Tokyo Round, the United States Government continued to conduct research on services, and a Services Advisory Committee was established to provide direct government-industry collaboration on issues relating to trade in services. The United States accordingly initiated in 1980 a public relations campaign aimed at achieving an "international consensus" for negotiations

on services under GATT auspices, including academic research, high level seminars and a work programme on services in the OECD. The United States advocacy of liberalization of services trade and investment appears to have been the result of three factors: (a) response to pressures from a group of transnational corporations; (b) its desire to strengthen the "free trade lobby" to offset the growing political power of protectionist interests; and (c) the recognition that services were of growing importance in the United States' exports and investment abroad.

The United States Administration, in Title III of the Trade and Tariff Act of 1984, provided the mandate for negotiations on trade in services. These objectives were later reconfirmed in the Omnibus Trade and Competitiveness Act of 1988.<sup>192</sup> These Acts authorize

<sup>192</sup> The enactment of the Trade and Tariff Act (TTA) on 30 October 1984 (Public Law No. 98-573) provided the United States Administration with a coherent integrated approach to negotiate on goods, services, high technology and investment, and identified the issues which that country would raise in such negotiations. Title III of this Act, itself cited as the "International Trade and Investment Act", amends the Trade Act of 1974 in several important respects, integrating trade, services, investment and technology objectives, and including a new concept of reciprocity, that of the "achievement of commercial opportunities in foreign markets substantially equivalent to those accorded by the United States".

The United States' negotiating objectives on services and investment include: (a) the reduction and elimination of barriers which deny national treatment and restrictions on establishment and operation in such markets; and (b) the development of international rules, including dispute settlement procedures, in conformity with this objective. Cited as examples of such barriers and distortions are "direct or indirect restrictions on the transfer of information into or out of the country" and "restrictions on the use of data processing facilities within or outside such country" (Section 305).

Title III also contains negotiating objectives on "high technology products" which establish the link between services, investment and technology. For example, one of the principal negotiating objectives is to "obtain and preserve the maximum openness with respect to international trade and investment in high technology products and related services". The main target is "foreign government intervention affecting United States exports of high technology products or investments in high technology industries" including "foreign industrial policies which distort international trade and investment" and "measures which deny national treatment or otherwise discriminate in favour of domestic high technology industries". Among the specific objectives are "national treatment" to "obtain commitments that official policy of foreign countries... will not discourage government or private procurement of foreign high technology products and related services" and reduction and elimination of other barriers. Subsequently, the Omnibus Trade and Competitiveness Act of 1988 renewed the President's multilateral and bilateral negotiating authority, establishing negotiating objectives for the Uruguay Round and, *inter alia*, strengthening the United States Trade Representative's retaliatory powers.

sanctions against offending countries, including the right to withdraw concessions on goods of countries which neither subscribe to nor apply these principles on services.

The United States argued that the priority issue of the 1982 GATT meeting at Ministerial level was to establish a work programme on services in GATT to prepare the technical base for multilateral negotiations in this area.<sup>193</sup> However, the developing countries and some developed countries resisted this initiative, on the grounds that the discussion of services in a GATT context could create a basic assumption that GATT principles should apply to services, thus placing the non-OECD countries in the defensive position of having to justify the "legitimacy" of departures from MFN or "national treatment" in services and investment when they had never accepted such principles multilaterally. Such discussion could also assume a link between concessions on goods and services and thus serve to legitimize

the cross-sectoral retaliatory provisions of the United States Trade and Tariff Act of 1984 (later strengthened in the Omnibus Trade and Competitiveness Act of 1988). A compromise position was ultimately adopted at the 1982 meeting that contracting parties with an interest in services could undertake national studies on trade problems in this sector and exchange relevant information through international organizations "such as GATT". The results of these examinations, along with the information and comments provided by the relevant international organizations, were to be reviewed at the Fortieth GATT Session in 1984. The decision also empowered the contracting parties to consider whether action on negotiations on services was appropriate and desirable.<sup>194</sup> At the November 1984 GATT Session, it was decided to establish a working group aimed at improving information regarding services. Discussions on this issue were also held at the Preparatory Committee for the Ministerial Meeting at Punta del Este.

## B. The Punta del Este Declaration

A compromise was reached at the Punta del Este Ministerial Meeting that launched the Uruguay Round in September 1986. The "Ministers", not the "Contracting Parties" of GATT, agreed to launch negotiations on trade in services as a part of the new round of multilateral trade negotiations (MTN) and embodied their decision in Part II of the Declaration of Punta del Este.<sup>195</sup> The text carefully balanced the United States' objective of including ser-

vices in the Uruguay Round, and the developing countries' dual objective of maintaining multilateral action on services (as distinct from goods) outside GATT, and of obtaining recognition of the priority of development objectives and the supremacy of national laws and regulations.<sup>196</sup> The developing countries succeeded at Punta del Este in establishing a legally distinct negotiating process on trade in services to be conducted in an ad hoc juridical frame of

<sup>193</sup> It should be noted that the United States at the 1982 Ministerial Meeting already had a sufficient mandate to negotiate on services agreements under Section 102 (g) of the Trade Act, 1974, which defined "international trade" as trade in goods and services. The mandate indicated that the Government should negotiate to liberalize the regulations in trade in goods as well as in services.

<sup>194</sup> Submissions were prepared by most industrial nations. Studies were submitted by the EC and its Member States, Canada, the United States, Australia, Japan, Norway, Sweden and Finland.

<sup>195</sup> Ministerial Declaration on the Uruguay Round (MIN.DEC). See also Murray Gibbs and Mina Mashayekhi, "Elements of a Multilateral Framework of Principles and Rules for Trade in Services", *Uruguay Round. Papers on Selected Issues* (UNCTAD/ITP/10), 1989, p. 81 and Annex I.

"Negotiations in this area shall aim to establish a multilateral framework of principles and rules for trade in services, including elaboration of possible disciplines for individual sectors, with a view to expansion of such trade under conditions of transparency and progressive liberalization and as a means of promoting economic growth of all trading partners and the development of developing countries. Such framework shall respect the policy objectives of national laws and regulations applying to services and shall take into account the work of relevant international organizations.

GATT procedures and practices shall apply to these negotiations. A Group of Negotiations on Services is established to deal with these matters. Participation in the negotiations under this Part of the Declaration will be open to the same countries as under Part I. GATT secretariat support will be provided, with technical support from other organizations as decided by the Group of Negotiations on Services. The Group of Negotiations on Services shall report to the Trade Negotiations Committee.

When the results of the Multilateral Trade Negotiations in all areas have been established, Ministers meeting also on the occasion of a Special Session of the CONTRACTING PARTIES shall decide regarding the international implementation of the respective results".

<sup>196</sup> For a summary of the Indian and Brazilian statements in the Group of Negotiations on Services on 25 February 1987, see C. Raghavan, "Trade: Services negotiations start", Special United Nations Service No. 1664, 3 March 1987.



reference outside GATT, as well as in achieving a balanced objective for the negotiations on trade in services, i.e. the promotion of economic growth of all trading partners and development of the developing countries through the expansion of trade in services under conditions of transparency and progressive liberalization. Hence, the objective of development

as provided in the Ministerial Declaration was an integral part of the General Agreement on Trade in Services (GATS). During the seven years of negotiations on trade in services the developing countries had to negotiate forcefully to preserve the balance achieved at Punta del Este in Part II of the Ministerial Declaration.

### C. The Group of Negotiations on Services

The Group of Negotiations on Services (GNS) adopted a plan for the initial stages of the negotiations,<sup>197</sup> during which the following five "elements" were addressed:

- definitional and statistical issues;
- broad concepts on which principles and rules for trade in services, including possible disciplines for individual sectors, might be based;
- coverage of the multilateral framework for trade in services;
- existing international disciplines and arrangements;
- measures and practices contributing to or limiting the expansion of trade in services, including participants, to which the conditions of transparency and progressive liberalization might be applicable.

These elements provided the framework for negotiations until the Montreal Mid-Term Review.<sup>198</sup>

At the Montreal Mid-Term Review meeting in December 1988, Ministers adopted a set of guidelines for removing many of the obstacles encountered in the GNS. In particular, it was agreed that work would proceed on a definition of trade in services, with a recognition of a series of principles that excluded right of establishment. The definition arrived at was flexible enough to include those services the delivery of which required the movement of factors of production across borders, i.e. trade in services involving the cross-border movement of services, of consumers and of factors of production where such movement is essential

to suppliers. It was decided that this issue should be examined further in the light of, *inter alia*, the following: (a) cross-border movement of services and payments; (b) specificity of purpose; (c) discreteness of transactions; and (d) limited duration. This agreement was a major compromise between the positions of the developed and the developing countries, allowing negotiators to include some cross-border movement of both capital and labour for the delivery of their services.

At its April 1989 meeting, the Group decided that the sectoral examination would begin with the telecommunications and construction sectors, followed by transportation, tourism and financial and professional services. Subsequently it initiated the process of "sectoral testing" envisaged in Part II, paragraph 6, of the Montreal Decision (i.e. that before agreement was reached on the principles, concepts and rules of the multilateral framework for trade in services, their applicability and the implications of their application would be examined in the context of individual sectors and the types of transactions to be covered by the multilateral framework). The principles of transparency, progressive liberalization, national treatment, most-favoured-nation (MFN) treatment and non-discrimination, market access, increasing participation of developing countries, safeguards and exceptions, and the regulatory situation were also examined.

In December 1989 the Group concentrated on assembling the necessary elements for a draft that would permit negotiations to take place for the completion of all parts of the multilateral framework in compliance with paragraph 11 of the Montreal text.<sup>199</sup> At its meet-

<sup>197</sup> The Programme for the Initial Phase of Negotiations (MTN.GNS/5).

<sup>198</sup> The discussions culminated in the drafting of the Report to the Trade Negotiations Committee meeting at Ministerial level at Montreal in December 1988 which endeavoured to capture the progress made in the negotiations. The Report contained a significant amount of bracketed alternative wording, which enabled the participants to identify the concerns underlying national positions (MTN.GNS/21).

<sup>199</sup> The Group agreed on draft elements which were mostly in square brackets. Of particular interest was the bracketing in the 'Elements' document (MTN.GNS/28) of the provisions on increasing participation of developing countries, which had been agreed on at Montreal.

ing in January 1990, it adopted an ambitious timetable for completion of work on a draft framework by July of that year. The negotiations were held at two levels. One related to the framework agreement, while the other covered sectoral annotations. The sectoral examination addressed telecommunications, financial services, labour mobility, construction and engineering, transport, professional services, audiovisual services and tourism. Sectoral working groups were established to discuss sectoral specificities and to determine whether the particular characteristics of the sectors warranted a specific "annotation" to clarify the application of the general principles or to provide for certain derogations from them.<sup>200</sup>

The delegations of the United States, Brazil, Switzerland, the European Communities (EC) and Japan, among others, submitted draft texts on a multilateral framework to the GNS, and two joint proposals were put forward by 11 Latin American countries members of SELA and 7 Afro-Asian countries, respectively. On the basis of these submissions and the discussions of the GNS and the working groups, the Chairman of the GNS presented a draft General Agreement on Trade in Services to the Brussels Meeting in December 1990 on his own responsibility. The text made an important contribution to the negotiating process, since its structure, like its approach and contents, reflected some of the positions and proposals of the developing countries.

The various proposals submitted on the elements of the multilateral framework, some

of them of much more global scope than others, fell within a spectrum which had at one extreme a strict initial set of multilateral obligations providing for across-the-board access commitments. These included national treatment from which countries would invoke sector-specific and also very strict individual reservations (i.e. the "negative list"), while at the same time abiding by the general obligations in the accepted sectors with very few reservations. This approach, which could be described as a "marriage" of the OECD and GATT frameworks for liberalization of trade in services, is best exemplified in the United States proposal. At the other end of the spectrum is the model constituted by a multilateral framework of very general obligations within which specific market access objectives would be negotiated in the course of the long-term process of liberalization along the lines of the GATT itself (i.e. the developing countries' proposals, the "positive list" approach).<sup>201</sup>

The developing countries made several proposals with respect to the sectors under discussion, among which the annexes on telecommunications and labour mobility are of particular interest. These proposals are reflected to a great extent in the final text of GATS. The dual role of telecommunications as a service sector and a mode of delivery for many other services is now widely appreciated, largely due to the insistence of developing countries on this point and the two joint submissions by India, Egypt, Cameroon and Nigeria.<sup>202</sup> The first submission, entitled "Sectoral annotation on telecommunication ser-

<sup>200</sup> In September 1990, the GNS agreed that an open-ended ad hoc working group consisting of GNS negotiators and sectoral experts should meet, as from the second half of October, with a view to taking stock of the situation in the light of the conclusions reached in the working groups, and finalizing the draft texts of annexes or annotations where necessary. The discussions in the Ad hoc Working Group highlighted the lack of consensus among the participants, in particular with respect to universal coverage and the application of MFN.

<sup>201</sup> On 26 February 1990, a joint proposal concerning the structure of a multilateral framework for trade in services was submitted by a group of 11 Latin American countries (Brazil, Chile, Colombia, Cuba, Honduras, Jamaica, Nicaragua, Mexico, Peru, Trinidad and Tobago and Uruguay) (MTN.GNS/W/95), and on 4 May 1990 7 African and Asian countries (Cameroon, China, Egypt, India, Kenya, Nigeria and Tanzania (United Republic of)) submitted a 'Multilateral framework of principles and rules for trade in services' (MTN.GNS/W/101). The structure of the "Afro-Asian" text has considerably influenced the GATS text. The Afro-Asian text makes a clear distinction between what is of a general, mandatory character - obligations and commitments of the parties that would be applicable to all sectors and signatories upon the entry into force of the Agreement, as, for example, increasing participation of developing countries, progressive liberalization, MFN and transparency - and the market access and national treatment principles which are to be implemented through the negotiation of specific concessions at the sectoral and subsectoral levels and incorporated in Schedules of Concessions (i.e. the positive list approach). Market access would result from individual commitments and concessions negotiated in pursuance of long-term progressive liberalization. National treatment would be negotiated, and would not be automatically granted pursuant to market access. In the Afro-Asian submission, the development objective is clearly included in chapter II that contains the obligations and commitments of the parties, and is elaborated further throughout the text with the object of avoiding an approach similar to GATT Part IV, in which undertakings with respect to developing countries are of an exhortative character only. The notion that developing countries undertaking liberalization in service sectors of interest to developed countries should obtain reciprocal access concessions in sectors of export interest to them has also found its way into the draft framework agreement owing to the provisions of the developing countries' text.

<sup>202</sup> See also the United States' submission of 23 March on an annex on access to and use of public telecommunications transport services, the purpose of which is to obligate countries to provide access to public telecommunications transport networks for the conduct of business including intracorporate communications which are singled out and the provision of services covered by the framework. The following provisions of the annex are of particular interest.

vices", addressed the scope, coverage and sectoral peculiarities arising from the application of the multilateral framework to international trade in such services. The second submission, which was an annex to the framework agreement, covered telecommunications as a mode of delivery. The purpose of the separation between them was to ensure that the issue of the conditions of use of telecommunication services as a mode of delivery did not affect the market access commitments made in schedules, naturally to the extent of the existing telecommunication capabilities.

Of particular interest is also the annex on "Temporary movement of services personnel" proposed by Argentina, Colombia, Cuba, Egypt, India, Mexico, Pakistan and Peru, which endeavoured to set out in the form of concrete obligations the principles relative to movement of personnel as a mode of supply, as agreed in paragraphs 4 and 7(e) of the results of the Mid-Term Review. Nothing in the annex was intended to affect immigration laws

and regulations dealing with permanent residence, establishment or citizenship.

The Ministerial Meeting held at Brussels in December 1990 had before it a draft General Agreement on Trade in Services with numerous square brackets submitted by the Chairman of the GNS on his own responsibility, in addition to draft annexes on maritime transport services; inland waterway transport services; road transport services; air transport services; basic telecommunications services; telecommunications; labour mobility; audiovisual, broadcasting, sound recording and publishing services; guidelines and recommendations for negotiations on initial commitments, and a text on guidelines for the initial commitments. All the above-mentioned texts submitted at the Brussels Meeting<sup>203</sup> included areas of disagreement. However, at that meeting some countries indicated that they would be prepared to withdraw certain reservations to enable agreement to be reached on the multilateral framework.

## D. Post-Brussels negotiations

It was agreed at the TNC to resume negotiations on services on 8 April 1991 to discuss the following main subjects: schedules of commitments; implications of a services framework agreement on other Uruguay Round negotiations; elaboration of a more detailed indicative list of services sectors and subsectors than was presented by the GNS secretariat in 1989; investigation of the horizontal effects of an agreement on existing international agreements on services; presentation of an indicative timetable for future work and identification of specific tasks. The discussions were structured around three main pillars: the framework, initial commitments, and sectoral annexes. Negotiations on the Agreement focused on the MFN Article, in particular the extent to which

parties could exempt selected sectors from MFN application. On 28 June 1991, the GNS reached an agreement on the Guidelines for Negotiations on Initial Commitments.<sup>204</sup> Under the Guidelines, conditional offers would be submitted by 13 July 1991 and would specify the commitments parties would undertake with respect to Parts III and IV of the draft text, with an explanation of the regulations affecting international trade in services. The parties were expected to present initial requests by 20 September of that year. Work on the scheduling of commitments did not proceed as planned, however, and by November 1991 most countries had still not submitted their offers. In the context of the annexes progress was made on maritime services, telecommunications, finan-

Article 2 of the annex provides for a broad coverage as follows "This annex applies to any existing or new measure of a Party that relates to access to public telecommunications transport services, whether or not covered by the Framework Agreement....". Paragraph 2.5 of this Article specifically emphasizes the fact that the obligations of the Annex will not imply that intracorporate communications are or are not traded. Article 3.1 provides for broad access to and use of public telecommunications transport services "offered within or into the territory of the Party". In accordance with Article 3.6.7, use of public telecommunications transport services would "include the movement, storage, and processing of information by a person within and across the borders of the Party". Article 3.7.4 has some important implications in that it would forbid the host countries to condition access by demands to obtain licences or comply with regulation procedures the effect of which would be "to nullify or impair" benefits derived from the accession to this annex or the framework agreement. The Annex in 3.7.3 also forbids the conditioning of access by technical standards which go beyond the requirements necessary for network-harm-prevention.

<sup>203</sup> Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations (MTN.TNC/W/35/Rev.1), 3 December 1990, annex II.

<sup>204</sup> "Procedural guidelines for negotiations on initial commitments" (MTN.GNS/W/119), 2 July 1991.

cial services and labour mobility. Progress on the conclusion of the annexes and the submission of initial commitments were largely related to resolution of the MFN issues.

The Director-General of GATT, at a meeting of the TNC on 20 December 1991, submitted a Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations (known as the Dunkel Draft), which was a consolidated document that brought together the results of five years of negotiations.<sup>205</sup>

On 13 January 1992, the TNC agreed to use the Dunkel Draft as a basis of negotiations with the aim of closing the Uruguay Round as quickly as possible, and adopted a four-track approach for rapidly concluding the negotiations. Track two involved non-stop negotiations on initial commitments in services.<sup>206</sup> Following the TNC meeting the submission of specific commitments accelerated. The GNS continued its work on the remaining issues in

the framework agreement, in particular exemption from the MFN, and the annexes on transport and on financial services. The United States proposed to exclude maritime services from the agreement and to undertake specific MFN exemptions in various service industries, such as financial services, basic telecommunications and maritime and air transport services. Its position on services was related to the problems it faced in other areas of the Round, in particular agriculture, as well as to its disappointment with the initial commitments in many areas, notably audiovisual, basic telecommunications and financial services sectors. The EC had difficulty with the inclusion of the audiovisual sector in the specific commitments, and was not satisfied with the offers of the developing countries, particularly in the area of financial services, threatening to withdraw its own offers if the developing countries would not improve theirs. These issues formed the basis of the discussions throughout 1992 and 1993 until the adoption of the Draft Final Act by the TNC on 15 December 1993.

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## E. General Agreement on Trade in Services

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The General Agreement on Trade in Services (GATS) establishes a multilateral framework of rules and principles for trade in services with a view to the expansion of such trade under conditions of transparency and progressive liberalization and as a means of promoting the economic growth of all trading partners and the development of developing countries. The Agreement addresses the particular need to facilitate their increasing participation in international trade in services and the expansion of their service exports, *inter alia*, through the strengthening of their domestic services capacity and of its efficiency and competitiveness.

In addition to the specific provisions of the Agreement, there are some special features that merit recognition. First, the Agreement provides a mechanism under which developing countries can claim credit for liberalization undertaken in the services sector, i.e. they are entitled to seek improved access in respect of other benefits in return for the commitment to

liberalize in any particular service sector. Second, by establishing such commitments in a precise form and providing a detailed contractual framework for trade in services, developing countries become less vulnerable to bilateral pressures to liberalize, particularly in service sectors of interest to the more powerful trading partners. Third, if Article IV on Increasing Participation of Developing Countries is effectively implemented through the negotiation of commitments on access to technology, distribution channels and information networks, as well as liberalization of markets in sectors and modes of supply of export interest to them, it could help to strengthen the developing countries' domestic services capacity and its efficiency and competitiveness.

GATS is based on three pillars: (i) the Agreement containing basic obligations applying to all parties; (ii) the annexes addressing the specificities of individual service sectors and modes of supply and Article II Exemptions,

<sup>205</sup> Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations (MTN.TNC/W/FA), 20 December 1991.

<sup>206</sup> GATT document MTN.TNC/W/99.

which form an integral part of the Agreement under Article XXIX; and (iii) the schedules of specific commitments which should be annexed to the Agreement and form an integral part thereof in accordance with Article XX.

The Agreement contains six parts, 29 articles and eight annexes. The annexes deal with Article II Exemptions (i.e. derogations from the MFN clause), Movement of Natural Persons Supplying Services under the Agreement, Telecommunications, Negotiations on Basic Telecommunications, two annexes on Financial Services, Air Transport Services, and Negotiations on Maritime Transport Services. The

other relevant documents are the four Ministerial Decisions on Institutional Arrangements and on Certain Dispute Settlement Procedures, the Decision concerning Article XIV (b) and the Decision on Trade in Services and the Environment. In addition, there are Ministerial Decisions relating to continuation of Negotiations on Basic Telecommunications, Financial Services, Professional Services, Negotiations on Movement of Natural Persons, Negotiations on Maritime Transport Services, and the Understanding on Commitments in Financial Services. The main provisions of GATS of crucial interest to developing countries are elaborated on below.

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## F. Structure

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The structure of GATS clearly separates the general obligations and disciplines that would be accepted by all parties upon their signature of the Agreement, of which the most important is the unconditional MFN clause in Part II (also concerned with increasing participation of developing countries, transparency, business practices, etc.) from specific sectoral commitments with respect to market access, national treatment and additional commitments in Part III, which would be the subject of specific negotiations and included in Schedules of Commitments. The modalities of achieving progressive liberalization through rounds of negotiations and the kind of measures that should be specified in the schedules of commitments are dealt with in Part IV.

The overall structure of the multilateral framework has been an issue of vital importance in the negotiations and the clear separation achieved in GATS between general obligations and specific commitments was seen to be essential for the developing countries, as it meant that their adherence to the framework would not, in itself, involve granting access in any particular sector (see box 14). Instead, access commitments could be offered in the negotiation of the schedules of commitments with respect to those sectors or subsectors in which liberalization would be consistent with their development strategies (i.e. the positive list approach).

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## G. Scope and definition

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The definition of "trade in services" was a key issue in the negotiations on a framework agreement. It was important to agree on such a definition in order to determine the exact

scope of the rules and the possible overall balance of advantages that would emerge from the expansion of trade in services, which related to the implications of the definition on

## Box 14

## PROPOSALS BY DEVELOPING COUNTRIES

The present structure and key provisions of the GATS derive to a large extent from a proposal by a group of African and Asian developing countries, i.e. Cameroon, China, Egypt, India, Kenya, Nigeria and Tanzania (United Republic of) (MTN.GNS/W/101) and another by a group of 11 Latin American countries (Brazil, Chile, Colombia, Cuba, Honduras, Jamaica, Nicaragua, Mexico, Peru, Trinidad and Tobago and Uruguay (MTN.GNS/W/95)). The guiding principles which the developing countries succeeded in incorporating into GATS are as follows:

- The multilateral framework should be constitutionally separate from GATT. GATS is one of the pillars of the World Trade Organization and is linked to GATT 1994 and TRIPs only through the integrated dispute settlement mechanism, which allows cross-retaliation under certain specific conditions.
- The paramount objective of the framework was the development of developing countries. The second preambular paragraph reads as follows: "Wishing to establish a multilateral framework of principles and rules for trade in services with a view to the expansion of such trade under conditions of transparency and progressive liberalization and as a means of promoting the economic growth of all trading partners and the development of developing countries," and the fifth preambular paragraph states: "Desiring to facilitate the increasing participation of developing countries in trade in services and the expansion of their service exports including, *inter alia*, through the strengthening of their domestic services capacity and its efficiency and competitiveness".
- The framework should have universal coverage. Article I on scope and definition provides that the Agreement applies to measures affecting trade in all services.
- The unconditional MFN clause was needed to fully multilateralize the liberalization achieved under GATS. Article II of GATS achieves this goal with the possibility of exemptions in accordance with the Annex on Article II Exemptions, and Article V on Economic Integration.
- Participation of developing countries should be based on the principle of relative reciprocity/development compatibility, and not be seen as "special treatment" along the lines of GATT Part IV. Article IV on Increasing Participation of Developing Countries and Article XIX:2 on Negotiation of Specific Commitments provide flexibility for the developing countries in liberalizing trade in services and attaching conditions to market access aimed at achieving the objectives established in Article IV. Developed countries are called upon to facilitate the participation of developing countries in trade in services through negotiated specific commitments relating to the strengthening of their domestic services capacity through access to technology, distribution channels and information networks, and market information, and the liberalization of market access in sectors and modes of supply of export interest to them.
- The movement of labour as a mode of supply should be included in the framework. Article I:2 (b) and the Annex on Movement of Natural Persons Supplying Services under the Agreement establish that temporary movement of natural persons is one of the four modes of supply of services.
- The adoption of the "positive list" approach comparable to Article II of GATT rather than the "negative list" approach applied by the OECD instruments, which provide for across-the-board access commitments, subject to reservations. The "positive list" approach has been adopted as the mechanics of liberalization in the GATS structure (i.e. the separation of general obligations that would be accepted by all parties upon their signature of the framework in Part II from the market access and national treatment provisions in Part III that would be the subject of specific negotiations. This means that each country can strategically select the individual service sector or transaction that it is willing to open up at a given time, subject to specific conditions and limitations. Market access would result from individual commitments negotiated in pursuance of long-term progressive liberalization, and national treatment would be negotiated and not automatically granted pursuant to market access.
- Developing countries should not be requested to make future concessions unless they would be able to derive meaningful benefits from the framework. Article XIX:3 provides for an assessment of trade in services in overall terms and on a sectoral basis with reference to the objectives of GATS, including those set out in paragraph 1 of Article IV for the purposes of establishing negotiating guidelines.

## Box 14 (concluded)

- Provisions on anti-competitive activities of transnational corporations in the Afro-Asian proposal have influenced Article IX on Business Practices. Although this Article only provides for consultation and exchange of information it is a general obligation of GATS.
- Developing countries should be able to regulate their services sectors, and standardization of national laws and regulations should not be sought. The fourth preambular paragraph of GATS recognizes the right of members to regulate, and to introduce new regulations on, the supply of services within their territories. In order to meet national policy objectives, and given the existing asymmetries with respect to the degree of development of services regulations in different countries, it recognizes the particular need of developing countries to exercise this right. Article VI on Domestic Regulation requires members to ensure that all measures of general application in sectors where specific commitments are undertaken are administered in a reasonable, objective and impartial manner.
- Provisions on emergency safeguard measures and restrictions to safeguard the balance of payments were included in the Afro-Asian draft. Article X on Emergency Safeguard Measures provides for future negotiations in this area and Article XII on Restrictions to Safeguard the Balance of Payments recognizes that particular pressures on the balance of payments of a member in the process of economic development or economic transition may necessitate the use of restrictions to ensure, *inter alia*, the maintenance of a level of financial reserves adequate for the implementation of the relevant programmes. Moreover, in determining the incidence of such restrictions, members may give priority to the supply of services which are more essential to their economic or development programmes.
- The dual role of telecommunications as a sector and as a cross-border mode of delivery should be recognized. The purpose of this separation is to ensure that the conditions of use of telecommunications services as a mode of supply do not impair the market access commitments made in the schedules to the extent of existing telecommunications capabilities, and that liberalization in any sector, including telecommunications, should only result from negotiated commitments in the specific sector or transaction included.

coverage.<sup>207</sup> Thus one of the major achievements was to negotiate a definition of "trade in services" (see box 13).

There are still some questions on the scope of GATS that remain to be settled, for example on governmental measures such as those relating to social security. This has relevance for the scheduling of such measures and for the question of MFN exemptions. Pending clarification of this and other matters relating to the scope of the Agreement, the participants have been urged to refrain from taking issues arising in this area to dispute settlement but to try to settle them through bilateral consultations instead. However, participants must assume the responsibility for deciding whether any measure of this sort which is in force in their countries should be scheduled or made the subject of MFN exemptions. They are expected to show restraint concerning the inclu-

sion of these measures in their MFN exemptions. These issues are now being discussed at the Sub-Committee on Services established by a Ministerial Decision at Marrakesh. The types of measures referred to in this regard relate to: (i) social security, including those measures pursuant to bilateral agreements on the avoidance of double contributions to, and/or double benefits from, social security systems; (ii) settlement of disputes pursuant to bilateral investment protection agreements; (iii) entry and stay of natural persons including those pursuant to international agreements on labour mobility; and (iv) entry and temporary stay of natural persons pursuant to bilateral agreements on entry and temporary stay of agricultural workers on a seasonal basis, working holidays and programmes for young workers, programmes for the exchange of university professors and school teachers, and cultural affairs.<sup>208</sup>

<sup>207</sup> In terms of empirical analysis, a service can be defined as an act which is the result of a productive activity and whose effect is to change the status or position of a beneficiary. The service output is not distinguishable from its production process and the result or effect of the service is inseparable from its beneficiary and cannot form the subject of a new transaction. Accordingly classifications of services are classifications of activities, since the nature of various service activities can be described, and not classifications of products which are difficult to define and measure. For further details see *Trade and Development Report, 1988*, Part Two, "Services in the world economy".

<sup>208</sup> For further details, see GATT document MTN.GNS/W/177/Rev.1.

## Box 15

## DEFINITION OF TRADE IN SERVICES

GATS has universal coverage and applies to measures by members affecting trade in services, whether in the form of a law, regulation, rule, procedure, decision, administrative action, or any other form. Measures by members include (i) the purchase, payment or use of a service; (ii) the access to and use of, in connection with the supply of a service, services which are required by those members to be offered to the public in general; and (iii) the presence, including commercial presence, of persons of a member for the supply of a service. The definition is therefore formulated in such a way to cover any measure that affects trade in services in any sector. Services comprise any service in any sector, except services supplied in the exercise of governmental authority. The definition finally included in GATS derives from the endeavour to identify the essential attributes of a service transaction so that it could be considered to constitute trade in services. The definition includes the movement of factors of production as well as of consumers. The spectrum of international service transactions includes investment and labour. This definition therefore goes well beyond the commonly used statistical concept of transactions between the residents of a country and non-residents, and includes the operations of foreign suppliers in domestic markets in addition to imports. The services sectoral classification list of the GATT secretariat (MTN.GNS/W/120), which has been used by the participants for drawing up their schedules of commitments, contains a list of 11 services sectors and 155 detailed subsectors.

For the purposes of GATS, trade in services is defined as the supply of a service through four modes of supply, namely, cross-border supply, consumption abroad, commercial presence and presence of natural persons suppliers of services. It consequently establishes that the movement of persons constitutes trade in services and is an appropriate subject for the negotiation of trade concessions. This is clearly an innovation of significant importance for developing countries. Such a wide definition of trade in services may lead to complications in future when the origin of the service traded has to be determined, given the impact of globalization and the nature of trade through establishment, which makes the application of notions of ownership and control more difficult. Article XXVIII on Definitions provides, *inter alia*, that a juridical person is "owned" by persons of a member if more than 50 per cent of the equity interest in it is beneficially owned by persons of that member. It is of interest to note that many of the offers under commercial presence contain less than 50 per cent equity which would mean that the juridical person established would be considered as domestic.

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## H. Most-favoured-nation treatment

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The major issue that has been settled in Article II of GATS is that MFN treatment is unconditional and is to be treated as a general obligation. Developing countries had been concerned that a "conditional" clause might have been included, which would have meant that they would not benefit from the concessions of GATS if they did not accept a certain level of liberalization. Article II.2. does, however, provide for certain exceptions from this obligation, governed by the criteria of the Annex on Article II Exemptions. As regards MFN exemptions, members are allowed to benefit from an exemption for a period of not more than 10 years, with a review requirement

after five years, although the possibilities of exemption are rather broad. MFN would not apply either to economic integration agreements that fulfil the conditions of Article V or to government procurement under Article XIII. The adoption of the unconditional MFN obligation will provide export opportunities in many sectors even if specific commitments on market access and national treatment have not been entered in the schedules, given that many participants already have relatively open markets. The benefits of existing preferential treatment, including under bilateral investment or friendship and commerce treaties, although excluding the preferential treatment included in



the integration arrangements justified under Article V, will have to be extended to others if they are not exempted.

In certain cases, however, such as basic telecommunications, financial services and maritime transport services, some participants, whose markets in these sectors are liberalized, when confronted with closed markets have entered exemptions to MFN treatment as a way of achieving greater reciprocity within these same sectors, and to meet their concern about

the loss of negotiating leverage once the unconditional MFN obligation applies to the sectors in question. Negotiations in the three sectors will continue, at the conclusion of which participants will decide whether to maintain or enter MFN exemptions. The fact that some of the MFN exemptions entered are couched in terms that would cover future measures as well confirms that attempts made to ensure a certain degree of sector-specific reciprocity have been relatively successful.

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## I. Increasing participation of developing countries

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Through the inclusion in GATS of a clear obligation on "increasing participation of developing countries" (Article IV), the developing countries have obtained recognition in the Agreement of the basic "asymmetry" in the situation of services in developed and developing countries and a commitment that the developed countries will take concrete measures aimed at strengthening the domestic services sectors of developing countries and providing effective market access for their exports, while the developing countries themselves will pursue this objective through the imposition of conditions on foreign suppliers in return for market access. This also permits developing countries undertaking liberalization in service sectors of interest to developed countries to seek reciprocal access concessions in sectors of export interest to them.

Article IV becomes operational through the specific terms of Article XIX on Negotiation of Specific Commitments in Part IV (Progressive Liberalization). Article XIX:2 provides that the process of liberalization will take place with due respect for national policy objectives and the level of development of individual parties, both overall and in individual sectors. There will be appropriate flexibility for individual developing countries for opening fewer sectors, liberalizing fewer types of transactions, progressively extending market access in line with their development situation and,

when making access to their markets available to foreign service suppliers, attaching to it conditions aimed at achieving the objectives referred to in Article IV.

The inclusion of this Article is important in that it recognizes the legitimacy of measures taken by developing countries to strengthen their services capacity, etc., such as imposing transfer of technology or access to network conditions on foreign services suppliers, or employment requirements, or applying other national policy measures for this purpose, including the possibility of subsidizing their services sector. In providing access to their markets for foreign service suppliers, some developing countries have attached conditions to access in their Schedules of Specific Commitments, such as limitations or requirements with regard to the type of commercial presence, e.g. joint venture requirements, or general criteria for authorization to deliver services through commercial presence, which would ensure development of competitive services sectors;<sup>209</sup> minimum requirements for training and employment, e.g. a specific number of directors to be nationals, effective control of the enterprise by the domestic shareholders, training of local employees and employment of domestic subcontractors; local content requirement, e.g. a certain percentage of screen time in private film screening must be devoted to domestic films or advertisements (80 per cent local content); sur-

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<sup>209</sup> An example of criteria for the grant of commercial presence from the Schedule of Commitment of Chile is as follows: (i) the effect of commercial presence on economic activity, including the effect on employment, on the use of parts, components and services produced domestically and on exports of services; (ii) the effect of commercial presence on productivity, industrial efficiency, technological development and production innovation; (iii) the effect of commercial presence on competition in the sector concerned and other sectors, on consumer protection, on the smooth functioning, integrity, and stability of the market, and on national interest; (iv) the contribution of commercial presence to integration in the world markets.

charges and different tax rates, e.g. a duty-free system with exemption from import duties applicable only to domestic producers; access to technology, e.g. a foreign service supplier should use appropriate and advanced technology, equipment and managerial experience and be under the obligation to transfer its technology and pass on its experience to the domestic personnel - the build-transfer-operate concept; information regarding operations, e.g. a foreign service provider must furnish accurately and promptly reports on operations including technological, accounting, economic and administrative data.

Moreover, Article IV provides for the establishment of contact points to facilitate access to information on commercial and technical aspects of the supply of services, registration, recognition and obtaining of professional qualifications, and the availability of service technology. The establishment of such contact points would help developing countries to obtain the relevant information to be able to access markets. These countries, however, have to establish the necessary institutional and administrative framework to manage this information and to bring it promptly to the attention of their service suppliers.

It should be noted, however, that paragraph IV:1 as it stands remains a statement of good intentions in providing that "The increasing participation of developing country members in world trade shall be facilitated through negotiated specific commitments, by different members pursuant to Parts III and IV of this Agreement, relating to: (a) the strengthening of their domestic services capacity and its efficiency and competitiveness, *inter alia*, through access to technology on a commercial basis; (b) the improvement of their access to distribution channels and information networks; and (c) the liberalization of market access in sectors and modes of supply of export interest to them."<sup>210</sup> India has included in its horizontal commitments on commercial presence the condition

that, in a joint venture with an Indian public sector enterprise or a government undertaking, preference will be given to foreign service suppliers that offer the best terms for transfer of technology.

The significance of information networks and distribution channels for the maintenance of a competitive position in international trade in services is dramatically apparent in many service sectors. Information technology is both a service in itself and an essential element to facilitate the internationalization of many other service activities. Information technology and transborder data flows have been used to establish networks and distribution channels for services that could act as a barrier to the market entry of developing countries. Entry barriers can, however, be lowered where the public telecommunication infrastructure is used to market or distribute services, especially when access to, and the cost of, the network is shared by all users. Access to such networks can be a determining factor not only in trade in services but also for providing services essential to trade in goods.<sup>211</sup> The extremely uneven distribution of the systems and infrastructure necessary to increase the productivity of transport services to the world markets is a major impediment to increasing exports of services of the developing countries, in particular financial services, audiovisual services, software services, professional services and tourism services. In the tourism sector, which is traditionally considered a sector of interest to developing countries, primarily because balance-of-payments figures show that developing countries are running large surpluses in tourism, world-wide tourist revenues are dominated by developed country firms that have been able to establish networks, i.e. hotel chains, travel agencies and computer reservation systems (CRS). The CRSs are a striking example of the importance of information networks. Even the major airlines have found it necessary to link up to maximize the profitability of information networks (i.e. CRSs, which have themselves become a significant

<sup>210</sup> The language of this paragraph has been further weakened since the Brussels Meeting in that the present text uses the word 'negotiated' in the second line and the list is now definitive and no longer open-ended. Moreover, the reference to access to technology has been removed from 1(b) and in 1(a) has been weakened by the words "on a commercial basis".

<sup>211</sup> Examples of these networks are Primex offered by British Telecom to link European facilities and Transpac offered by France Telecom. Private firms are also offering value-added network services such as MCI, the United States long distance carrier, which offers a wide range of network services including (i) Commax, an agreement with Japanese and telecommunications companies to offer voice, data and messaging services between Japan, the United States and the United Kingdom; (ii) Infonet, which provides global services including electronic data interchange (EDI), electronic mail and virtually private networks, owned in conjunction with 10 other telecommunications operators in Europe and the Pacific rim; (iii) Financial Services Association, which is a joint venture with a number of telecommunications companies from Belgium, France, Italy, the Netherlands, Spain and other countries to provide specialized communications services to the global financial services industry; and (iv) Global Communications Services, a one-stop shopping agreement involving 20 other operators. For more information, see Ken Ducatel and Ian Miles, "Internationalization of information technology services and public policy implications", *World Development*, 20 December 1992, pp. 1844-1857.

source of profit) and distribution channels, i.e. routes. In air transport, the distribution channels can be expanded only through difficult bilateral negotiations, and profitability depends on linking up and sharing the existing channels and information networks. The anti-competitive behaviour of CRSs has been the subject of special legislation in both the EC and the United States, as well as of an ICAO Code of Conduct. In media services, the control of distribution channels permits the producer of a film to control the timing of its presentation - a vital component of the value of the production - as well as to ensure a market for its products and its technology. The competitive position of developing country service suppliers would be greatly enhanced by the development of public R&D networks, for example, along the lines of ESPRIT in Europe, at the world level.<sup>212</sup>

The question of the effective transfer of technology is of the utmost importance in the development of services capacity. Some developing countries have ensured that, if they include in their specific commitments the commercial presence of foreign-controlled entities in particular services subsectors, and the temporary entry of key personnel for such entities, efforts would be made to train local per-

sonnel and that they would be given access to state-of-the-art technology through the incorporation of the various conditions regarding measures to ensure an adequate transfer of technology in individual country subsector lists of commitments.

With respect to the least developed countries, the Preamble, paragraph 3 of Article IV, Article XIX:3, and the Decision on Measures in Favour of Least-Developed Countries provide that particular account shall be taken of their serious difficulties and that they will be required to undertake commitments and concessions only to the extent consistent with their individual development, financial and trade needs, or their administrative and institutional capabilities. The least developed countries are given an additional period of one year from the date of the Special Ministerial Meeting concluding the Uruguay Round of Multilateral Trade Negotiations to submit their schedules as required in Article XI of the Agreement Establishing the WTO. It should be noted that implementation of the general disciplines and obligations of GATS would in itself be a major commitment on their part. Moreover, despite their serious economic difficulties, most of the least developed countries have submitted their Schedules of Commitments.

## J. Economic integration

Article V on Economic Integration is similar to Article XXIV of GATT in requiring arrangements to have substantial sectoral coverage and to provide for the absence or elimination of substantially all discrimination among members.<sup>213</sup> Paragraph 3 of Article V provides for developing countries to have flexibility with respect to the conditions to be fulfilled for such agreements to be acceptable under the provisions of GATS. These conditions are substantial sectoral coverage (in order

to meet this condition, agreements must not *a priori* exclude any mode of supply); and absence or elimination of substantially all discrimination in the sense of Article XVII on National Treatment. Article V:6 provides that a service supplier of any other member that is a juridical person constituted under the laws of a party to an agreement on economic integration and liberalization of trade in services shall be entitled to treatment granted under such agreement, provided that it engages

<sup>212</sup> See UNCTAD, "A comparative analysis of services sectors in developing countries" (TD/B/CN.4/23), August 1993, prepared under item 3(a) of the work programme of the Standing Committee on Developing Services Sectors. Part Two of the document highlights access to information networks and distribution channels as a major difficulty which must be surmounted by developing countries if they are to increase their share of world service trade. See also UNCTAD VIII: *Analytical Report by the secretariat to the Conference* (TD/358) (United Nations publication, Sales No. E.92.II.D.3), 1992, chap. IV, and "Access to networks and services trade: The Uruguay Round and beyond" in *Trade in Services - Sectoral Issues* (UNCTAD/ITP/26), 1989.

<sup>213</sup> At the Marrakesh Ministerial Meeting, suggestions were made that the existing provisions in GATT are not sufficiently specific and transparent to provide criteria for acceptable forms of regional integration and that the WTO should discuss this issue in greater detail with the aim of specifying the rules for free trade agreements and customs unions that would serve as a supplement to and strengthen the multilateral regime.

in substantive business operations in the territory of the parties to such agreement. Notwithstanding this provision, in the case of an economic integration agreement involving only developing countries, more favourable treatment may be granted to juridical persons owned or controlled by natural persons of the parties to such an agreement.<sup>214</sup> Some of the existing integration agreements such as the European Union, the European Economic Area (EEA), the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA), the North American Free Trade Agreement (NAFTA), the Southern Common Market (Mercosur), the Chile-Mexico Agreement on Economic Cooperation, the Caribbean Community (CARICOM), the Latin American Integration Association (ALADI), the Andean Group (GRAN), the

Gulf Cooperation Council (GCC), the African Economic Community (AEC), the Arab Maghreb Union (AMU) and the Economic Community of West African States (ECOWAS) include services. Most of the developing countries' integration agreements cover liberalization of services in principle, but have not operationalized such goals by adopting the modalities of freeing movements of capital and labour. Progress towards liberalizing or establishing free trade in service under these agreements has proved difficult because of the differentiated and highly regulated nature of services, but recent initiatives have been successful.<sup>215</sup> The emphasis therefore remains on the development and strengthening of infrastructural networks among member countries.

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## K. Monopolies and exclusive service providers and business practices

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Article VIII of GATS contains strict provisions on the operations of monopolies. These provisions stipulate, *inter alia*, that: "Each Member shall ensure that any monopoly supplier of a service in its territory does not, in the supply of the monopoly service in the relevant market, act in a manner inconsistent with that Member's obligations under Article II and specific commitments". Comparable provisions have not been included with respect to the treatment of restrictive business practices (RBPs) and other anti-competitive practices of private corporations. Although it has been an achievement to secure the inclusion of Article IX on Business Practices which, in paragraph 1, states that: "Members recognize that certain business practices of service

suppliers, other than those falling under Article VIII, may restrain competition and thereby restrict trade in services", there is no specific obligation to eliminate these practices. On anti-competitive behaviour of business operators, Article IX only provides for consultations, cooperation and exchange of information. The provision on the behaviour of private operators could be interpreted by enterprises as a clear indication that there is no determination on the part of governments to deal with anti-competitive practices. For example, in spite of the concern expressed in the United States about dumping of banking services (*inter alia*, during hearings of a Congressional Subcommittee)<sup>216</sup> no explicit reference to the subject is included in GATS.

<sup>214</sup> The latter provision, which grants some flexibility to developing countries, was not included in the Dunkel Draft. Paragraph 6 of that text, however, included a subparagraph providing that "A Member that is a party to such an agreement may refuse to grant the treatment referred to in sub-paragraph (a) above, if: (i) the service supplier was not established in the territory of a party to such agreement prior to signature of the agreement; and (ii) the parties to such agreement do not provide common treatment to third countries with respect to the sector concerned." The deletion of this subparagraph implies that the juridical person could be established before or after the entry into force of the integration agreement.

<sup>215</sup> See UNCTAD secretariat documents circulated under item 3(j) of the work programme of the Standing Committee on Developing Services Sectors, e.g. TD/B/CN.4/Misc.4. It should be noted that a preferential service area, with a defined market and technological resource base, could facilitate the development of an efficient and competitive regional services supply. Furthermore, it could help service firms from the region or subregion to strengthen their competitive position with respect to third countries.

<sup>216</sup> Uruguay Round Negotiations on Financial Services, Hearing before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance Task Force on International Competitiveness of U.S. Financial Institutions of the Committee on Banking, Finance and Urban Affairs, House of Representatives, One Hundred First Congress, Second Session, 17 July 1990 (Washington, D.C.: U.S. Government Printing Office, 1991), pp. 21-22, 32, 34, 36, 38-40 and 68.

So-called "club arrangements" such as groupings or associations with responsibility for clearance, payments and settlements or quotation and dealing are potential vehicles for restrictive business practices against outsiders, including foreign banks. The need to ensure that such arrangements do not discriminate against foreign banks is specified in section C on National Treatment in the Understanding on Commitments in Financial Services. But it is not clear why obligations regarding the practices of "club arrangements" should be limited to parties choosing to schedule their commitments according to the Understanding. Indeed, there would appear to be a case for including such obligations in GATS.

For a number of service sectors, international trade is distorted by anti-competitive

practices and it would be difficult for more vulnerable developing countries to include such sectors in their schedules in the absence of more stringent disciplines. A clear obligation for the control of anti-competitive practices, as foreseen in submissions by developing countries, which provided that parties should take all possible measures, by legislation or otherwise, to ensure, within their jurisdiction, that service suppliers do not engage in unfair trade practices and that international standards and disciplines for the control of adverse trade effects of anti-competitive behaviour, and a multilateral mechanism to enforce such standards and disciplines, could preserve a further liberalization of trade in services. At present, discussions are taking place on the inclusion of competition policy in the agenda of a new round of multilateral trade negotiations.<sup>217</sup>

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## L. Safeguards

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Developing countries have stressed that any safeguard clause in the multilateral framework should enable them to take safeguard action not only for balance-of-payments reasons, but also to deal with adverse trade effects caused by situations of concentration of ownership, market domination and restrictive business practices (as the possibility of such a situation arising might have been completely unforeseen when the market access conditions were initially negotiated), as well as to permit the creation of services sectors, the protection of infant industries, and the correction of structural problems.

Article X of GATS on Emergency Safeguard Measures provides for negotiations on a safeguards clause based on the principle of non-discrimination, with the results of such negotiations entering into effect not later than three years from the date of entry into force of the WTO Agreement. In the period before the results enter into force, any member may modify or withdraw its concessions after a period of one year, notwithstanding the three-year period stipulated in Article XXI:1, provided that

the member shows cause that the modification or withdrawal cannot await the lapse of the three-year period. The reasons for the need for such modification or withdrawal are not stipulated in the Article.

One of the difficulties faced by participants in the negotiations on obligations in this area is that such obligations would be related to judgements on import penetration and the related economic impact of service imports for which few criteria for measurement exist. The concepts and criteria in the Agreement on Safeguards included in the Final Act, such as how to measure increased imports and serious injury or threat thereof and to impose quotas and surcharges, could be difficult to apply to services. There is therefore a need to explore these difficulties and the potential applicability of the provisions of the Safeguards Agreement to services.<sup>218</sup>

The manner in which the negotiations took place further complicated the consideration of the safeguards issue, since the initial commitments were negotiated at the same time

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<sup>217</sup> It should also be noted that there are no provisions for "anti-dumping" measures in GATS.

<sup>218</sup> The Peruvian proposal contained in document MTN.GNS/W/74 could be used as a basis for drawing up provisions on temporary derogations.

as the Agreement. Consequently, there seems to have been a tendency to build self-contained safeguards into the initial lists. It would appear, however, that the main concern in drawing up a safeguard clause should be to avoid incorporating those aspects of GATT Article XIX that have proved unworkable or subject to abuse into the services framework. Some of them might be avoided, if there were a clear understanding from the very beginning as to what situations justified recourse to safeguards measures, and what measures were appropriate,

perhaps through an indicative list. It should be noted that the Agreement on Safeguards does tackle many of the problems posed by Article XIX.

The Agreement on Safeguards provides that members applying safeguard measures should endeavour to maintain a substantially equivalent level of concessions, and to achieve this objective the members concerned may agree on any adequate means of trade compensation for the adverse effects of the measures on their trade.<sup>219</sup>

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## M. Payments and transfers

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The right of countries to exercise control over international capital movements was a central issue in the negotiations, as it was the subject of considerable pressure by developed countries for relaxation as part of the process of opening up economies to cross-border financial transactions, many of which would be classified as payments for the purpose of transferring capital according to the definition provided by Article XXX(d) of the IMF Articles of Agreement. During the negotiations OECD countries submitted proposals which would have required the removal of restrictions on payments for the purpose of cross-border transfers of capital. GATS, Article XI:2 provides that "...a Member shall not impose re-

strictions on any capital transactions inconsistently with its specific commitments regarding such transactions, except under Article XII or at the request of the Fund". This provision is intended to ensure that restrictions on capital movements do not frustrate concessions with respect to commercial presence; however, they should not impede the developing countries' policy autonomy regarding control of international capital movements. Nevertheless, under Article XVI, if a country undertakes a commitment whose realization presupposes cross-border movements of capital, then it must also allow the movements required for this purpose.

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## N. Government procurement

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Article XIII:1 of GATS on Government Procurement states that "Articles II, XVI and XVII shall not apply to laws, regulations or requirements governing the procurement by

governmental agencies of services purchased for governmental purposes and not with a view to commercial resale or with a view to use in the supply of services for commercial resale".

<sup>219</sup> A temporary waiver provision, similar to the provision contained in the Agreement on Safeguards, Article 11:2, which is limited to one measure per importing member for a period not exceeding four years, could be drawn up for countries wishing to take safeguard action without resorting to Article XXI provisions and compensation. Negotiation of the safeguard provisions could be based on the experience gained in the operation of this waiver provision. Consideration could also be given to provisions on quantitative restrictions since in many services sectors these restrictions are applied to prevent injury to domestic producers and to control entry into the market. It should also be noted that the notion of equivalent level of concessions will have to be clarified in trade in services, in particular in terms of defining objective indicators to evaluate what could be considered as 'equivalent'.

The question of rules on government procurement are left for future negotiations to be completed two years after the date of entry into force of the Agreement Establishing the WTO. A lack of rules in this area could create uncertainties with respect to a major issue in trade in services in that government contracts are extremely important in certain sectors (e.g. construction) and the absence of provisions could create distortions in trade in services.

The Agreement on Government Procurement, which is in Annex 4 of the Agreement Establishing the WTO, is a revision of the Tokyo Round Code. However, being a plurilateral agreement it will be applicable only to its signatory countries.<sup>220</sup> The Agreement extends the scope of international competition in this area to cover services for the first time, including construction services, and procurement at sub-central level. Annexes 4 and 5 of the Agreement define the services and construction services whose procurement by the entities covered is subject to the rules of the Agreement. As national treatment and non-discrimination are the cornerstone of the rules, foreign suppliers and foreign goods and services

should be given no less favourable treatment in government procurement by the covered entities than national suppliers and goods and services. There is also provision for special and differential treatment of developing countries, the objective of which is to take duly into account the development, financial and trade needs of the developing countries in order to safeguard their balance of payments; promote the establishment or development of domestic industries; support industrial units so long as they are wholly or substantially dependent on government procurement; and encourage their economic development through regional or global arrangements among developing countries. To implement these objectives the developed countries should endeavour to include entities procuring products or services of export interest to developing countries. Moreover, certain mutually acceptable exclusions from the rules of national treatment may be granted to the developing countries, although as Hong Kong and Singapore are not participating in the new Code, the only non-OECD participant is Israel. This expanded Agreement will influence the future negotiations on government procurement under GATS.

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## O. General exceptions

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Article XIV on General Exceptions was the subject of considerable discussion at the very end of the Round, owing to the problems that the European Communities (EC) faced in the audiovisual sector (see box 16) and the United States' concerns as regards national treatment for taxation. The EC had made proposals to insert language regarding the cultural exception into Article XIV of GATS or to include language on the cultural specificity of the audiovisual sector in certain other GATS provisions (Article XIX on Progressive Liberalization, Article XV on Subsidies and the Annex on Article II Exemptions). Finally, owing to the reservations expressed by other participants, the EC has included its agreements on the audiovisual sector in its MFN exemptions and has not included the sector in its offers.

In view of the concerns of the Treasury and Internal Revenue Services in the United States about interference in matters of taxation as a result of GATS Article XVII on National Treatment, the United States proposed to include in its Schedule of Concessions a horizontal limitation on national treatment covering all forms of direct taxation. Other participants in the Round believed that to grant such an exception on national treatment could render the United States' offers meaningless. To meet the concerns of the Treasury, Article XIV(d) contains a footnote elaborating on the type of measures aimed at the equitable or effective imposition or collection of direct taxes and a definition of direct taxes. The list of these measures is only illustrative.<sup>221</sup> The listing in the footnote of types of measures which governments may find it necessary to take is without

<sup>220</sup> Committee on Government Procurement, "Agreement on Government Procurement" (GPR/74), 6 January 1994.

<sup>221</sup> For further clarification on this issue, see GATT documents MTN.GNS/W/178 and Add. 1, MTN.GNS/W/210 and MTN.GNS/49.

## Box 16

## AUDIOVISUAL SERVICES

In the final stage of the Uruguay Round negotiations on trade in services, a stand-off developed on audiovisual services between the European Communities and the United States. This had its origins in the rise of commercial television broadcasting in Europe. In a process which initially began as a result of court rulings in Italy, during the 1980s government television monopolies were dissolved across Western Europe, commercial broadcast licences were granted and government broadcast entities were wholly or partially privatized in country after country. By 1990, the number of television channels available in EC countries had increased from 36 to 125, the obvious consequence being an explosion in the number of hours of broadcast time to be filled. Also, commercial operators were now free to bid competitively around the world for programme material, whereas government broadcasters had previously fixed - at modest levels - the prices they were willing to pay for purchased programming. That the United States, with the world's most highly developed commercial film and television industries, was in the best position to benefit from these developments was a foregone conclusion. The United States dominates world trade in audiovisual services, as far as media products such as films, television programmes and video productions are concerned, with an estimated 40 per cent of the market. However, the fastest growing market is the European Community, which has been estimated at ECU 23 billion and is expected to double by the year 2000. In 1992, United States exports of film and tape rentals, television programmes and recordings of live entertainment to the EC amounted to some \$3.6 billion against EC exports to the United States market of about \$ 290 million.<sup>1</sup>

This situation is perceived in Europe as an "invasion" of United States programming, owing to the sudden and unprecedented increase in demand unmatched by local productive capacity to fill it. Whereas the rising demand for programming in Europe has produced a significant increase in the importation of foreign (mainly United States) products, a similar rise in programming demand in the United States has not resulted in any increase in imports. In 1991, the United States' products accounted for almost 80 per cent of cinema screenings in the EC and for over half of all dramas and comedies broadcast on television whereas the percentage of foreign films on American television and theatre screens remains at an exceptionally low level (less than 2 per cent), although Latin American and Asian suppliers are beginning to make inroads.

The specific trade barriers most at issue were film subsidies and television quotas. Film production subsidies, which are nearly ubiquitous, have existed for decades and vary from country to country. France has the most substantial programme, levying an 11 per cent duty on box office sales which is funneled directly into film production support overseen by a national commission. (Revenues are also obtained by special taxes on video sales and rentals.) This system is widely credited with maintaining the viability of the French film industry, the most robust in Europe, which produces some 150 films annually, indeed, a larger number of films per capita than the United States.

In the final stages of the Uruguay Round negotiations in the autumn of 1993, it might have been thought that the status quo was proving relatively satisfactory to all parties. Film subsidies allowed European producers to assure the survival of artistically serious and culturally particular film-making. Television quotas were adopted EC-wide by a Community directive in September 1989 on "television without frontiers", which recommended a minimum of 50 per cent programming "of European origin" on all channels. Individual countries are permitted to adopt more stringent and specific standards. The EC quota system is voluntary and reportedly has never been enforced, as imported non-European programming has not risen above 30 per cent. Consequently, the quota system did not affect the current demand for United States television programming. The concern of the United States industry would appear to be for the future. The 1989 EC directive regarding television quotas was probably more alarming to that industry as a foretaste of communal action than for the particular strictures it laid down. In 1990, MEDIA (Measures to Encourage the Development of the Industry of Audiovisual production) was established in the existing EC countries plus Austria and Switzerland. MEDIA has established a venture capital fund (Media Venture) to help finance the production and distribution of high budget commercial films and television series, the European Film Distribution Office (EFDO) to sponsor worldwide distribution of European films, and a number of other divisions devoted to dubbing and subtitling (BABEL), script development (SCRIPT), and animation (CARTOON),



## Box 16 (continued)

among other endeavours. MEDIA was created to break out of the "cottage industry" syndrome in European filmmaking and build a commercial rival to the Hollywood model. It is realized that this is only conceivable on a Community-wide scale, not at the level of a single European State.

The audiovisual service sector is a fast growing economic activity benefiting from the rising demand for entertainment. Annual growth rates of around 10 per cent in real terms have been sustained even in the recent recessionary climate. Demand has been fuelled by technical progress, deregulation and privatization and increased leisure time. At the world level, the software side of the audiovisual industry had an estimated value of roughly ECU 120 billion in 1992. The power, scope and diversity of the new media technologies and regulatory transformation are providing a rapidly expanding choice of supply modes that is affecting the growth and development of the audiovisual industry. The new technologies provide stability in quality, multiplication of transmission possibilities, reduction of costs and creation of market overlap. Regulators are struggling to keep pace with these new media technologies and the multi-media alliances between telephony, broadcasting, computing and publishing. They are faced, in particular, with issues such as treatment of regulated monopolies, transition to open competition, ensuring a universal service, promoting the interests of domestic film and television programme industries, and tracking the transmission of audiovisual productions when no physical support is needed for such cross-border services.

Television technology is moving towards vastly increased channel capacity ("bandwidth"), interactive (or "switched") transmission networks, and new programme options such as video-on-demand and a vast array of "transaction" services such as home shopping, home banking, and so on. This emerging "information highway" will evolve gradually over time and incorporate a complex of delivery technologies such as satellites, fiber optic cables and advanced wireless devices. It is sometimes said that new technologies like digital broadcast satellite (DBS) transmission will "erase" national or even Community-wide boundaries and render quotas and other trade and regulatory obstacles obsolete. However, it is far from clear that this is true. As the number of channels and programme offerings expands, the market becomes more fragmented and it becomes increasingly necessary to supplement advertising revenues with subscriptions, pay-per-view and other fees. Even satellite system operators need a substantial on-the-ground presence (which may be provided by a third party) to establish service, do billing and collect fees. These activities will be just as subject to governmental oversight as any other terrestrial enterprise.

The control of distribution channels is of particular importance in the audiovisual sector. Many film and media producing companies are part of groups vertically integrated into the distribution and exhibition of films in cinemas. Close control over the sequence in which films are released, both geographically and temporally, among the media allows producers to maximize the earnings on their films. Access to distribution channels is made difficult for independent competitors, through various techniques. For instance, large distributors are in a position to decide which cinemas have the right to show a film first, and often impose 'block booking' which obliges the exhibitor to take and exhibit a given series of films (a practice prohibited on antitrust grounds in the United States). Control of distribution is also fundamental to maximize downstream revenue from video sales and television broadcast rights. An export cartel, Motion Picture Export Association of America (MPEAA), comprising 20th Century Fox, Columbia Tristar, Disney (Buena Vista), Paramount, Warner Bros., MCA Universal, Orion and MGM/UA is now present in 50 countries of the world. These firms also control the distribution of their films and aim at doing away with intermediaries in foreign markets<sup>2</sup> Importing countries have to face up to the market power of the MPEAA. By maintaining a highly effective joint marketing and distribution system in Western Europe, helped by control of a large number of cinemas, fewer than a dozen United States distributors take 80 per cent of the box office receipts in the EC, whereas the remaining 20 per cent is supplied by over 1,000 European distributors. For film makers, the cinema phase in the lifecycle of a feature film is important not in itself but because it determines the returns during the rest of the film's exploitation cycle in the form of videocassettes, pay-TV, video-on-demand and, finally broadcasting in the open. Hence, the all-out promotion campaigns of powerful feature film makers to get their products rapidly and widely accepted at the cinema-launching phase.

**Box 16 (concluded)**

A new world of strategic alliances, of co-production and co-financing of films, television programmes, electronic information and games, of joint shareholding in satellite launches and cable/telephony networks, distribution and even audience measurement, has come into being. Media conglomerates and small niche players in telecommunications, film and cable are teaming up with others in different parts of the world to meet the rising and diversifying demands of viewers.<sup>3</sup>

As a result of the emergence of the new information technologies the stakes may be higher than the image of television shows and motion pictures would immediately suggest. The national mandate for the "information infrastructure" as set forth by the United States Administration envisions these technologies as supporting and directly stimulating a large part of the industrial, scientific and commercial enterprise of the next few decades. Scientific research, medical diagnosis, industrial planning and development, financial services of all types, professional consulting, "telecommuting" - these and many more activities that add up to a large proportion of the total economic activity of a modern nation - are projected as taking place "over the network." Entertainment programming is only a part of the whole, but it is widely seen by government and industrial planners as the one that can best and most immediately help to finance the development of the expensive infrastructure needed to support the whole system. In other words, the revenues generated by new entertainment services could become a kind of general tax to finance the construction of a wholly new industrial infrastructure. Under the circumstances, it is easy to understand why no country would wish to surrender control of this sector to foreign competition without at least having a better perception of what role it might play in the more general economic future.

1 OMSYC and IDATE reports. Estimates based on figures of the 100 largest companies in the world. Rate: 1 ECU = US\$ 1.298238.

2 Financial and creative links between Hollywood studios and European and Japanese firms have been increasing. MCA and Columbia Tristar are owned by Matsushita and Sony, respectively. United States companies are established in Europe both in production of films and television programmes (United Artist European Holding, owned by TCI) and in distribution (United International Pictures (UIP), incorporated in the Netherlands, is a joint venture between MGM/UA, Paramount and MCA Universal for film distribution all over the world except North America). The reverse is more rare but, for instance, Credit Lyonnais owns the Hollywood studio MGM/UA; and Philips has substantial interests in United States audiovisual firms.

3 Production of audiovisual services resembles manufacturing in the sense that it ends with a physical product composed of labour and capital inputs. Practically all the costs incurred in making the product accrue in turning out the first copy of the film, video or broadcast. Additional copies can be made inexpensively. These production characteristics explain the search for control of the distribution of the product notably through ownership of distribution networks. Such control allows distributors exhibitors to favour their own products, thus limiting the choice of products available to buyers.

prejudice as to whether any of them would be inconsistent with Article XVII. Moreover, the measures found to be justified under the footnote would normally be expected also to meet the requirement in the chapeau to Article XIV that they should not constitute a disguised restriction on trade. Nothing in the footnote is intended to affect or influence any question

concerning taxation at issue between members in the context of bilateral tax treaties. In principle, this exception clause does not necessarily imply acceptance of any tax measure taken by a GATS member, whether or not covered by the exception clause. Therefore, any tax measure could be taken to dispute settlement.<sup>222</sup>

<sup>222</sup> See the statement by the delegation of Switzerland to the GNS at its Meeting on 14 December 1993.

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## P. Subsidies

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Some developing country proposals have provided for a standstill and rollback on subsidies of developed countries and flexibility in the use of subsidies by developing countries to achieve specific objectives. It is recognized in Article XV of GATS that, in certain circumstances, subsidies may have distortive effects on trade in services. Members should therefore enter into negotiations with a view to developing the necessary multilateral disciplines to avoid such trade-distortive effects.<sup>223</sup> It would seem that these negotiations should address the appropriateness of countervailing procedures. The text also provides that future negotiations or disciplines shall recognize the role of subsidies in relation to the development programmes of developing countries and take into account the needs of members, particularly developing countries, for flexibility in this area. The negotiation of precise disciplines was postponed because obligations would reflect judgements on the economic impact of trade. It is clear that for many services it would be difficult to obtain adequate data on market shares and prices, and that the concept of "unit of output", and consequently "unit costs", might be difficult to apply to many services sectors. Other problems would arise from difficulties in identifying the "origin" of services and from confusion between foreign and domestic firms. Difficulties in calculating the price differential arising from a subsidy, and the consequent injury to domestic producers, have led to proposals that subsidies to trade in services, as well as dumping, should be dealt with under dispute settlement procedures or through competition law, rather than unilaterally.<sup>224</sup> Some countries have made entries in their schedules of commitments on subsidies (see box 17).

The broad definition of trade in services under GATS, which includes trade effected through commercial presence and the move-

ment of natural persons to supply services as well as movement of consumers, could mean that benefits accruing to enterprises in the sense of Article I of the Agreement on Subsidies and Countervailing Measures, such as preferential tax regimes for foreign operations, which directly or indirectly benefit their foreign-based subsidiaries, might also be considered as subsidies to exports of services. Moreover, subsidies to the parent firm in the home country could provide competitive advantages to foreign subsidiaries abroad. Special fiscal and other benefits in favour of foreign consumers purchasing services in the country might also fall in this category. Given the heterogeneity of the services sector, including the differences in the way trade takes place between sectors, the subsidy question might best be addressed on a sector-specific basis, as it would be extremely difficult to devise a common approach to identify the trade impact of subsidies.

There is not much published information concerning subsidies to services although it is clear that some services sectors are highly subsidized, and that members, particularly the more vulnerable developing countries, will be reluctant to include such sectors in their schedules of commitments until clear rules are drawn up with respect to subsidies. While the reduction and elimination of trade-distorting subsidies could be an eventual objective, it would be important to define, from the outset, the legitimate objectives of subsidies in services (e.g. to assure a minimum level of services to the population, to preserve national security, and to provide cultural and environmental protection). The possibility of taking unilateral countervailing measures could cause difficulties in the services sector, given the experience with countervailing duties on goods (which would be potentially open to even greater abuse in that sector).

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<sup>223</sup> It should be noted that GATT Article III provides, in paragraph 8(b), that the "provisions of this Article shall not prevent the payment of subsidies exclusively to domestic producers, including payments to domestic producers derived from the proceeds of internal taxes or charges applied consistently with the provisions of this Article and subsidies effected through governmental purchases of domestic products".

<sup>224</sup> For further details, see "The impact of subsidies on trade in services" (UNCTAD/SDD/SER/3), 4 October 1993, which was prepared under item 3(d) of the work programme of the Standing Committee on Developing Services Sectors. The Uruguay Round Agreement on Subsidies and Countervailing Measures provides a definition of a subsidy. It divides subsidies into three categories, i.e. prohibited subsidies, actionable subsidies and non-actionable subsidies, and establishes special and differential treatment for developing countries in its Article 27, which includes the phase-out of export subsidies within an eight-year period. It should be noted that this Agreement already addresses some services, for example, the preferential provision of internal transport and freight on export shipments, provided or mandated by governments on terms more favourable than for domestic shipments, constitutes a prohibited export subsidy, and government assistance to consultancy services used for research purposes is considered to be a non-actionable subsidy.

## Box 17

## ENTRIES ON SUBSIDIES IN THE SCHEDULES OF COMMITMENTS

Some schedules of commitments include in their horizontal sections covering measures applicable to all sectors, and under the column on limitations to national treatment, an entry on subsidies. Certain schedules provide for the possibility of applying all types of subsidies across the board in specific modes of supply, for example the Schedules of Switzerland, Iceland, Finland, Sweden, Norway, Austria and Brazil include the entry "unbound for subsidies", or eligibility for subsidies may be limited to established juridical persons or citizens, which means that all subsidies across the board to national suppliers of services will not be offered to foreign suppliers of services. The United States Schedule includes the entry unbound for national treatment under cross-border movement and movement of consumer mode of supply. Under commercial presence and movement of natural persons mode of supply, however, the United States Schedule enters specific types of subsidies, i.e. the Federal Overseas Private Investment Corporation (OPIC) insurance and loan guarantees are not available to certain aliens, foreign enterprises, or foreign-controlled enterprises established in the United States; Trade and Development Agency financing is limited to: I. individuals (1) who are either United States citizens or non-United States citizens lawfully admitted for permanent residence in the United States, and (2) whose principal places of business are in the United States, or II. privately-owned commercial corporations or partnerships that are incorporated or legally organized under the laws of the United States and whose principal places of business are in the United States, and (1) that are more than 50 per cent beneficially owned by individuals who are United States citizens or (2) that have been incorporated or legally organized in the United States for more than three years, have performed similar services in each of the prior three years, that employ United States citizens in more than half of their permanent full-time positions in the United States and have the existing capability in the United States to perform the contract. Subsidies granted under the Schedule also include Federal Small Business Administration Loans restricted to United States citizens or 100 per cent United States-owned companies, whose directors are all citizens; measures at the federal, state or local levels that accord rights or preferences to members of socially or economically disadvantaged groups; and research and development. The EC also provides for subsidies in its Schedule, by including a horizontal entry under national treatment limitations relating to commercial presence and movement of natural persons mode of supply. These entries provide that subsidies are unbound for branches established in a Member State by a non-Community company; eligibility for subsidies from the Communities or Member States may be limited to juridical persons established within the territory of a Member State or a particular geographical subdivision thereof; unbound for subsidies for research and development; supply of a service, or its subsidization, within the public sector, is not in breach of national treatment; and to the extent that subsidies are made available to natural persons, their availability may be limited to nationals of a Member State of the Community. Some schedules, such as those of Japan, Canada, the Nordic countries, and the Republic of Korea, with regard to commercial presence and/or movement of natural persons mode of supply, enter under national treatment limitations "unbound for research and development subsidies". The Republic of Korea also provides that eligibility for subsidies including tax benefits may be limited to companies which are established there or to residents according to the pertinent laws. In July 1994, the United States submitted a long list of additional taxes and subsidies imposed by sub-federal jurisdictions, which will be considered by other participants to ensure that they do not result in any alteration in the negotiated balance of rights and obligations.

### Q. Specific commitments

With respect to the specific commitments proposed by the developing countries, GATS adopts the positive list approach for the listing of sectors, subsectors and transactions. The text separates the concepts of market access and national treatment, and provides for separate columns in the schedules of commitments for market access and national treatment com-

mitments as, under the structure of GATS, market access and national treatment provisions are not general obligations but are exchanged as negotiated commitments with respect to individual sectors or subsectors (see box 18). Market access commitments would be negotiated in accordance with the definition of trade in services, and foreign suppliers could

**RESTRICTIONS AND LIMITATIONS ON MARKET ACCESS**

When a member undertakes market access commitments for a sector or sub-sector in accordance with Article XVI of the GATS, it should not maintain or adopt the following measures, unless such measures are specified in its Schedule of Commitments: (i) limitations on the number of service suppliers, whether in the form of numerical quotas, monopolies, exclusive service suppliers or the requirement of an economic needs test; (ii) limitations on the total value of service transactions or assets in the form of numerical quotas or the requirement of an economic needs test; (iii) limitations on the total number of service operations or on the total quantity of service output expressed in terms of designated numerical units in the form of quotas or the requirement of an economic needs test; (iv) limitations on the total number of natural persons who may be employed in a particular service sector or that a service supplier may employ and who are necessary for, and directly related to, the supply of a service in the form of numerical quotas or the requirement of an economic needs test; (v) measures which restrict or require specific types of legal entity or joint venture through which a service supplier may supply a service; and (vi) limitations on the participation of foreign capital in terms of a maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment.

be compelled to accept obligations as described under Article IV on Increased Participation of Developing Countries as a condition for market access. GATS provides for parties to seek liberalization in those sectors and subsectors where they possess comparative advantage and to grant concessions in those sectors where liberalization is judged most compatible with their economic, social and development interests (similar to the situation under GATT). Such an approach would mean that, as was the case of goods under GATT, negotiations could address those sectors where liberalization is less difficult and thus quickly consolidate the legal structure of GATS (see box 19).

Article XVII on National Treatment, in paragraph 3, stipulates that "Formally identical or formally different treatment shall be considered to be less favourable if it modifies the conditions of competition in favour of services or service suppliers of the Member compared to like services or service suppliers of any other Member", which involves the principle of "equal competitive opportunity". This paragraph could give rise to many disputes as regards its interpretation.

A member might use the concept of equality of competitive opportunity to try to

broaden the market access granted to its suppliers. This concept could also be used as a means of linking the concepts of market access and national treatment, and is potentially capable of leading to far-reaching intrusions into countries' domestic policies. For example, in the banking sector, the argument in favour of the concept could be that restriction of market access to some submarkets only puts the banks at a disadvantage in competition with domestic institutions. Such a claim would constitute an alternative approach to achieving the objectives of the section on Non-discriminatory Measures in the Understanding on Commitments in Financial Services, which merges the concepts of national treatment and market access, and commits members to remove or limit the significant adverse effects of such measures "that prevent financial service suppliers from offering in the Member's territory, in the form determined by the Member, all the financial services permitted by the Member" or "that limit the expansion of the activities of financial service suppliers into the entire territory of the Member". In this context, it should be noted that exchange control has long been seen by certain OECD countries as a potential impediment to equality of competitive opportunity for foreign banks.<sup>225</sup>

<sup>225</sup> In the first National Treatment Study by the United States Department of the Treasury in 1979, it is stated that "even handed application of foreign exchange controls may affect foreign bank operations which are more heavily involved in foreign lending differently than their domestic counterparts". More recently, in the surveys of selected countries' banking systems in the National Treatment Study of 1990, attention is drawn to instances in which exchange controls prevent banks from fully exploiting their competitive strengths and capacities to innovate with respect to certain financial products, see Department of Treasury, *Report to Congress on Foreign Government Treatment of U.S. Commercial Banking Operations* (Washington, D.C.: 1979), p. 1, and *National Treatment Study 1990* (Washington, D.C.: 1990), pp. 18 and 235-236, relating to foreign securities firms in Japan, and pp. 19 and 259 where the situation of foreign banks in the Republic of Korea is discussed.

## Box 19

## SPACE TRANSPORT SERVICES

Space Transport Services<sup>1</sup> is a sector in which, in addition to the traditional launch service operators of United States and Europe, some potential newcomers such as China, India, Brazil, Israel, Australia, and Russia are emerging. The traditional launch service operators do not welcome the enlargement of the membership, but as launcher technology, and indeed satellite technology also, become more widespread, it is hard to believe that the new members can be indefinitely excluded. One of the few points on which United States and European launch service operators agree - after years of mutual recrimination about unfair government subsidies - is that the market cannot withstand the arrival of other suppliers, particularly if they are offering attractive prices and associated conditions. The United States and Europe have resorted to measures used for protection in trade in goods, such as VERs, to restrict access to the world market in this services sector. Both in the United States and in Europe there has been reluctance on the part of the space agencies to have the subject of launch services included in more general trade negotiations owing to its specialized character. It should be noted that some countries originally included offers on this subsector in their list of specific commitments, but they were later withdrawn. However, on both sides of the Atlantic, non-space agencies are becoming increasingly involved.

Parallel to the Uruguay Round negotiations, the United States and Europe have for some years been trying to develop what they call 'rules of the road' for determining fair pricing for launch services with a view to reducing friction between them. According to press reports, European suppliers have recently expressed their indignation at United States actions which appear to them to give the green light unilaterally to one of the INMARSAT 3 series of satellites being launched by a Russian PROTON launcher. The United States simply made it known that an export licence for this satellite would be issued by the United States (it is being built by a United States prime contractor) if it were decided to launch it from Russia.

This has been a significant departure from previous policy, and the Europeans have interpreted it as unjustified interference in the decision-making mechanism of the international organization concerned. There has been a similar European reaction to the report that the United States had 'approved' the launch of two Aussat satellites by Chinese launchers on the basis of an agreement that the Chinese would limit launches of United States-built satellites between 1989 and 1994 to a total of nine, and that, after the launch of the Aussat and Asiasat satellites, China would 'lift its prices to world levels' and conclude a fair trade agreement with the United States in respect of launch services.

The first public allegations of unfair competition pointed to 'government subsidies' as the culprit, in both the original development of a launcher and its principal subsystems. It is undeniable that all those that now dominate the market have inherited designs that were originally funded by governmental budgets, and that in many cases the subsequent improvements have also been paid for, directly or indirectly, by government agencies. Indirect subsidies cover several such examples in the United States, where government agencies have ordered a series of launches sufficiently large to make it attractive for the private launcher developer to invest company money in making updates and improvements to the launcher system. In Europe, Arianspace, a private company created under private law to market and provide Ariane launch services, had a formal agreement with the European Space Agency (ESA) in which it was made clear that the company would not be expected to return any of ESA's up-front development costs (or the cost of upgradings to Ariane 3, 4 and 5) until the company's financial position made this possible. Moreover, the agreement with ESA provided that the Agency's spacecraft would normally be launched by Ariane at a predetermined price. The same was expected of ESA Member States.

The market for satellite launching services can be divided into the "predestined" and "open" markets. Within the predestined market there is no opportunity for outside suppliers to compete for the launch contract. In some cases, such as that of military satellites, the national security exception is clearly difficult to contest (Article XIVbis of GATS). Another component of the predestined market involves satellites launched for the government's own use and is thus covered by the exception for Government Procurement (Article XIII). However, when such satellites are used for commercial purposes (i.e. comparable to government purchases for resale), it would seem equivalent to giving the launcher concerned monopoly rights and it would thus be governed by

## Box 19 (concluded)

Article VIII of GATS. Article VIII:1 provides that each party shall ensure that any monopoly provider of a services in its territory does not, in the supply of the monopoly service in the relevant market, act in a manner inconsistent with that party's obligations under Article II (MFN treatment) and specific commitments under Part III of GATS.

The rest of the market, considered "open" in the sense that the owner of the satellite is free, in principle, to select the launcher offering the best service at the best price, is still subject to a series of trade barriers in the sense of GATS. The barriers and distortions to trade resulting from government practices that most affect satellite launching services fall into three categories. The first category of barriers covers cases where the launcher does not have access to the market because the client (i.e. the "importer" of the launching service) is denied an export licence for the satellite. Such restrictions have been justified as necessary to ensure that the launching country (i.e. the exporter) does not obtain access to advanced technology. In most cases, refusals to provide an export licence are simply intended for protectionist purposes, either to protect the domestic launching services, or the owners of satellites already in orbit, from unwanted competition. Such restrictions can be attacked by obtaining bindings with respect to market access and national treatment on satellite launching services from the countries concerned.

A second type of barrier arises when governments provide special subsidies to induce domestic or foreign clients to use their launching services (the second example being equivalent to an export subsidy). These can take the form of government insurance guarantees or government-supported export credits. As noted above, GATS is notably weak on the issue of subsidies, not providing any definitions or criteria or effective disciplines in its Article XV, which simply states that a request from a member for consultation with another member, which it considers to have adversely affected it by a subsidy, "shall be accorded sympathetic consideration". The same Article provides that members "shall enter into negotiations with a view to developing the necessary multilateral disciplines to avoid ... trade-distortive effects" of subsidies.

A third type of barrier relates to anti-subsidy actions, in the form of the export restraints which the United States has imposed on China, on the grounds that China is providing launching services at "unfair" or "dumping" prices. As GATS does not establish any criteria for identifying subsidies or "unfair" prices (and no rules on subsidies), it does not provide any basis for resolution of this issue other than the fact that the burden of proof would seem to be on the United States to justify a deviation from the MFN clause. An early negotiation of disciplines on subsidies and government procurement is important for satellite launching services. Moreover, the scope of satellites used for commercial purposes needs to be clearly defined.

*1* Space services are not limited to space transport services. The space services sector is of considerable importance to countries which are in the process of converting their military industries to civilian use. The services in question are those provided by satellites and space stations, and could include: (i) transportation of people, e.g. for working on space stations in orbit; (ii) meteorology and monitoring of the earth's surface in relation to, *inter alia*, environment, cartography and geography; (iii) research and development; (iv) control of navigation; (v) prevention of natural catastrophes; and (vii) education.

The possibility of including "additional commitments" in the schedules further widens the scope of the commitments covered by GATS, which stipulates in Article XVIII that members may negotiate commitments with respect to measures affecting trade in services not subject to scheduling under Articles XVI and XVII, including those regarding qualifications, standards or licensing matters. The scope of Article XVIII on Additional Commitments is not clearly defined, unlike Article XVI on Market Access, and as it stands it is too permissive. Because of the vagueness of this provision most of the schedules of specific

commitments do not include the column "Additional commitments" or leave the column blank. The Schedules of the United States, the Republic of Korea, Japan, Australia and Malaysia are among the rare Schedules that have entries in the "Additional commitments" column, some of which relate to future liberalization measures. The Japanese entry relates to consultancy on the law of jurisdiction where the service supplier is a qualified lawyer and to banking and other financial services. With respect to the latter, under commercial presence mode of supply, it is stated that Japan intends to expand the scope of the Employees' Pension

Fund assets, which can be managed by discretionary investment management firms, as regards the funds qualified by the Minister of Health and Welfare, by removing the distinction between new money and assets other than new money. The Schedule of the Republic of Korea contains a horizontal entry on additional commitments which provides that residents who have been treated as foreigners in the Securities Exchange Act will be accorded national treatment in portfolio investment in Korean stocks in 1994. Under the subsector "Accounting, auditing and bookkeeping services" the following additional commitment is provided: a Korean accounting firm or office may, by paying an annual membership fee, acquire membership in international accounting organizations that have world-wide business networks. The services that may be supplied to a Korean accounting firm or office through a membership contract are consultancy for foreign accounting standards and auditing, training of CPAs, transfer of auditing technology and exchange of information. Under "Temporary movement of natural persons" the Schedule allows the movement of persons who are qualified as CPAs under their home country's laws and are employed by international accounting firms for the purpose of supplying the services mentioned above. Entry and stay of these persons is limited to a one-year period which may be extended. The second Korean entry under "Additional commitments" relates

to architectural services and covers all modes except commercial presence. This entry provides that the supply of services by foreign architects through joint contracts with architects licensed under Korean law will be allowed as of 1 January 1996. Foreign architects licensed under their home country's law may acquire a Korean architect's license by passing a simplified examination which covers only two of the test's six subjects. The Schedules of New Zealand, Australia, Canada, Malaysia, Japan, Republic of Korea, Thailand and Singapore provide for additional commitments in the maritime transport services sector by enumerating a list of services that would be made available on reasonable and non-discriminatory terms and conditions to international maritime transport suppliers. The United States provides for an additional commitment in legal services: consultancy on the law of jurisdiction where the service supplier is qualified as a lawyer. The additional commitment relates to the possibility of partnership between foreign lawyers and domestic lawyers, employment of local lawyers, use of firm name and details on the areas in which the lawyers could practise. Malaysia, for specific professional services, provides, under the additional commitments column, in respect of the natural persons mode of supply, that the qualifying examination to determine competence and ability to supply service will be conducted in English.

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## R. Progressive liberalization

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In accordance with Article XIX of GATS on Negotiation of Specific Commitments, the time-limit for the next round of negotiations on specific commitments is five years after the date of entry into force of the Agreement Establishing the WTO. A longer time-limit for further negotiation may be more conducive to effectively evaluating the benefits developing countries have gained based on clear statistical data.<sup>226</sup>

As mentioned above, Article XIX:2 operationalizes Article IV, since it stipulates that "The process of liberalization shall take

place with due respect for national policy objectives and the level of development of individual members, both overall and in individual sectors. There shall be appropriate flexibility for individual developing country members for opening fewer sectors, liberalizing fewer types of transactions, progressively extending market access in line with their development situation and, when making access to their markets available to foreign service suppliers, attaching to such access conditions aimed at achieving the objectives referred to in Article IV". It follows from this provision that developing countries should not be asked to adopt liberalization

<sup>226</sup> See document UNCTAD/SDD/SER/1, prepared under item 2(a) of the work programme of the Standing Committee on Developing Services Sectors, 1993, which provides information on progress achieved at international and national levels on services statistics and addresses some of the inadequacies of internationally comparable statistics on trade in services.



measures that would conflict with their developmental and technological objectives, and that progressive liberalization by developing countries should be governed by the actual expansion of their service exports, not judged by hypothetical market opportunities. The provisions of Article XIX:3 to the effect that the establishment of guidelines for future negotiations is to be preceded by an assessment of international trade in services with reference to the objectives of the Agreement, including those set out in Article IV:1, is of positive im-

portance in this context. Appropriate statistical information would be required to carry out this assessment, in particular to determine the importance of services in the world economy, country groups and individual countries, globally and at sectoral levels, to monitor the sectoral evolution over time, especially with regard to the impact of GATS, and to demonstrate the relationship between services and goods as well as between trade, production, investment and employment in various sectors.

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## S. Dispute settlement mechanism

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GATS Articles XXII and XXIII on Consultation, and on Dispute Settlement and Enforcement, respectively, should be read in the context of the integrated dispute settlement system contained in the Understanding on Rules and Procedures Governing the Settlement of Disputes, which provides that suspension of concessions is not limited to the concessions resulting from GATS, but that cross-retaliation with concessions on trade in goods and intellectual property would be permitted under certain conditions.<sup>227</sup>

The "commercial presence" aspect of concessions on services introduces an element peculiar to services and not pertinent to trade

in goods. This means that in services it may not always be clear who has a right to invoke the dispute settlement provisions on behalf of whom. The definition of "juridical person" in Article XXVIII on Definitions is intended to provide some guidelines in this respect. It states, *inter alia*, that a juridical person is "owned" by persons of a member if more than 50 per cent of the equity interest in it is beneficially owned by persons of that member. It is of interest to note that many of the offers under the commercial presence mode of supply contain less than 50 per cent equity, which would mean that the juridical person established would be considered as domestic.

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## T. Annexes and Ministerial Decisions

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The annexes are an integral part of GATS and may be divided into four categories as follows: (i) annex on MFN exemptions enabling a member to add exemptions to Article II prior to the entry into force of GATS; (ii) annexes covering sectoral specificities, notably air transport, and financial services; (iii) annexes defining in more precise terms the modes of supply, namely movement of natural persons

and telecommunications; and (iv) annexes providing the modalities for continuation of negotiations on financial services, basic telecommunication services and maritime transport services. Some of these annexes are elaborated on by Ministerial Decisions and the Understanding on Commitments in Financial Services.

<sup>227</sup> In the Dunkel text, the dispute settlement system (Articles XXII and XXIII) was based on the corresponding GATT Articles, but not as yet interpreted and amplified by the kind of detailed procedural understandings that have filled out the GATT Articles. The provisions were self-contained, that is, recourse to a dispute settlement mechanism outside the GATS system was not contemplated.

## 1. Annex on Article II Exemptions

As mentioned above, GATS contains an Annex on Article II Exemptions, which specifies the conditions under which a member, at the entry into force of the Agreement, is exempted from its obligations under Article II:1. The universal coverage of GATS could be circumvented through the unlimited possibility to seek exemptions provided for in paragraph 2 of Article II on MFN Treatment. The limitation to the open-ended possibility to put forward exemptions is that the Annex relates to existing measures only, although some of the exemptions scheduled are future measures drafted as existing measures. For example the EC list of MFN exemptions contains several exemptions which refer to future measures such as an exemption applying to all sectors for an indefinite duration for measures based on existing or future bilateral agreements between the EC and certain Member States and the countries and principalities concerned providing for (a) the right of establishment for juridical and natural persons, and (b) waiving the requirement of work permits for natural persons supplying services.<sup>228</sup> In paragraph 2 it is provided that any new exemptions applied for after the date of entry into force of the Agreement Establishing the WTO shall be dealt with under paragraph 3 of Article IX (Decision-Making) of that Agreement. Paragraph 3 relates to the grant of waivers, stating that: "In exceptional circumstances, the Ministerial Conference may decide to waive an obligation imposed on a Member by this Agreement or any of the Multilateral Trade Agreements provided that any such decision shall be taken by three fourths of the Members ....". The Conference or the General Council should hold an annual review of the waiver.

The developed countries have entered more exemptions to the MFN than the developing countries. Developing countries that were unable to identify the exemptions they required before 15 December 1993 will have to fulfil the strict conditions of Article IX.<sup>229</sup> As the negotiations have not been concluded in three major sectors and one mode of supply, the Ministerial Decisions on Financial Services, Negotiations on Basic Telecommunications and Negotiations on Maritime Transport Services provide that MFN exemptions could be made in relation to these sectors until the conclusion of the negotiations, which is targeted for six

months after the date of entry into force of the WTO in the case of Financial Services and of Basic Telecommunications and for June 1996 in that of Maritime Services.

Of particular interest in the application of the MFN principle is the continuing existence of reciprocity in many countries' regulations governing the granting of market access to foreign banks. Reciprocity conditions enable a country to withhold such access from the banks of another country if their own banks are not granted broadly similar opportunities in that country. Such conditions are in conflict with the MFN principle, but have none the less been specified as part of the regulatory regimes that several countries have offered to bind in initial offers already submitted. The objective of the continuing negotiations on financial services will be to obtain complete elimination of reciprocity from all members' regulatory regimes for foreign banks. In their initial offers some parties (such as the EC) have expressed a willingness to abandon reciprocity contingent on the quality of other parties' offers. It would seem that the United States, prior to the adoption of the Final Act by the TNC, attempted to use exemptions from Article II in financial services as a negotiating tactic in order to improve the offers of certain countries. The United States also indicated that it will maintain its derogation from Article II for "basic long distance domestic and international telecommunications services" pending liberalization in "major telecommunications markets".<sup>230</sup>

The Annex on Article II Exemptions is supposed to specify the conditions under which a member, at the entry into force of the Agreement, is exempted from its obligations under Article II:1, but no such conditions are mentioned in the Annex, except that the Council for Trade in Services will review all exemptions granted for a period of more than five years. In that review the Council will examine whether the conditions which created the need for the exemptions still prevail and determine the date of any further review. There is no provision for the initial examination of the exemptions put forward to determine whether they are reasonable, legitimate and do not nullify the benefits under the Agreement.

The absence of multilaterally agreed criteria on the legitimacy of seeking exemptions means that countries could abuse the open-ended possibility of entering exemptions, and

<sup>228</sup> See MTN.GNS/W/228/Rev.1.

<sup>229</sup> Despite the December deadline for submission of exemptions, it is understood that since 15 December 1993 more countries have entered MFN exemptions and that around 77 countries in all have submitted such exemptions.

<sup>230</sup> GATT document MTN.GNS/W/145.

therefore that many exemptions could be put forward mainly to gain advantages in the negotiations, which would undermine the functioning and credibility of the Agreement. A balance needs to be struck between individual concerns and limitation of the scope and number of such exemptions, and some payment should be required for the maintenance of certain types of exemptions, either by the withdrawal of offers or by seeking compensatory concessions from countries making extensive use of Article II:2.

With respect to the termination of the exemptions, the Annex provides in paragraph 6 that: "In principle, such exemptions should not exceed a period of 10 years. In any event, they shall be subject to negotiation in subsequent trade liberalizing rounds". The language indicates that the 10-year period is not definitive and that it could be extended. In actual fact the Annex does not lay down criteria or conditions for the inclusion of exemptions, and most of the exemptions scheduled in the MFN exemption lists are for an indefinite period. For example out of the 28 exemptions entered by the EC, 26 are for an indefinite period and all the exemptions entered by the United States are for an indefinite period.

## **2. Annex on Movement of Natural Persons Supplying Services under the Agreement**

The inclusion of the Annex on Movement of Natural Persons, deriving from an initiative taken by a group of "like-minded" developing countries,<sup>231</sup> is a clear recognition that concessions with respect to all categories of natural persons could be negotiated. The Annex also clarifies that movement of natural persons mode of supply involves both service suppliers of a party and natural persons of a member who are employed by a service supplier of another member. However, as developed countries have not included the categories of interest to developing countries in their specific commitments, and recognizing the importance of achieving higher levels of commitments on the

movement of natural persons in order to provide for a balance of benefits under GATS, the Ministerial Decision on Negotiations on Movement of Natural Persons stipulates that negotiations on further liberalization of movement of natural persons for purposes of supplying services are to continue beyond the conclusion of the Uruguay Round, with a view to achieving higher levels of commitments by participants under GATS. The Decision provides for the establishment of a negotiating group to carry out the negotiations and produce a final report no later than six months after the entry into force of the Agreement Establishing the WTO.

There still remain some asymmetries between the treatment of capital and labour. The Annex on Movement of Natural Persons Supplying Services under the Agreement establishes that members may negotiate specific commitments applying to the movement of all categories of natural persons supplying services under the Agreement, which would relate to entry and temporary stay, and provides in paragraph 4 that: "The Agreement shall not prevent a Member from applying measures to regulate the entry of natural persons into, or their temporary stay in, its territory, including those measures necessary to protect the integrity of, and to ensure the orderly movement of natural persons across, its borders, provided that such measures are not applied in such a manner as to nullify or impair the benefits accruing to any Member under the terms of a specific commitment". Similar limitations are not applied to the movement of capital. Nothing in the Agreement limits foreign direct investment, but offers by developing and some developed countries have indicated that commitments with respect to commercial presence are made within the limitations of existing legislation governing foreign investment in the same way that offers on movement of natural persons are circumscribed by immigration laws.<sup>232</sup>

Some questions have arisen with respect to the types of measures which fall within the scope of GATS in the area of movement of natural persons. The Annex provides that the Agreement will not apply to measures affecting natural persons seeking access to the employ-

<sup>231</sup> Annex proposed by Argentina, Colombia, Cuba, Egypt, India, Mexico, Pakistan and Peru, with a view to setting out, in the form of concrete obligations, principles relative to movement of personnel as a mode of delivery (MTN.GNS/W/106).

<sup>232</sup> For more details on the temporary movement of persons as service suppliers, see the note by the UNCTAD secretariat prepared under item 3(h) of the work programme of the Standing Committee on Developing Services Sectors (TD/B/CN.4/24). The note addresses such aspects as the importance of the temporary movement of persons to trade in services of developing countries, the sectors where temporary movement of persons is important for developing country exports, the general characteristics of immigration laws pertaining to the temporary movement of service suppliers, including the identification of sectors and occupations that tend to benefit from more favourable treatment, and international, regional, subregional and bilateral agreements on movement of persons. It states, *inter alia*, that barriers to the temporary movement of persons that arise from immigration laws and regulations constitute a major impediment to the realization of the competitive potential of developing countries in labour-intensive services.

ment market of a member, nor will it apply to measures regarding citizenship, residence or employment on a permanent basis. The Sub-Committee on Services is addressing questions relating to modalities of identification of such measures within the domestic regulatory systems of members, e.g. how to distinguish the case of a person seeking access to the employment market from the case of entry and temporary stay for the purpose of supplying a service. Such a distinction could be based on whether that person has a contract for the supply of a service or an employment contract with a service supplier prior to entry. A distinction also needs to be drawn between permanent employment and temporary employment. Discussions are also taking place in the Sub-Committee concerning bilateral agreements which clearly involve entry and temporary stay of natural persons, such as young workers' programmes, agricultural workers, and exchange programmes for students and university professors. The issue to be settled is to what extent these agreements actually involve the movement of persons for the purpose of supplying a service and how far the measures taken pursuant to them result in actual discrimination.

### **3. Annex on Telecommunications**

The Annex on Telecommunications recognizes the dual role of this sector. It relates to telecommunications as a mode of supply and applies to all measures of a member that affect access to and use of public telecommunications transport networks and services. The purpose of this Annex is to ensure that any service supplier is accorded access to and use of public telecommunications transport networks and services on reasonable and non-discriminatory terms and conditions for the supply of a service included in its schedule. Such an annex was needed because telecommunications has become strategic to the delivery of most services, such as financial services. The Annex, therefore, does not in itself result in liberalization in any sector, including telecommunications, without the inclusion of a negotiated commitment in the schedules of concessions. The Annex strikes a balance between the needs of the users for fair terms of access and the needs of the regulators and public telecommunications operators to maintain a system that functions and fulfils public policy objectives. The recognition of the dual role of telecommunications derives to a considerable extent from the insistence of developing countries on this point and the two submissions by India, Egypt, Cameroon and Nigeria. The Annex ensures

that the conditions of use of telecommunications services as a mode of supply do not impair the market access commitments made in schedules, which are limited by existing telecommunications capabilities offered to the public generally. There is no obligation, therefore, to authorize other members to establish, construct, acquire, lease, operate or supply telecommunications transport networks or services, other than as provided for in their respective schedules, or to require members to establish additional facilities not offered to the public generally.

In paragraph 5(g), the Annex provides that a developing country member "may, consistent with its level of development, place reasonable conditions on access to and use of public telecommunications transport networks and services necessary to strengthen its domestic telecommunications infrastructure and service capacity and to increase its participation in international trade in telecommunications services". Such conditions should be specified in the member's Schedule. This should provide the possibility of derogating from some of the more onerous provisions. To date, only Thailand has scheduled such conditions in its Schedule (i.e. build-operate-transfer requirement). The Annex, in paragraph 6, provides for technical cooperation through the development programmes of ITU, UNDP and IBRD, and the availability of information with respect to international telecommunications services and information technology. The proposed provision in the earlier drafts to the effect that pricing of telecommunications services should be cost oriented has not been included in the Annex on Telecommunications owing to opposition from developing countries. Such a provision would have prevented developing countries from cross-subsidizing to finance the extension of more modern telecommunications services on a wider scale throughout their territories. The Annex provides for user rights in paragraph 5(b), which could cause developing countries additional costs and difficulties, and reduce their ability to exercise control over their telecommunications networks. Paragraph 5(c) on cross-border data flows could mean that developing countries would not be able to apply measures to strengthen their store of knowledge, e.g. by ensuring use of local databases or the copying of all data sent abroad. Although these obligations apply only to sectors included in the schedules of commitments, it is not clear whether they apply when a commitment has not been made with respect to "cross-border" mode of supply. The negative impact of these provisions on the interests of developing countries may be mitigated by the special dispositions of paragraph 5 (g).

### BASIC TELECOMMUNICATIONS SERVICES

Informal meetings were held in 1992 to discuss the possibility of extending negotiations on the liberalization of basic telecommunications beyond the completion of the Uruguay Round and the modalities of clearly reflecting commitments on basic telecommunications in schedules. The three issues dealt with were coverage and definition, regulatory issues and practical considerations related to liberalization. As a result of these discussions, an informal "model schedule of commitments on basic telecommunications" was developed to help clarify and resolve technical concerns and to serve as a guide for the conduct of the negotiations. One of the conclusions stemming from this technical exercise was that, in order to capture accurately all relevant limitations, the inscriptions in schedules would need to be supplemented to indicate sub-categories relating to the geographical scope of the services offered (local, long distance, international), the technology concerned (wire/radio based), the means of delivery involved (resale/ facilities-based), and end-use (public/non-public). The participants believed that the addition of these categories to describe the services being offered would be the best way to adapt the requirements of GATS Articles XVI and XVII (Market Access and National Treatment respectively) to the regulatory complexities of the sector.

Certain issues still remain to be settled concerning the model schedule. Some clarifications are required on the application of cross-border and consumption abroad modes of supply to the basic telecommunications and types of limitations that should be scheduled under market access and national treatment. For example, on cross-border supply, one of the questions that has been raised is whether there are particular types of government measures, such as the requirement to interconnect with the public telecommunications operator, that might need to be scheduled as limitations. Another issue relates to technical constraints on the number of suppliers, for example, the number of radio frequencies that can be made available for assignment or allotment. If such measures involve discrimination against foreign suppliers, participants agree that they would need to be scheduled under national treatment, but if the limitation is for strictly technical reasons Article XVI might not apply. The latter may be covered by Article VI obligations as long as the limitations are based on objective and transparent criteria.

The model schedule also outlines other measures on which further discussion would be required to decide whether such measures listed as candidates for additional commitments would need to be addressed in the context of negotiations or whether they have already been adequately addressed by GATS provisions (e.g. Articles III, VI, VIII, IX, or the provisions of the Annex on Telecommunications.) These measures are: procedures or requirements related to licensing, allotment of radio frequencies, numbering and identification codes, type approval and interconnection; measures related to pricing (e.g. cost-oriented pricing); and rights of way for the construction of infrastructure. International agreements between operators would also be considered in the context of the model schedule. The issues that need clarification are whether any of the kinds of terms and conditions in such agreements might constitute a departure from MFN treatment or any other GATS obligations, for example the accounting rates. Some consider these agreements as government measures, while others believe they are commercial arrangements. The Negotiating Group on Basic Telecommunications has met twice to discuss the above-mentioned issues. It has agreed on the distribution of a questionnaire to explore each government's market structure, conditions of competition and regulatory environment regarding the supply of basic telecommunications networks and services, and will meet in late 1994 to discuss the replies to the questionnaire.

The Annex on Negotiations on Basic Telecommunications (see box 20) relates to the negotiations on market access and national treatment in this subsector. This Annex is included to accommodate the concerns of the United States, which wished to exclude the subsector from MFN coverage. This position derived from the perception that, whereas the United States has privatized the basic telecommunications services sector, most other countries reserve this sector for PTI adminis-

trations, and thus the extension of any concessions on an MFN basis would deprive the United States of the ability to negotiate market access with such countries. Forty-eight participants have made commitments on value-added enhanced telecommunications services. Initially some of these offers did include basic telecommunications services, but once the decision was taken to continue negotiations most of these offers were withdrawn. In accordance with the Ministerial Decision on Negotiations

on Basic Telecommunications a negotiating group on this subsector has been established. During the negotiations on the Decision and the Annex, the resolution of the time-frame of negotiations and the standstill commitment were among the most controversial issues tackled. As regards the time-frame, some participants preferred a duration of as little as 18 months or so, while others sought as long as three years. The compromise reached was that these negotiations should conclude no later than 30 April 1996. On standstill, the participants agreed that, until the implementation date of the results of the negotiations, no participant should apply any MFN-inconsistent measure affecting trade in basic telecommunications in such a manner as to improve its negotiating position and leverage. Until the conclusion of the negotiations on basic telecommunications, the exemptions to the MFN will therefore not be applicable even if listed in the MFN exemption list. Twenty-two countries are participating in these negotiations. The outstanding issues that are being considered at the Negotiating Group include the necessity of greater clarity regarding the application of obligations under Article VI to measures affecting trade in basic telecommunications. The types of measures in question relate to licensing, approval, and standard setting procedures. Some of these concerns would be taken up in the context of the Article VI:4 work programme. Article VI:4 provides that the Council for Trade in Services should work on the establishment of any necessary disciplines relating to qualification requirements and procedures, technical standards and licensing requirements, with a view to ensuring that such measures do not constitute unnecessary barriers to trade. The work would be expected to begin after the entry into force of the Agreement Establishing the WTO. Another issue raised in the discussions of the Negotiating Group concerns safeguards against anti-competitive practices. These are measures that would ensure that monopolies or dominant suppliers of basic telecommunications may not exploit their dominant position to distort market forces and impede the ability of competitors to supply networks or services for which commitments have been made. Other issues include measures that may affect suppliers' ability to build facilities or rights of way and the limitations that would need to be scheduled in this regard; the relationship between the Agreement on Technical Barriers to Trade and standards-related measures affecting trade in basic telecommunications; the treatment of new basic telecommunications services and the scheduling approach to be adopted for such services; a

means test or public interest criteria to gain access to telecommunications markets and to obtain the requisite licences to supply the relevant networks or services, which would relate to a need to clarify the applicability and obligations of Article VI; and the requirements for scheduling of commitments in basic telecommunications.

#### **4. Annex on Air Transport Services**

The Annex on Air Transport Services applies to measures affecting trade in air transport services and ancillary services. It excludes from GATS coverage traffic rights and directly related activities that might affect the negotiation of traffic rights. The Agreement applies, however, to aircraft repair and maintenance services, the marketing of air transport services and computer reservation system services. The operation of the Annex will be reviewed at least every five years.<sup>233</sup> Australia, Malaysia, New Zealand, the Nordic countries and Singapore have proposed that, in order for such reviews to be conducted expeditiously and in an adequately prepared manner, it will be necessary to gather and compile the relevant information, including on statistics and modalities in the aviation sector, through the establishment of a Working Party on Air Transport Services. A draft Ministerial Decision was tabled in this regard but was not adopted.

#### **5. Annex on Negotiations on Maritime Transport Services**

The Annex on Negotiations on Maritime Transport Services provides that the MFN exemptions in this sector will enter into force only on the date of the implementation of the results of the negotiations mandated by the Ministerial Decision on Negotiations on Maritime Transport Services or, should the negotiations not succeed, on the date of the final report of the Negotiating Group on Maritime Transport Services. Before the implementation of the results, a member will be free to improve, modify or withdraw all or part of its commitments in this sector without offering compensation. The Ministerial Decision provides for the Negotiating Group to begin its activities one month after the date of the Decision and to conclude its

<sup>233</sup> GATT document MTN.GNS/W/243, 9 December 1993.

negotiations no later than June 1996. Until then the application of Article II and paragraphs 1 and 2 of the Annex on Article II Exemptions are suspended in their application to this sector and it is not necessary to list MFN exemptions. The participants should not apply any measure affecting trade in maritime transport services except in response to measures applied by other countries and with a view to maintaining or improving the freedom of provision of maritime transport services, nor in such a manner as would improve their negotiating position and leverage. The Negotiating Group on Maritime Transport has met twice, and will meet again in the autumn of 1994 to discuss and improve the model schedule of commitments informally circulated by the European Communities in August 1993. The model schedule is composed of three pillars, namely international shipping, auxiliary services, and access and use of port facilities. Further technical work is required on the coverage of international transport services, the definition of auxiliary services and the need for a definition of "reasonable and non-discriminatory terms and conditions" in relation to multimodal operations. Port services are dealt with as additional commitments. Further work is also taking place on relevant commercial practices in the sector, whether based on governmental or private arrangements, and the extent to which they are covered by GATS provisions. A questionnaire will be distributed to provide information on the market structure and regulatory environment in this sector.

## **6. Annex on Financial Services and the Understanding on Commitments in Financial Services**

Serious weaknesses in the regimes of prudential supervision for banks at national and international levels have been revealed by the experience of the last decade, the outstanding event in this respect being the collapse of the Bank of Credit and Commerce International (BCCI) in 1991. Recently there has been a widespread move in OECD countries towards stricter prudential policies. Indeed, as a result of this shift in emphasis in comparison with the 1980s, the cause of prudential regulation would now be more likely to prevail over that of liberalization or deregulation in the event of a conflict between them. One of the manifestations of the new policy thrust is increased insistence on adequate supervision in foreign banks' parent countries as a condition for granting them market access. This accords

with the recommendations of the statement issued by the Basle Committee on Banking Supervision in July 1992 concerning minimum standards for the supervision of international banks. The statement was the outcome of the Committee's evaluation of the state of governance of international banking and of the weaknesses highlighted by BCCI's collapse. It is centred around four principles. Firstly, all international banks or banking groups should be adequately supervised on a consolidated basis by a parent country authority. Secondly, the creation of a cross-border banking establishment should receive the prior consent of the supervisory authority of both the host country and of the bank's parent country. Thirdly, supervisory authorities should have the right to gather information from the cross-border banking establishments of the banks of which they are parent country supervisors. Fourthly, if a host country determines that any of these three standards is not being satisfactorily met, then it may impose restrictive measures designed to satisfy its prudential concerns, including prohibition of the creation of banking establishments.

The Annex on Financial Services included in GATS provides for the right of a member to take measures for prudential reasons, including the protection of investors, depositors, policy holders, or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. The Annex includes a section on recognition of the prudential measures of any other country and another on definition of a financial service, including its components - insurance, banking and related services. Recognition of the prudential measures of other countries, which may be achieved through harmonization or otherwise, may be based upon an agreement or arrangement with the country concerned or may be accorded autonomously. Other interested members will have adequate opportunity to negotiate their accession to such agreements or arrangements or to negotiate comparable ones. The Annex on Financial Services is influenced by the proposal submitted by Malaysia (on behalf of the South East Asia Central Banks and Monetary Authorities (SEACEN group of countries, i.e. Indonesia, Malaysia, Thailand, Nepal, Sri Lanka, Republic of Korea, the Philippines, Singapore and Myanmar). The Annex applies to measures affecting the supply of financial services and does not impose liberalization obligations. Its provisions on domestic regulation are based on the overriding importance of prudential considerations, monetary policies, and the integrity and stability of the financial system. A contentious issue during the Uruguay Round negotiations has been whether

or not measures of domestic regulation (including the refusal of market access) taken for prudential reasons should be subject to recourse to dispute settlement.<sup>234</sup> GATS and the Annex do not treat the issue directly, but it could be argued that their texts lean towards making prudential measures subject to such recourse. Thus paragraph 2(a) of the Annex, under Domestic Regulation, states that "a Member shall not be prevented from taking measures for prudential reasons" but also that "Where such measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement". In paragraph 4 under Dispute Settlement, provision is made for panels to handle disputes on prudential issues and other financial matters. Such panels "shall have the necessary expertise relevant to the specific financial service under dispute". Since the competence of such panels is not specified, in the Annex as currently drafted they are not subject to any limitations as to the categories of issues that could be submitted to them.

The Second Annex on Financial Services provides that, notwithstanding Article II on MFN Treatment and paragraph 2 of the Annex on Article II Exemptions (which contains strict provisions for the grant of a waiver of an obligation under Article IX of the WTO), a member may, during a period of 60 days beginning four months after the date of entry into force of the WTO Agreement list in that Annex measures relating to financial services that are inconsistent with Article II:1 of the Agreement. The Second Annex also provides that, during a period of 60 days beginning four months after the date of entry into force of the WTO Agreement, any member may improve, modify or withdraw all or part of the commitments on financial services inscribed in its schedule, notwithstanding Article XXI of GATS on Modification of Schedules, and covering compensatory adjustments.

The Understanding on Commitments in Financial Services resulted from the wish of certain OECD countries to establish a procedure for making commitments regarding financial services in accordance with guidelines intended to ensure a minimum level of liberalization and a certain degree of uniformity (see box 21). The Understanding contains more

onerous liberalization obligations than GATS Part III. It enables participants in the Uruguay Round to undertake commitments with respect to financial services by means of an alternative approach. The Understanding is based on the proposals submitted by the United States and the EC, and the joint proposal by Canada, Japan, Sweden and Switzerland, but has been influenced by the developing countries' positions. The developing countries were successful in preventing the adoption of a self-contained financial services agreement, which would exclude the sector from the overall agreement on services and would involve an immediate commitment to implement a programme for the liberalization of financial services for all participants. This is clear from the introductory paragraph of the Understanding, which stipulates that the alternative approach could be applied subject to the following understanding:

- "it does not conflict with the provisions of the Agreement;
- it does not prejudice the right of any Member to schedule its commitments in accordance with the approach under Part III of the Agreement;
- resulting specific commitments shall apply on a most-favoured-nation basis;
- no presumption has been created as to the degree of liberalization to which a Member is committing itself under the Agreement".

Thus the Understanding does not appear to be a source of potential problems for the countries that choose not to make commitments on the basis specified therein but under GATS itself. Commitments undertaken on the basis of the Understanding would apply to all members of GATS according to the MFN principle. Members not making commitments under the Understanding would nevertheless benefit from the greater liberalization of financial services by countries that did so. Commitments submitted under the procedure specified in the Understanding are more fully articulated than the principles in the Articles of GATS, and in some cases go beyond them. There is a stand-still commitment that any limitation to the commitments in the Understanding should be confined to existing non-conforming measures. Moreover, concerning market access, the Understanding provides for the scheduling of existing monopoly rights, and requires the

<sup>234</sup> Thus, for example, in the communication from the delegation of Malaysia to the Working Group on Financial Services including Insurance (MTN.GNS/FIN.W/3) on behalf of the SEACEN group of countries, the susceptibility of measures taken for prudential reasons to dispute settlement is rejected. The draft sectoral annex on financial services submitted by Canada, Japan, Sweden and Switzerland (MTN.TNC/W/50), on the other hand, while acknowledging the compatibility with the draft agreement of "reasonable measures taken for prudential reasons", specifies that parties shall none the less not be prevented from recourse to dispute settlement regarding such measures.



## FINANCIAL SERVICES

When the Uruguay Round negotiations on trade in services began, it was generally expected that the negotiations on financial services would be particularly difficult owing to the pervasive relations between financing, payments and economic activity. These relations are central to both monetary policy and policies designed to influence the allocation of credit. The sensitivity of issues included in the negotiations extended both to cross-border transactions and to the supply of financial services through commercial presence. Central to the failure so far to achieve a mutually satisfactory outcome to the negotiation of commitments regarding financial services have been difficulties arising from the widespread application of the principles of reciprocity in this sector. Reciprocity denotes the linkage by a country of its policies towards foreign banks to the treatment accorded by their countries of origin to its own banks. As such it is not compatible with the MFN principle. Reciprocity has long been part of the laws and regulations in several developing and developed countries participating in the Uruguay Round negotiations. In a group of 13 developing countries (Argentina, Brazil, China, India, Indonesia, Malaysia, Mexico, Philippines, Republic of Korea, Singapore, Thailand, Turkey and Venezuela), the laws of the great majority contain provisions for some kind of reciprocity. The same is true of many of the EC Member States (for example, Denmark, France, Greece, Ireland, Italy, Netherlands, Spain and the United Kingdom). Moreover, the Second Council Directive of 15 December 1989 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions in EC countries (the so-called Second Banking Directive) provides for reciprocity towards non-member countries with regard to the granting of market access to foreign banking entities other than subsidiaries. In the United States, reciprocity is a provision of the laws of several states concerning market access for foreign banks. It also applies to certain dealing activities in debt securities of the Federal Government. In offers submitted at various stages of the negotiation of commitments, countries have drawn attention to these policies of reciprocity, usually also noting their willingness to abandon them so long as they are satisfied with the quality of other parties' offers. However, such satisfaction has proved difficult to achieve. Indeed, offers by the United States have involved a two-tier approach to other countries under which existing access to its market would be guaranteed to foreign banks already present but future access would depend on commitments as regards liberalization. The resulting differential treatment of countries would be spelled out in the country's MFN Exemption List. Other parties have been unwilling to acquiesce in so far-reaching an exception to the MFN principle, preferring instead to continue negotiations on commitments in the hope that a more acceptable outcome (involving, *inter alia*, less serious divergences from non-discrimination) could eventually be reached. Disagreements during the negotiations on commitments have concerned both the appropriate pace of liberalization by different countries and the present degree of openness of their banking markets. Certain developing countries, which have been subject to strong pressure from major OECD countries, have professed their acceptance of the objective of liberalization in principle, while expressing their determination to maintain close control over the speed at which it takes place. In this context, some countries have drawn attention to the problems that can be caused for small banking markets by the addition of even limited numbers of additional suppliers. Among the targets of the pressures from the United States (which have been directed at Japan as well as developing countries) have been restrictions on permission for banks to introduce new financial services, granting such permission is one of the commitments specified in the Understanding on Commitments in Financial Services. But significant disagreements remain among countries concerning the balance of costs and benefits resulting from certain financial innovations, especially those involving derivative contracts such as futures, options and swaps - disagreements which are reflected in their banking regulations and in offers submitted in the Uruguay Round. The banking regime of the United States itself has been the subject of important differences among the parties. Many countries have drawn attention to the continuing existence of restrictions in this market on banks' permissible activities (such as the underwriting of securities) and on their geographical expansion across state boundaries. The United States has responded that regulations concerning banks' activities actually provide more leeway than is sometimes supposed, and that the laws of several states now provide for inter-state banking. Disagreements expressed during the negotiations undoubtedly reflect real differences of perception as well as of positions adopted as part of negotiating stances. Consequently, final achievement by the parties of a mutually acceptable set of commitments is likely to prove difficult, especially since the negotiations regarding financial services will no longer benefit from the momentum generated by efforts to arrive at a broader agreement covering other subjects and sectors as well.

members to endeavour to eliminate them or reduce their scope. Each member should also ensure that MFN and national treatment are accorded as regards the purchase or acquisition of financial services by public entities. The Understanding provides for market access and national treatment to non-resident suppliers of financial services for cross-border trade in some types of non-life insurance, reinsurance and retrocession, services auxiliary to insurance, and the provision and transfer of financial information and financial data processing as well as advisory and other auxiliary services relating to banking and other financial services. Such access does not include life insurance or intermediation. Commercial presence is granted to other members, which includes the right to establish or expand within their respective territories, including through the acquisition of existing enterprises. The Understanding also requires countries to grant permission to foreign financial service suppliers to offer any new financial services in their territories. Commitments on the temporary entry of personnel relate to senior managerial personnel, specialists in such areas as computer services, telecommunication services and accounting, as well as actuarial and legal specialists associated with commercial presence. The members should also endeavour to remove or limit significant adverse effects on financial service suppliers of certain specified non-discriminatory measures.<sup>235</sup> The reference to limitations regarding persons employed would make it possible for policies to be designed to achieve the transfer of skills through on-the-job training for a country's nationals.<sup>236</sup> The references to restrictions on the types of legal entity or joint venture through which services would be supplied and on the scale of foreign investment in

domestic enterprises would permit a broad range of policies directed at "indigenization".

Such control over market access is to be exercised in a non-discriminatory way. Observance of this obligation in the treatment of foreign banks of different countries seems unlikely to present major problems in principle, although its implementation may prove difficult with regard to the allocation of quotas for banks or other methods of putting ceilings on total permitted market access. However, non-discrimination towards foreign banks in comparison with domestic ones may prove more difficult if, for reasons associated with monetary policy, the authorities prefer to keep certain activities predominantly or entirely in the hands of domestic banks.<sup>237</sup> In cases of this kind it is not easy to envisage an approach compatible with GATS other than the complete exclusion from the commitments in the country's schedule of an appropriately delimited set of banking activities.

The obligations contained in the section on Non-discriminatory Measures in the Understanding commit members, *inter alia*, to remove or limit the adverse effects of such measures "that prevent financial service suppliers from offering in the Member's territory, in the form determined by the Member, all the financial services permitted by the Member" or "that limit the expansion of the activities of financial service suppliers into the entire territory of the Member". These provisions merge the concepts of national treatment and market access. The obligations laid down in this section with regard to equality of competitive opportunity seem intended to bring about a process of progressive liberalization of banking markets until there are approximately similar

<sup>235</sup> With respect to banking services, GATS Article XVI on Market Access merits especially close attention since it appears to legitimize in principle the kinds of control over market access widely found in practice as part of countries' banking regimes. This control may be exercised with regard to either the sector or subsectors specified in countries' commitments. For example, the Article's reference to limitations on the total number of service suppliers on the basis of an economic needs test presumably permits policies with the objectives of admitting foreign banks to activities where their competition is judged to be beneficial, on the one hand, and of avoiding "overbanking", on the other. It should be noted that tests regarding economic needs and the avoidance of overbanking are common features of licensing procedures for banks in developed as well as developing countries. For example, community needs are generally among the criteria considered in applications for access to the United States market by foreign banks in the form of branches or subsidiaries. See, for example, W. A. Lovett, *Banking and Financial Institutions Law in a Nutshell* (St. Paul, Minnesota: West Publishing Co., 1988), pp. 214-217, and N. L. Deak and J.C. Celusak, *International Banking* (New York: Prentice-Hall for the New York Institute of Finance, 1984), pp. 25-33. In Japan banking licences are granted to new banks only if the Ministry of Finance judges that their establishment would not be detrimental to the existing order. *The Banking System in Japan* (Tokyo: Federation of Bankers' Associations of Japan (Zenginkyo), 1989), p. 40.

<sup>236</sup> The application of nationality restrictions to the personnel of foreign enterprises is common in both developed and developing countries. Moreover, the objective of transferring skills is to be found in the former as well as the latter. See, for example, the account of the regulations under which foreign investment is admitted to the Canadian Province of Quebec in C.D. Wallace, *Legal Control of the Multinational Enterprise* (The Hague: Martinus Nijhoff Publishers, 1982), p. 70.

<sup>237</sup> Concerning reasons connected with monetary policy why countries may wish to limit or prohibit foreign banks' participation in certain submarkets, see *Trade and Development Report, 1990* (United Nations publication, Sales No.: E.90.II.D.6), Part Two, chap. II, section F.

levels in all countries undertaking commitments on the basis of the Understanding.

The provisions of section C on National Treatment in the Understanding are also more stringent. Each member is supposed to grant to financial service suppliers of any other member established in its territory access to payment and clearing systems operated by public entities, and to official funding and refinancing facilities available in the normal course of ordinary business. Moreover, it is provided that national treatment should be accorded for membership or participation in, or access to, any self-regulatory body, securities or futures exchange or market, clearing agency, or any other organization or association, when this is required by a member in order for financial services to be provided on an equal basis by the financial services suppliers of any other member, or when such entities are provided by the member directly or indirectly with privileges or advantages in supplying financial services.

The Ministerial Decision on Financial Services provides that, during a period of six months after the date of entry into force of the WTO Agreement, exemptions listed in the Annex on Article II Exemptions, which are conditional upon the level of commitments undertaken by other participants or upon exemptions by other participants, will not be applied. These provisions were included in GATS to meet the United States' concern that some countries were not putting forward acceptable offers in the financial services sector, and to prevent the United States from requiring reciprocity in the financial services sector, which would lead to the undermining of the MFN principle. According to this compromise, the United States would schedule its commitments in line with its two-tier approach, providing access to financial service suppliers already having presence in the United States market and an MFN exemption for a second tier of countries to which the United States would grant full liberalization on the basis of the Understanding. This MFN exemption would not be effective for the first six months of the entry into force of the WTO Agreement, during which time the United States would evaluate the offers of other countries and de-

cide whether or not it would seek MFN exemption. A Group has been established by the Sub-Committee on Services to continue negotiations on financial services.

## **7. Ministerial Decision on Professional Services**

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In addition to the above annexes and Ministerial Decisions, there are four Ministerial Decisions on institutional arrangements. The Decision concerning Professional Services contains a recommendation to the Council for Trade in Services to establish a Working Party on Professional Services at its first meeting. The mandate of the Working Party would be to examine and report, with recommendations, on the disciplines necessary to ensure that measures relating to qualification requirements and procedures, technical standards and licensing requirements in the field of professional services do not constitute unnecessary barriers to trade. As a matter of priority, the Working Party should make recommendations for the elaboration of multilateral disciplines in the accountancy sector, so as to give operational effect to specific commitments. It should be noted that the professional services sector is one of the sectors in which some developing countries have achieved competitiveness but their trade in such services faces significant difficulties.<sup>238</sup>

## **8. Ministerial Decisions on Institutional Arrangements and on Trade in Services and the Environment**

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The Decision on Institutional Arrangements for GATS empowers the Council for Trade in Services, at its first meeting, to establish subsidiary bodies as appropriate including sectoral committees. The Decision also em-

<sup>238</sup> Under item 3 (i) of the work programme of the Standing Committee on Developing Services Sectors, the secretariat has prepared a background note (UNCTAD/SDD/SER/2) to provide information on harmonization and recognition of qualifications. The note covers laws and regulations in the professional services sector, highlighting those pertaining to qualifications and standards, and outlines the initiatives of governments, regional and subregional agreements and the private sector aimed at achieving such harmonization and recognition. The note also identifies some of the barriers to trade in professional services as follows: non-accreditation, non-recognition of foreign qualifications, denial of access to examinations for completion of qualifications, non-recognition of non-citizens or non-residents, requirement of joint venture or prohibition of joint venture, local establishment requirements, foreign exchange controls affecting the repatriation of earnings by firms, restrictions on staff that could be employed, entry restrictions such as visa restrictions, denial of access to transborder data flows or distribution channels, and anti-competitive practices of transnational corporations.

powers the Council to establish a Committee on Trade in Financial Services.

The Decision on Trade in Services and the Environment acknowledges that measures necessary to protect the environment may conflict with the provisions of the Agreement, and recommends to the Council for Trade in Services that, at its first meeting, it should adopt a decision requesting the Committee on Trade and Environment to examine Article XIV of GATS. Such an examination should be undertaken in order to determine whether any modification to Article XIV is required to take account of the above-mentioned measures, and whether recommendations should be made on the relationship between services trade and the

environment, including the issue of sustainable development. The Committee should also examine the relevance of intergovernmental agreements on the environment and their relationship to the Agreement.

The Decision on Certain Dispute Settlement Procedures for GATS relates to dispute settlement panels. The Decision provides that the panels should be composed of governmental and/or non-governmental individuals with experience in issues relating to GATS and/or trade in services, including associated regulatory matters. Panels for disputes in specific sectors should have the necessary expertise relevant to the specific sector concerned.

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## U. The problems of assessing the impact of the results of the negotiations on specific commitments

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It is difficult to establish criteria and parameters for an evaluation of the "value" of concessions and the estimation of their "trade impact" and of the impact of liberalization in the services sector. The impact of the specific commitments should be evaluated in overall terms and on a sectoral basis with reference to the objectives of GATS, including those set out in Article IV:1 and Article XIX:3. The objectives of the negotiations on trade in services are laid down in the Punta del Este Declaration and the Preamble to GATS. They are, in particular, to establish a multilateral framework of principles and rules for trade in services with a view to the expansion of such trade under conditions of transparency and progressive liberalization and as a means of promoting the economic growth of all trading partners and the development of developing countries.

The impact of the specific commitments on market access and national treatment will be a function of the extent to which: (i) services sectors and subsectors have been included in individual schedules; (ii) all modes of supply are bound; (iii) market access and national treatment in the transactions listed are limited or qualified; (iv) economic needs test requirements are included without specifying objective criteria; and (v) exemptions to the MFN are entered. The impact of the commitments has to be addressed in the context of the existing domestic regulatory framework, taking into account whether the country concerned has

introduced legislative changes to implement the commitments it has undertaken. A meaningful assessment would also require appropriate disaggregated statistical data on services trade through all modes of supply and a study of the impact of the barriers to entry. Given that disaggregated statistical data on production, trade and foreign direct investment (in the case of the two latter on the basis of origin and destination) are not available, that negotiations have not been concluded on major sectors and a mode of supply, and that objective criteria to weigh offers are lacking, only a very general and qualitative analysis of specific commitments can be undertaken at this stage. Moreover, it should be noted that even if disaggregated statistics were available and comparable across countries, the complexities associated with quantifying barriers and limitations to market access or national treatment and the bindings on different modes of supply would preclude the development of quantifiable criteria, as in the case of tariffs used in trade in goods. Thus, there are no quantifiable values available for either the existing level of market access or for the proposed liberalization.

By 15 December 1993, 96 countries had submitted their schedules of specific commitments. Most of the offers (i.e. 61) are accompanied by an MFN exemption list. The offers vary widely in sectoral coverage, extent of limitations to market access and national treatment and modes of supply coverage. The degree of

development of the services sector is reflected in the coverage of the sectors offered. Whereas some of the least developed countries have offered only one sector, many developing and developed countries have put forward comprehensive offers covering most sectors. The majority of offers cover tourism services. Sectors with a high degree of coverage in the specific commitments include business services, transport services, communications services, and financial services. Sectors with a low degree of coverage include construction, distribution, education, environment, health, and recreational services. It should be noted that many developing countries improved their offers significantly in the course of the negotiations by adding more sectors and removing market access and national treatment limitations.

Most offers of both the developed and developing countries provide a standstill on a wide range of sectors, although the standstill often incorporates important qualifications and limitations, such as nationality and residence requirements, limited equity participation, exclusion of acquisitions, etc. The extent to which the commitments actually provide a rollback of restrictions can only be determined by an analysis of the legislative changes introduced by members to implement their concessions. However, even the consolidation of the status quo through the application of the MFN clause, and the specific market access and national treatment commitments made in specific sectors and subsectors by guaranteeing security of access, will expand trade and investment in services. Given the fact that the developing countries have a weaker services sector, their offers include a more limited number of sectors than the offers of the developed countries examined. It should be noted that certain developed countries have excluded some important services sectors, for example audiovisual (e.g. EC), maritime services (e.g. USA), and specific subsectors in financial services and business services (e.g. Japan).

The modes of supply most frequently included in the schedules of commitments are those of commercial presence and movement of consumers. The mode of supply through cross-border trade has been left unbound in many offers because of lack of feasibility or because commercial presence is preferred (e.g. EC, in some business services subsectors). The movement of natural persons mode of supply has been offered in nearly all schedules through

"horizontal" concessions in the limited category of intracorporate transferees (managers, specialists, executives) and business visitors, which is linked to commercial presence but is without sectoral specificity.

A few countries have offered access for additional categories of natural persons.<sup>239</sup> Canada has offered access to "contract related natural persons" providing services that cover engineers, agrologists, architects, forestry professionals, geomatics professionals and land surveyors for a period of three months; and the United States has offered "fashion models and specialty occupations" up to 65,000 persons annually on a worldwide basis in occupations requiring highly specialized knowledge, full state licensing and very strict conditions, i.e. the employer has taken steps to recruit and train sufficient United States workers in the specialty occupation, entry is limited to three years. Japan provides access to natural persons engaged in some specific aspects of legal services, accounting, auditing, bookkeeping and taxation for a period not exceeding five years. Certain developed countries withdrew some of their horizontal categories at the last stage of the negotiations; for example, Switzerland withdrew the category of "other natural persons supplying services" who are employees of an enterprise that does not have a commercial presence in Switzerland but have a contract with a Swiss consumer of services, and Canada withdrew its offer on computer systems analysts. Many of the offers by developed countries, e.g. EC and the Nordic countries as regards the business sector, have nationality or residence requirements that render access very difficult.

Most developed countries have therefore made horizontal offers regarding the movement of natural persons, accepting commitments with respect to intracorporate transferees - executives, managers, specialists and business representatives - with very little specificity in terms of sectors or occupational categories (although more stringent requirements are imposed in certain sectors). In many cases, these bindings only cover a small proportion of the various visa categories for temporary entry.<sup>240</sup> Movement of persons in categories other than managers, specialists and executives is unbound, despite the fact that the developing countries have repeatedly included this mode of supply in their requests. Such offers could be advantageous to the firms of a few develop-

<sup>239</sup> Some developing countries offered access for additional categories, in particular *independent* professionals, e.g. Malaysia, Argentina and India.

<sup>240</sup> For more details on temporary movement of persons see UNCTAD secretariat document TD/B/CN.4/24, which elaborates on domestic legislation on movement of persons and international regimes based on regional arrangements and bilateral agreements.

ing countries, but obviously would be of greater benefit to other developed countries. These offers, in their present form, do not provide any security of access for developing country service suppliers, regardless of their skills, to be recruited for special assignments, and the lack of indications of sectoral or occupational category makes it difficult to assess the value of the offers to the developing countries and design a serious export capacity.<sup>241</sup> It should be noted that, in the area of access to distribution channels and information networks, the offers of some developed countries (e.g. United States, Canada, Switzerland) omit access to computer reservation systems.

The emphasis in most offers made by the developed countries is on commercial presence mode of supply and movement of persons in the form of intracorporate transferees. Few developing countries are in a position to benefit from the commercial presence mode of supply, given the high cost of establishment in devel-

oped countries and the weaknesses of the developing countries' firms in terms of financial and human capital and access to distribution networks and information channels and technology.

Sectors of particular interest to developing countries, most of which require the movement of persons other than specialists, executives and managers, such as tourism-related services, construction and engineering, business services, health-related services and maritime transport, are included in the offers of the developed countries examined. However, only top management personnel are allowed to move to provide such services. Moreover, the negotiations on maritime, basic telecommunications and financial services and mode of supply of natural persons are continuing. It should be noted that in the financial services sector the United States is pursuing the opening of markets in, for example, Japan and the ASEAN countries.

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## V. Conclusions

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Negotiations are continuing on the specific commitments, particularly in three major sectors, namely financial services, maritime services and basic telecommunication services, as well as on the mode of supply of movement of natural persons, which is of particular interest to developing countries. These negotiations will provide developing countries with the final opportunity to pursue their requests in the area of movement of persons in this Round of negotiations. It should be noted, however, that in the negotiations on the three sectors the developing countries are under very heavy pressure to offer even more market access to developed countries. Once the negotiations on the major sectors mentioned above, on the movement of natural persons and on exemptions to the MFN have been concluded, it will be possible for the results of the negotiations on trade in services to be fully evaluated.

Although in this Round of negotiations developing countries may not have obtained commitments of major economic value to them for the reasons mentioned above, the Agree-

ment establishes a framework within which developing countries can obtain reciprocity for liberalization of trade in services, including access for foreign direct investment in the services sector in the form of improved access for services of interest to them, such as movement of persons. It provides a mechanism for them to win "credit" for liberalization in services which has largely been unilateral in the past. They can also negotiate specific commitments with respect to transfer of technology, access to distribution channels, etc. What they can actually obtain in future negotiations will be a function of the preparedness of governments and the skills of their negotiators. Another major achievement is that GATS clearly establishes the rights and obligations of members, with particular reference to the fact that they have no commitments regarding market access and national treatment other than those that have been specified in their schedules. This should shield them from bilateral pressures for further unilateral liberalization from major trading powers. ■

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<sup>241</sup> The GATT evaluation of the results of the Round emphasizes the benefits achieved through the commercial presence mode of supply, that is, investment in services sectors of developing countries, and deemphasizes the movement of persons mode of supply that would provide market access for developing countries to markets of developed countries. See GATT document MTN.TNC/W/122, 29 November 1993.

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## AGREEMENT ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS

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### A. Introduction

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The purpose of this chapter is to examine the Agreement on TRIPS with a view to assessing its implications, particularly for developing countries. The chapter deals first with an overview of the negotiation process, its main aspects and direction, followed by an analysis

of the content of the Agreement and a discussion of the possible impact the new standards could have on developing countries. In this context, it attempts to assess the possible costs associated with the implementation and enforcement measures of the Agreement.

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### B. Background

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Technological advances and their rapid diffusion, especially in the area of information, have contributed to the creation of new markets and the transformation of innovation and production processes. Information technologies have radically altered the nature of competition due to the inherent vulnerability of such technologies to rapid appropriation.<sup>242</sup> Moreover, the growing technological capacity of some developing countries enabled them to penetrate distant markets for a range of industrial goods, thereby disrupting the equilibrium that had resulted from more traditional comparative advantages in the production of in-

dustrial products. These changes and the attendant shift towards global competition necessitate a continued search for alternative strategies by enterprises and for improved policy instruments by Governments. Therefore, the international convergence of technological capabilities<sup>243</sup> among developed and a limited number of developing countries and the gradual erosion of competitiveness in the traditional areas of production of a number of developed countries have made intellectual property a new basis of comparative advantage.<sup>244</sup> The lack of, or weak protection of intellectual property in several countries led to a series of trade ten-

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<sup>242</sup> "Laws and regulations dealing with transfer and development of technology: An overview", report by the UNCTAD secretariat (TD/B/WG.5/10), 4 February 1994, para. 4.

<sup>243</sup> See R. Lawrence, "Futures for the world trading system and their implications for developing countries" in M.R. Agosin and D. Tussie (eds.), *Trade and Growth: New Dilemmas in Trade Policy* (New York: St. Martin's Press, 1993), p. 43.

<sup>244</sup> See A. Subramanian, "The international economics of intellectual property rights protection: A welfare - theoretic trade policy analysis", *World Development*, Vol. 19, No. 8 (1991), p. 945.

sions and, in certain cases, retaliation. The United States Trade and Tariff Act of 1984 tied the application of the generalized system of preferences (GSP) to developing countries to the willingness of those countries to provide "adequate and effective" protection for IPRs. Section 301 of the Act allowed the President to limit trade from those countries in the case of unjustifiable or unreasonable trade practices. In 1988, the Omnibus Trade and Competitiveness Act extended this action further by authorizing the United States Trade Representative (through the so-called "Special 301") to draw up a list of countries that had been given deadlines for an improvement of their IPRs protection and threatened them with sanctions should such improvements not occur. The European Union (EU) has also pursued intellectual property objectives in its dealings with developing countries, notwithstanding its reservation about unilateral actions to obtain adequate and effective protection. EU activities in this field were facilitated by the adoption in 1984 of a set of new trade policy instruments.<sup>245</sup>

Trade tensions thus prompted consideration of the issue of trade implications of intellectual property at the multilateral level. In this context, the most comprehensive and far-reaching multilateral efforts to establish international standards of intellectual property protection have been channelled through the TRIPS negotiations in the Uruguay Round.

The Ministerial Declaration on the Uruguay Round set the objectives of the negotiations as follows: "In order to reduce the distortions and impediments to international trade, and taking into account the need to promote effective and adequate protection of intellectual property rights, and to ensure that measures and procedures to enforce intellectual property rights do not themselves become barriers to legitimate trade, the negotiations shall aim to clarify GATT's provisions and elaborate as appropriate new rules and disciplines".<sup>246</sup>

It was against this background that, for the first time, the protection of intellectual property rights was discussed within multilat-

eral trade negotiations which aimed at linking intellectual property rights to multilateral trade rights and obligations as a component of the international trading system. It should be remembered that the subject of intellectual property protection was first introduced into the GATT negotiations during the Tokyo Round in 1978 on the basis of a draft proposal put forward by the United States and the European Communities (EC), with specific regard to anti-counterfeiting measures. As no agreement was reached at that time, the United States circulated a new draft in 1982, and a GATT Group of Experts held several meetings on the matter in 1985.<sup>247</sup>

Countries recognized the damage that counterfeiting might cause to legitimate vendors in terms of direct sales losses and lost reputation, and they also acknowledged the producers' need for incentives to maintain high quality standards. Because the issue of counterfeiting did not normally involve technological undertakings, the developing countries found it easier to address the latter issues than those concerning substantive standards of protection dealt with in existing international treaties and administered by specialized agencies in this field.<sup>248</sup> Moreover, it was realized that the practice of counterfeiting did not confer advantages in terms of national policy aimed at building up industrial and technological capabilities. However, owing to the insistence of the developed countries, the discussions at the TRIPS negotiations centred more on the establishment of substantive and uniform standards involving a higher level of protection for intellectual property rights.<sup>249</sup> In this respect, the attitudes of developed and developing countries evolved considerably in the process of negotiation.

The developing countries were initially prepared to discuss only the clarification of existing GATT rules and provisions dealing with intellectual property, such as Articles IX and XX (d) and measures to restrict trade in counterfeit goods that could be understood as clarifying Article 9 of the Paris Convention, which deals with the seizure, on importation, of goods unlawfully bearing a mark or trade

<sup>245</sup> See *Trade and Development Report, 1991* (UNCTAD/TDR/11) (United Nations publication, Sales No. E.91.II.D.15), Part Three, chap. III.

<sup>246</sup> The Declaration also stated that "Negotiations shall aim to develop a multilateral framework of principles, rules and disciplines dealing with international trade in counterfeit goods, taking into account work already undertaken in the GATT. These negotiations shall be without prejudice to other complementary initiatives that may be taken in the World Intellectual Property Organization and elsewhere to deal with these matters". Ministerial Declaration on the Uruguay Round, GATT document MIN.DEC (20 September 1986).

<sup>247</sup> See T. Stewart (ed.), *The GATT Uruguay Round: A Negotiating History (1986-1992)* (Deventer (Netherlands), Boston: Kluwer Law and Taxation Publishers, 1993), Vol. II, Trade-related intellectual property rights, p. 15.

<sup>248</sup> See *TDR 1991*, p. 185.

<sup>249</sup> *Ibid.*



name. They regarded any discussion of substantive intellectual property norms as beyond the competence of GATT and within the exclusive jurisdiction of the World Intellectual Property Organization.<sup>250</sup> Developed countries, on the other hand, interpreted the Punta del Este Declaration as allowing for the elaboration of new substantive rules of international intellectual property law. After two years of analysis and discussion, at the Mid-Term Review in December 1988 at Montreal and at the senior officials meeting of April 1989 in Geneva, the mandate was clarified by explicit reference to the elaboration of adequate standards including relevant international agreements, dispute prevention and settlement, and transitional arrangements. In this respect, a number of developed countries made detailed written submissions concerning the international minimum standards for the protection of intellectual property.<sup>251</sup> Their submissions generally centred on the premise that inadequate, excessive and discriminatory protection of intellectual property rights could or might constitute a major distortion of and impediment to trade and should as such be dealt with within the framework of GATT.<sup>252</sup> They indicated their preference for an integral package deal that would require all contracting parties to accept the results of the Uruguay Round as a whole and that would deny single States the right to choose which of the various agreements they wished to adhere to. This view had offered the "possibility of trade-offs between subjects, so that States that see themselves as making concessions in one area can seek countervailing benefits in others".<sup>253</sup> In addition, a "single undertaking" implied that countries become liable to cross-sectoral retaliation for non-

compliance with prescriptive norms governing intellectual property rights.

Signalling an evolution in their initial position with regard to the negotiating mandate within GATT, a group of 14 developing countries submitted detailed proposals covering trade in counterfeit and pirated goods, and standards and principles concerning the availability, scope and use of intellectual property rights.<sup>254</sup> The proposals included various elements related to the scope of patentability, duration of patents, compulsory licensing and the control of anti-competitive practices that, in their view, should have been part of the outcome of the negotiations on TRIPS. This was a crucial element for the negotiations; it enabled the Chairman of the Negotiating Group to consolidate the various texts and prepare a comprehensive proposal for the purposes of discussion at the Brussels Ministerial Meeting in December 1990, and finally made it possible to successfully conclude the negotiations on TRIPS on 15 December 1993.

The entire process should be viewed against the recent technology-related developments and trends that have radically altered the nature and tone of the debate on intellectual property rights.<sup>255</sup> Indeed, intangible creations with major knowledge components are likely to become the most valuable form of property in the twenty-first century, and global economic integration will require these creations to be adequately protected.<sup>256</sup> The historical trend for purely territorial intellectual property rights will thus give way to norms of international economic law which should ideally aim at achieving a fair balance between the interests of economic actors and countries at different stages of development.

<sup>250</sup> See J.H. Reichman, "Intellectual property in international trade: Opportunities and risks of a GATT connection", *Vanderbilt Journal of Transnational Law*, Vol. 22, No. 4 (1989), pp. 828-860.

<sup>251</sup> The first draft proposal was submitted by the EEC. Additional proposals followed by the United States, Switzerland and Japan. See "Draft Agreement on trade-related aspects of intellectual property", Communication from the European Communities, GATT document MTN.GNG.NG11/W/68 (29 March 1990); "Draft Agreement on trade-related aspects of intellectual property rights", Communication from the United States, GATT document MTN.GNG.NG11/W/70 (11 May 1990); "Draft amendment to the General Agreement on Tariffs and Trade on the protection of trade-related intellectual property rights", Communication from Switzerland, GATT document MTN.GNG.NG11/W/73 (14 May 1990); and "Main elements of a legal text for TRIPS", Communication from Japan, GATT document MTN.GNG.NG11/W/74 (15 May 1990).

<sup>252</sup> See A. Yusuf, "Developing countries and trade-related aspects of intellectual property rights" in UNCTAD, *Uruguay Round, Papers on Selected Issues* (UNCTAD/ITP/10), 1989, p. 185. See also R.M. Gadbar and T.J. Richards (eds.), *Intellectual Property Rights. Global Consensus, Global Conflicts?* (London: Westview Press, 1988), pp. 18-38.

<sup>253</sup> See D. Hartridge and A. Subramanian, "Intellectual property rights: The issues in GATT", *Vanderbilt Journal of Transnational Law*, Vol. 22, No. 4 (1989), p. 898.

<sup>254</sup> See "Communication from Argentina, Brazil, Chile, China, Colombia, Cuba, Egypt, India, Nigeria, Peru, Tanzania and Uruguay", GATT document MTN.GNG.NG11/W/71, 14 May 1990.

<sup>255</sup> P. Roffe, "Technology issues in the international agenda: A review of two decades of multilateral deliberations in the United Nations and GATT", in R. Wolfrum (ed.), *Law of the Sea at the Crossroads: The Continuing Search for a Universally Accepted Regime* (Berlin: Duncker and Humblot, 1991), p. 301.

<sup>256</sup> See J. H. Reichman, "Implications of the draft TRIPs Agreement for developing countries as competitors in an integrated world market" (UNCTAD/OSG/DP/73), November 1993, p. 41.

## C. Content of the Agreement

### 1. Basic principles

The Final Act embodying the results of the Uruguay Round of 15 April 1994 contains, in Annex IC, the Agreement on Trade-Related Aspects of Intellectual Property Rights (hereinafter called the "Agreement").<sup>257</sup> The Agreement recognizes that, in order to reduce distortions and impediments to international trade, and to ensure that measures and procedures to enforce intellectual property rights do not themselves become barriers to legitimate trade, new rules and disciplines are needed. To this end, the Agreement addresses the applicability of the basic principles of GATT and those relevant to intellectual property rights, the provision of effective enforcement measures for those rights, multilateral disputes settlement, and transitional arrangements. The Agreement establishes minimum universal standards on patents, copyrights, trademarks, industrial designs, geographical indications, integrated circuits and undisclosed information. It supplements the basic agreements in the field of intellectual property with the harmonizing effects of the substantive rules on intellectual property rights. In setting out general provisions and basic principles, the Agreement introduces, in addition to the well-established principle of national treatment, that of "most-favoured-nation" treatment, a novelty in international intellectual property regimes, whereby any advantage a member grants to the nationals of any other country must be extended immediately and unconditionally to the nationals of all other members.

The basic principles refer to criteria and objectives of special interest to developing countries, namely, the contribution that the protection and enforcement of intellectual property rights should make to the promotion of technological innovation and to the transfer and dissemination of technology, and the measures that countries may adopt to protect

public health and nutrition and to promote public interest in sectors of vital importance to their socio-economic and technological development. These principles also establish that appropriate measures may be needed to prevent the abuse of intellectual property rights or practices which unreasonably restrain trade or adversely affect the international transfer of technology.

In respect of each category of intellectual property rights, the Agreement<sup>258</sup> builds on the main existing international conventions in the field, and specifies a number of higher and additional standards of protection. In the following paragraphs, an attempt is made to define and highlight the key issues of intellectual property protection covered by the Agreement.

### 2. Patents

Provisions on protection of patents are among the most important aspects of the Agreement, with substantial changes as compared to the *ex ante* situation. The issue of patentability and exclusion therefrom has constituted one of the key areas in the discussions on the Agreement. At the start of the negotiations in 1986, approximately 50 countries did not confer full patent protection on pharmaceuticals. This was also the case, in some instances, of food and beverages. Since then, however, important legislative changes have taken place in many developing countries within the framework of the economic and trade liberalization process which these countries are undergoing. For instance, changes in patent legislation with respect to pharmaceuticals have been introduced in Bolivia, China, Chile, Colombia, Ecuador, Indonesia, Mexico, Peru, the Republic of Korea and Venezuela.<sup>259</sup> Other countries are likely to follow the same

<sup>257</sup> The Uruguay Round of Multilateral Trade Negotiations, Trade Negotiations Committee, *Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations*, Marrakesh, Morocco, 15 April 1994.

<sup>258</sup> The structure of the Agreement is the following: Part I: General provisions and basic principles; Part II: Standards concerning the availability, scope and use of intellectual property rights; Part III: Enforcement of intellectual property rights; Part IV: Acquisition and maintenance of intellectual property rights and related *inter-partes* procedures; Part V: Dispute prevention and settlement; Part VI: Transitional arrangements; and Part VII: Institutional arrangements; Final provisions.

<sup>259</sup> "Laws and regulations..." (TD/B/WG.5/10), paras. 26-28.

path, even before the entry into force of the Agreement.<sup>260</sup> Notwithstanding this trend, the Agreement introduces a number of new obligations in the area of patents as in the case of other categories of intellectual property, which are examined later.

#### (a) Patentable subject-matter

As provided in Article 27:1 of the Agreement, protection will be available for any inventions, whether products or processes, in all fields of technology without discrimination as to the place of invention, the field of technology and whether products are imported or locally produced. Under this Article, a major shift occurred in the position of many developing countries which resolved one of the most conflictual issues of intellectual property diplomacy in the 1970s and 1980s, namely, that patentability will be extended to all types of inventions, independently of the industrial sector or field of technology to which they belong. Moreover, any differential treatment based on the place where the invention is made will not be allowed. However, inventions may be excluded from patentability if their commercial exploitation is prohibited for reasons of *ordre public* or morality. Their exclusion is also possible on the grounds of protecting human, animal or plant life or avoiding serious prejudice to the environment. Exclusions based on general reasons related to economic development will no longer be permitted.<sup>261</sup>

In addition, the Agreement allows for exclusions from patentability for diagnostic, therapeutic and surgical methods for the treatment of humans or animals, and for plants and animals (other than micro-organisms), as well as for essentially biological processes for the production of plants or animals (other than microbiological or non-biological processes). Plant varieties, however, must be protectable either by patents, a *sui generis* system or by any combination of the two. The choice for the protection of plant varieties reflects the difference existing between the legislation of the United States, on the one hand, where some plant varieties are patentable, and that of most European countries, on the other, where plant varieties are only protectable by a *sui generis*

system. It should be noted that intellectual property protection in the area of living matter is still in its early years of development. For that reason Article 27:3(b) of the Agreement calls for a review four years after the date of entry into force of the Agreement. The review will thus take place one year before the end of the five-year transitional period of the Agreement on TRIPS for developing countries (see below). This waiting period illustrates the difficulties confronting negotiators in respect of the biotechnology-related issues and the need for further in-depth examination of these issues.

Actually, the aim in the Agreement is to limit the exclusion of patentability to naturally occurring and traditional breeding methods, while preserving the possibility of obtaining protection for developments based on cell manipulation or, with advances in biotechnology, the transfer of genes. The Agreement does not take a position with regard to biological materials that already exist in nature. Indeed, in many developed countries, patentability could be extended to a naturally occurring substance provided that it is isolated or presented in a purified form. A debate is going on in this respect in developed countries concerning the possibility of obtaining patent protection for natural-product-based inventions, which reflects the long-term importance of this aspect.<sup>262</sup> In contrast, in developing countries, Decision 313 of the Andean Group, for example, states that biological material that already exists in nature is not considered an "invention" and is therefore not patentable.<sup>263</sup> Similarly, the Agreement on TRIPS does not provide guidance on how to solve the problem of disclosure in the case of inventions that consist of or are based on biological material that cannot be fully described. In this case it appears that countries could impose the obligation to deposit a sample of the relevant biological material in order to supplement the descriptions and facilitate access to it.

In respect of the duration of patents, the Agreement calls for a minimum period of 20 years of patent protection. This would have a worldwide harmonizing effect and exclude shorter terms of protection in respect of certain areas of technology, or based on the extent of exploitation of the invention, or on any other grounds.<sup>264</sup>

<sup>260</sup> Such as Argentina. See the *Financial Times*, 10 May 1994.

<sup>261</sup> Similarly, exclusions used to be permitted by Decision 85 of the Andean Group.

<sup>262</sup> See M. Gollin, "Patenting recipes from nature's kitchen", *Bio/Technology*, Vol. 12, April 1994, p. 406.

<sup>263</sup> "Laws and regulations..." (TD/B/WG.5/10), para. 43.

<sup>264</sup> See *Intellectual Property Rights and Foreign Direct Investment* (ST/CTC/SER.A/24) (United Nations publication, Sales No.93.II.A.10), 1993, p. 14.

### (b) *Compulsory licensing*

On one of the important, and controversial, elements of the patent system, the Agreement lays down detailed conditions for the use of patents without the authorization of the patent owner. The question of compulsory licensing referred to in Article 31 concerning "Other Use Without Authorization of the Right Holder"<sup>265</sup> was a significant and controversial issue in the TRIPs negotiations. One of the main aspects was in relation to the provisions in intellectual property laws that require a patent to "be worked" in the territory where the patent was granted within a specified period (three to five years) of the grant. In practice, the application of these provisions has been rather limited.<sup>266</sup> The Agreement does not prohibit the granting of compulsory licensing; it only sets out the conditions to be met where the law of a country allows use without the authorization of the right holder. Compulsory licences may, therefore, be contemplated on any grounds. Public health and nutrition have been recognized explicitly in Article 8 and, in addition, Article 31 contains some special provisions related to other grounds, namely, national emergency and extreme urgency; public non-commercial use; anti-competitive practices; and the exploitation of a dependent patent. In this respect, the second sentence of Article 27:1, which prohibits discrimination in patent protection based on the place of invention, the field of technology or whether products are imported or locally produced, should also be taken into account.

As mentioned before, the Agreement focuses particular attention on the conditions under which a compulsory licence may be granted. A requirement that many legislations have so far omitted, particularly in cases of licences granted on the grounds of public interest, refers to efforts to be made for obtaining authorization from the owner of the patent on reasonable terms and conditions prior to granting a licence. If such efforts have not been successful within a reasonable period of time, a compulsory licence could be granted (provided other conditions are also met) and the patent owner be paid an adequate remuneration, taking into account the economic value of the licence. An additional important innovation is the introduction of the principle according to which a compulsory licence is liable to be terminated when "the circumstances which led to it cease to exist and are unlikely to recur" (Article 31 (g)). For this

reason the competent authorities should have the power to review, upon a motivated request, the continued existence of such circumstances. In these cases, the interests of the licensee who has invested in exploiting the licence should be protected. Finally, mention should be made of a condition under which the patent owner should be given the possibility of a review, by a judicial or other higher authority, of the legal validity of any decision relating to the granting of a licence as well as to the determination of adequate remuneration.

### (c) *Reversal of the burden of proof*

As indicated earlier, the Agreement sets forth the rights that a patent should confer on the title-holder for any invention, whether it is a product or process. The category of product patents has been significantly strengthened. The Agreement extends the protection conferred on a process to the product "obtained directly by that process" (Article 28). In addition, the reversal of the burden of proof is provided in civil litigation involving process patents. The extension of protection, coupled with a procedural remedy, such as the reversal of the burden of proof, has not yet been recognized by most legislation in the area of intellectual property. In court proceedings, even though in principle it is for the party alleging a breach of law to prove its case, the Agreement authorizes the judicial authorities to order the defendant to prove that the process used to obtain an identical product is different from the patented process. Provisions on this question establish a presumption that "any identical product when produced without the consent of the patent owner shall, in the absence of proof to the contrary, be deemed to have been obtained by the patented process: (a) if the product obtained by the patented process is new; (b) if there is a substantial likelihood that the identical product was made by the process" (Article 34).

## 3. *Other categories of IPRs*

Among other categories of IPRs, the Agreement covers copyright and related rights, trademarks, geographical indications, undisclosed information such as trade secrets, industrial designs, and the layout-designs of

<sup>265</sup> In the sense of other use than that allowed under Article 30 dealing with "Exceptions to Rights Conferred".

<sup>266</sup> See Reichman, "Implications of the draft TRIPs Agreement...", *op. cit.*, p. 18 and Note 105.

integrated circuits. This subsection briefly refers to each of these categories.

#### (a) *Copyright and related rights*

With respect to this category of intellectual property rights, the Agreement provides that parties should comply with the substantive provisions of the Berne Convention for the Protection of Literary and Artistic Works (as revised in 1971), though they are not required by the Agreement to protect moral rights as stipulated in that Convention. They may, of course, be obliged to do so under the Berne Convention itself. Eligible works must be protected on the basis of their expression as a literary or artistic work, not on the basis of the idea, procedure, method of operation or mathematical concept behind them as such. The Agreement clearly opts for copyright protection of computer programs, and provides for protection of these as literary works under the Berne Convention. It also specifies the conditions under which compilations of data should be protected by copyright.<sup>267</sup> Another important addition to existing international rules in the area of copyright and related rights concerns the provisions on rental rights, under which the title-holders of computer programs and sound recordings must have the right to authorize or prohibit the commercial rental of their works to the public. In principle, this obligation also applies with respect to cinematographic works, but if reproduction rights are not materially impaired by widespread copying of these works, an exception to that obligation can be invoked.

Specific provisions are also introduced in the Agreement for the protection of the performers, who will at least be accorded the legal possibility of preventing unauthorized fixation of unfixed performance, reproduction of such fixation of their performance, as well as unauthorized broadcasting by wireless means and communication to the public of their performance. However, they are not necessarily entitled to an exclusive right in respect of those performances. Producers of sound recordings will enjoy exclusive reproduction rights. Broadcasting organizations will have exclusive rights to prohibit unauthorized fixation of broadcasts and reproduction and rebroadcasting by wireless means, as well as communication to the public of television broadcasting.

The term of protection for performers and producers of phonograms is extended from 20 to 50 years. These provisions represent a step forward in the international recognition of these categories of right holders. However, "conditions, limitations, exceptions and reservations" as stipulated in the Rome Convention of 1961 for the protection of performers, producers of phonograms and broadcasting organizations, remain valid. These enable countries, for example, to impose reciprocity in some respects or to permit both private use and use for the purposes of teaching and scientific research with remuneration.

It should also be noted that, according to Article 61 of the Agreement, countries must provide for "criminal procedures and penalties" in cases of "copyright piracy on a commercial scale". Remedies must include imprisonment and/or monetary fines sufficient to provide a deterrent and, in appropriate cases, will also include the seizure, forfeiture and destruction of the infringing goods.

#### (b) *Trademarks*

In respect of trademarks, the Agreement gives pre-existing norms greater specificity in supplementing the Paris Convention, in particular. It provides equal treatment to trade and service marks. Any sign that is capable of distinguishing goods or services of one enterprise from those of other enterprises will be eligible for registration as a trademark. In respect of certain signs, it may be necessary that they first acquire such capability through use. Only signs that are not visually perceptible may be denied this eligibility altogether. Specific protection is given to marks that have become well-known in a particular country. In this respect, the Agreement, adding to Article 6bis of the Paris Convention, goes some way towards clarifying the issue of how to determine whether a mark is well known. It is indicated that account should be taken of the knowledge of the mark in the relevant sector of the public, including knowledge resulting from promotion, i.e. extensive advertising. With regard to the requirements for the use of trademarks, the Agreement lays down a number of obligations. The requirement that a mark be used in conjunction with another mark is, in principle, not allowed.<sup>268</sup> Moreover, while countries may

<sup>267</sup> Article 10:2 provides that "Compilations of data or other material ... which by reason of the selection or arrangement of their contents constitute intellectual creations shall be protected as such. Such protection, which shall not extend to the data or material itself, shall be without prejudice to any copyright subsisting in the data or material itself".

<sup>268</sup> This was a practice followed during the 1970s and 1980s in many developing countries. In using the local marks in conjunction with foreign marks, it was intended to create "goodwill" for the former.

elaborate conditions on licensing, the compulsory licensing of trademarks is not permitted.

### (c) *Geographical indications*

The Agreement establishes protection of the indications which identify a good as originating in a country, or a region or locality where a given quality, reputation or other characteristic of the good is essentially attributed to its geographical origin. It should be mentioned that any characteristic of a good which is attributable to its geographical origin, including reputation, can constitute protection. Countries are called upon to provide legal means to prevent the use of any indication in the designation or presentation of a good that misleads the public as to the origin of the good, as well as to prevent any use that constitutes an act of unfair competition.<sup>269</sup> Higher standards apply to geographical indications for wines and spirits, which are protected even where the public is not misled as to the true origin of the goods. This broad protection is, however, balanced by provisions which allow countries to make exceptions for names that have become generic in their territory, for pre-existing trademarks and for products of certain firms of longstanding prior use. These countries should, however, be willing to negotiate further, whether or not these exceptions continue to apply in their territories. In order to facilitate protection, provisions are made for further negotiations within the Council for TRIPS for the establishment of a multilateral system of notification and registration of geographical indications for wines.

### (d) *Trade secrets and other undisclosed information*

It is particularly significant that the Agreement establishes protection for trade secrets. This is the first time, in a multilateral agreement, that trade secrets are specifically treated as a category of "intellectual property".<sup>270</sup> However, their legal treatment is within the context of the discipline of unfair competition as regulated by Article 10 bis of the Paris

Convention and it does not imply any obligation to confer exclusive rights.<sup>271</sup> Countries are required to establish two essential forms of protection. First, trade secrets that have a commercial value will be protected against breach of confidence and other acts contrary to honest commercial practices. Trade secrets that are voluntarily revealed, insufficiently guarded or reverse-engineered will lose all protection and become subject to free competition. Therefore, trade secrets may be regarded, in certain instances, as an incentive to develop incremental innovations not meeting the standard of patents.<sup>272</sup> Second, the Agreement also provides protection for undisclosed test or other data submitted to governments or governmental agencies in order to obtain marketing approval for pharmaceutical or agricultural chemical products which utilize new chemical entities.<sup>273</sup> However, in order to qualify for protection against unfair commercial use, the origination of such data should involve a "considerable effort" by the data producers.

### (e) *Industrial designs*

The Agreement contains a number of basic rules about the way in which industrial designs should be protected.<sup>274</sup> Protection will be provided for independently created industrial designs that are new or original. Owners of protected designs will have the right to prevent the manufacture, sale or importation of articles bearing or embodying a design which is a copy of the protected design. However, the Agreement makes it possible not to extend protection to designs dictated essentially by technical or functional considerations. With regard to textile designs, requirements for securing protection, in particular with regard to cost, examination or publication, should not unreasonably impair the opportunity to seek and obtain such protection. It is up to each country to decide whether to meet this requirement through copyright law or industrial design law. For industrial designs, the duration of protection under the Agreement will amount to at least 10 years.

During the negotiations the problem of the relevance of novelty and originality to pro-

<sup>269</sup> See Article 22:2 of the Agreement.

<sup>270</sup> The North American Free Trade Agreement (NAFTA) was the first international agreement (at the regional level) to provide protection for trade secrets. See "Laws and regulations..." (TD/B/WG.5/10), para. 44.

<sup>271</sup> Article 10bis of the Paris Convention stipulates that countries "are bound to assure to nationals of such countries effective protection against unfair competition".

<sup>272</sup> See Reichman, "Implications of the draft TRIPs Agreement...", *op. cit.*, p. 32.

<sup>273</sup> See Article 39:3 of the Agreement.

<sup>274</sup> Articles 25 and 26 of the Agreement.

tection was raised. A number of countries favoured a cumulative test (designs should be new and original). Other countries felt that the cumulative test would be too restrictive. In the final text of the Agreement, the criterion established of "new or original" suggests that it will be easier to obtain protection for a design.<sup>275</sup> The Agreement in establishing a *sui generis* regime permits the eligibility requirements of novelty and originality, but not the tests of non-obviousness and usefulness mentioned in Article 27:1 (see footnote 5 to Article 27). In addition, the Agreement allows countries to exclude from protection designs dictated essentially by technical and functional considerations. The replacement part industry is supportive of such a position as well as consumer groups and insurance companies.<sup>276</sup>

#### (f) *Layout-designs of integrated circuits*

After the United States, the EC and Japan had introduced specific protection for integrated circuit layouts, an international treaty on Intellectual Property in Respect of Integrated Circuits (the Washington Treaty) was concluded and opened for signature in May 1989. The Agreement adopts the major part of the Washington Treaty but with a number of changes. In particular, the rights are extended to articles incorporating infringing layout-designs; innocent purchasers of infringing products are not treated as infringers but, after notice of infringement, must use or sell stock in hand and pay a sum equivalent to a reasonable royalty; and the term of protection is raised from 8 to 10 years from first commercial exploitation or application for registration.<sup>277</sup>

### 4. *Control of anti-competitive practices in contractual licences*

Section 8 of the Agreement provides a basis for maintaining some degree of domestic control over licensing practices. It recognizes

that countries may adopt measures to regulate practices that amount to an abuse of intellectual property rights in accordance with certain established criteria. In doing so, it provides, for the first time in an internationally binding instrument, a number of rules on restrictive practices in licensing contracts. It recognizes that some licensing practices pertaining to intellectual property rights which restrain competition may have adverse effects on trade and may impede the transfer and dissemination of technology (Article 40:1). Therefore, countries are free to specify, in their legislation, "licensing practices or conditions that may in particular cases constitute an abuse of intellectual property rights having an adverse effect on competition in the relevant market". The last qualification, namely "adverse effect on competition" is tantamount to the so-called "competition test" for evaluating practices which may be deemed abusive.<sup>278</sup> The Section in question provides a few examples: exclusive grant-back provisions, i.e. practices which impose an obligation on the licensee to transfer the improvements made on the licensed technology exclusively to the licensor; conditions preventing challenges to the validity of the licensed patent; and coercive package licensing, i.e. practices which impose an obligation on the licensee to acquire from the licensor other technologies or inputs. In this connection, mention should be made of the discussions on an international draft code of conduct on the transfer of technology, which have identified 14 practices that may be deemed anti-competitive: grant-back provisions; challenges to validity; exclusive dealing; restrictions on research; restrictions on use of personnel; price fixing; restrictions on adaptations; exclusive sales or representation agreements; tying arrangements; export restrictions; patent pool or cross-licensing agreements and other arrangements; restrictions on publicity; payments and other obligations after expiration of industrial property rights; and restrictions after expiration of arrangement.<sup>279</sup>

It is clear from Section 8 of the Agreement that the adoption of the exclusive "competition test" in the Agreement has put an end to a long-standing international debate as to how to treat restrictive practices in transactions

<sup>275</sup> Stewart, *op. cit.*, note 383.

<sup>276</sup> *Ibid.*, p. 56.

<sup>277</sup> Regarding compulsory licensing or government use, Article 31(c) provides that the purpose is limited to "public non-commercial use or to remedy a practice determined after judicial or administrative process to be anti-competitive".

<sup>278</sup> See "The sixth session of the United Nations Conference on an international code of conduct on the transfer of technology" - Background Note (TD/CODE TOT/49), p. 5.

<sup>279</sup> See "Draft international code of conduct on the transfer of technology" - Note by the UNCTAD secretariat (TD/CODE TOT/47), pp. 8-10.

pertaining to transfer of technology.<sup>280</sup> At the national level, a recent UNCTAD report suggested that, in developing countries, the treatment of restrictive practices in technology transfer regimes has also been liberalized to varying degrees.<sup>281</sup>

## 5. Enforcement measures

For industrialized countries, the absence of an effective enforcement mechanism within the framework of WIPO Conventions, in particular, the Berne and Paris Conventions, was a major problem in the international protection of intellectual property rights, and the GATT framework was considered by them to offer an appropriate alternative.<sup>282</sup> The Agreement consequently contains a comprehensive set of provisions on the enforcement of intellectual property rights.<sup>283</sup> "General Obligations" call on countries to ensure that procedures and remedies are available under their laws to enable right holders to take action against any act of infringement of intellectual property rights. One of the most significant provisions in this context is that the court should have the authority to order, without the alleged infringer being heard by the court, provisional measures to prevent infringement, to preserve evidence or take other conservatory measures that may be appropriate. The power to stop and even destroy infringing goods at borders is a major enforcement procedure defined in the Agreement. In addition, procedures must not be complicated or costly or entail unreasonable time-limits or unwarranted delays. These obligations have important implications for developing countries, which will be discussed in section D of this chapter.

## 6. Settlement of dispute mechanisms

As indicated earlier, the question of effective mechanisms for the enforcement of

treaty obligations laying down standards for intellectual property rights was a major driving force, particularly among industrialized countries, in the initiative for a multilateral agreement on trade-related aspects of intellectual property rights. The Agreement will consequently establish a Council for Trade-Related Aspects of Intellectual Property Rights,<sup>284</sup> which will monitor the operation of the Agreement and compliance with obligations thereunder. Moreover, a WTO member country, which is of the opinion that another member is not complying with its obligations, would be entitled to bring the matter before the Dispute Settlement Body (DSB) of the WTO. Disputes will be settled in accordance with Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding.<sup>285</sup> In the case of non-compliance by a member country with a DSB ruling, sanctions could be authorized against that country by the General Council of the WTO.

## 7. Transitional arrangements

As observed in the previous paragraphs as regards compliance with the obligations relating to intellectual property protection, the Agreement on TRIPs does not differentiate between countries in respect of their stage of technological development. However, it allows for a general transitional period during which the developing countries and countries in transition are given 5 years, and the least developed countries 11 years, to comply with the provisions of the Agreement.<sup>286</sup> Despite this provision, the obligations to provide national treatment and most-favoured nation treatment will come into effect one year after the general entry into force of the Agreement, which is expected to be 1 January 1995. Where implementation of the Agreement would entail extending product patent protection to a field of technology not previously protected (on the general date of application of the Agreement), an additional transitional period of five years is allowed for the extension of such protection.<sup>287</sup> This will apply to countries which currently do

<sup>280</sup> See "Negotiations on an international code of conduct on the transfer of technology: Consultations carried out in 1992" - Report by the Secretary-General of UNCTAD (TD/CODE TOT/58).

<sup>281</sup> See "Laws and regulations..." (TD/B/WG.5/10), paras. 24 and 30.

<sup>282</sup> See Reichman, "Intellectual property in international trade ...", *op. cit.*, p. 862.

<sup>283</sup> See Articles 41 to 61 of the Agreement.

<sup>284</sup> See Article 68 of the Agreement.

<sup>285</sup> See Article 64:1 of the Agreement.

<sup>286</sup> See Article 65:2 and 65:3 and Article 66:1 of the Agreement.

<sup>287</sup> See Article 65:4 of the Agreement.



not provide protection for pharmaceuticals. In addition, subparagraphs I(b) and I(c) of Article XXIII of GATT 1994 will not apply to the settlement of disputes under the Agreement for a period of five years from the date of entry into force of the WTO Agreement.<sup>288</sup>

### 8. Transitional or "pipeline" protection

The relevance of patent protection for pharmaceuticals and chemicals attracted attention in the debate on TRIPS. In particular, bilateral and multilateral efforts were made to obtain patent protection in a country that denied such protection to pharmaceuticals that were the subject of a pending patent application or had been granted a patent in, for example, the United States, but which had not been marketed in the other country in question.<sup>289</sup> This type of protection, known as "pipeline" protection, would have assured pharmaceutical and chemical industries of benefits for a period of 10 years from the date of entry into force of the Agreement. It would thus have given an industry the possibility of obtaining patent protection for the remainder of a patent's term.

The following specific transitional arrangements are made in the Agreement: to the extent that a developing country does not extend protection to pharmaceutical and agricultural chemical products, it is required to receive applications for patents for such inventions as from the date of entry into force of the WTO

Agreement. However, these patent applications will not have to be examined until after the expiration of the 10-year transitional period, as indicated above. During the total period between the filing of the application and the granting of the patent, the novelty of the application will be preserved as if the application had been examined on the date of filing of the application in that country (i.e. in accordance with the normal provisions of patent law for testing novelty) and not when the examination actually took place (i.e. at the end of the transitional period). The patent so granted will last for the remainder of the patent term, calculated from the date of the filing of the application.

In addition, the same country is required to grant "exclusive marketing rights" for the above-mentioned products if marketing approval is obtained before the patent is granted but, at a minimum, for a period of five years.<sup>290</sup> The granting of the "exclusive marketing rights" is subject to the following conditions: a patent application has been filed; a patent has been granted, and marketing approval for that product has been obtained in another country (after the entry into force of the WTO Agreement). It is also required that the product in question should obtain marketing approval in the country where the patent application is filed. Nevertheless, it should be noted that the concept of "exclusive marketing rights" may mean that the patent applicant is, during a period of five years, the only one that can be given marketing approval; however, its exact meaning is not entirely clear and should be examined in terms of its possible implications for fair competition in a given market.<sup>291</sup>

## D. Implications of the Agreement for developing countries

The above analysis highlighted the profound changes introduced by the Agreement in the traditional standards of intellectual property rights. Such changes will influence competition in the world economy, as well as the

generation and diffusion of technological innovations, and, ultimately, the technological development prospects of developing countries. The impact of the changes can thus be far-reaching, though at this early stage it is difficult

<sup>288</sup> See Article 64:2 of the Agreement.

<sup>289</sup> See Stewart, *op. cit.*, pp. 41-44 and 54-55.

<sup>290</sup> See Article 70:9 of the Agreement.

<sup>291</sup> The overall economic impact of the above arrangements would depend on different factors: for example, the time necessary to obtain marketing approval before the granting of exclusive marketing rights and the possible abuse of the dominant position created by the granting of such rights which have no relation to rights derived from intellectual property rights.

to assess the full implications of the Agreement. An attempt is made in this section to consider in a preliminary manner some possible implications of the new regime.

## 1. General considerations

Any assessment of the implications for developing countries of the new international standards and principles must be made in conjunction with the evolving perception of the interrelationship between trade, intellectual property protection, transfer of technology and investment. Until recently, intellectual property was viewed as a subject reserved for a few specialists in a narrow domain.<sup>292</sup> It is now considered to be one of the most important variables bearing on competitive capacity and transfer of technology in general. It has attracted attention as countries have become increasingly interdependent through the globalization of international production. However, viewing intellectual property protection exclusively from the angle of trade is tantamount to ignoring its paramount role in technological innovation and in access to technology.<sup>293</sup> Indeed, the aim of protection is to maintain an appropriate balance between the encouragement of inventive activity and the diffusion of inventions which forms the underlying rationale of the whole system. While the nature and scope of the proper balance depends on the level of technological development in each country, it is increasingly recognized that the creation of technological knowledge, whether in the form of new ideas, products or processes, will provide benefits for society by allowing the economy to grow, develop and perform competitively.<sup>294</sup> The recent literature tends to support the assumption that, without any appropriate legal protection, there will be no incentive to invest in inventive activity.<sup>295</sup>

In analysing the costs and benefits of a harmonized legal protection system in developing countries, it would be important to bear in mind a number of factors affecting the development of intellectual property protection. First, the changing nature of domestic innovations in developing countries, including a number of these countries that are increasingly involved in intensive R&D activities.<sup>296</sup> Second, the growing share of technology in international trade and its strategic importance in competitiveness. Third, the increasing costs of R&D combined with the shorter commercial life-cycles of products and processes, and the concomitant necessity for the widest possible commercialization for the rapid recovery of such costs. Finally, the increasing incidence of counterfeiting due to the relative ease of copying as a spin-off from new technologies. As a result of these factors, the transfer of technological knowledge to developing countries is becoming increasingly dependent on the legal protection these countries can provide.<sup>297</sup> In such cases the granting of legal protection could produce some social benefits by way of improving technological capabilities in developing countries.

In this sense, the economic value of a protection system appears to be positive in that the social benefits of a legal protection regime would be higher than without protection. However, although legal protection may be a prerequisite for innovative activities and transfer of technology, it is far from being a sufficient condition, given the importance of a host of other factors affecting investment and the transfer and diffusion of technology in developing countries.<sup>298</sup>

Thus, the net benefit that would accrue to developing countries from stronger protection would be the possible benefit obtainable from the transfer and diffusion of technology. However, the benefits that a developing country receives from legal protection tend to increase as the country develops; most of these

<sup>292</sup> See "Intellectual property rights ..." (ST/CTC/SER.A/24), p. 1.

<sup>293</sup> Yusuf, *op. cit.*, p. 86.

<sup>294</sup> See also C.A. Primo Braga, "The economics of intellectual property rights and the GATT: A view from the south", *Vanderbilt Journal of Transnational Law*, Vol. 22, No. 2 (1989), pp. 251-252.

<sup>295</sup> Siebeck (ed.), *Strengthening Protection of Intellectual Property in Developing Countries: A Survey of Literature*, World Bank Discussion Papers, No. 112 (Washington, D.C.: The World Bank, 1990), pp. 17 and 69; see also R. Rozek and Rapp, "Benefits and costs of intellectual property protection in developing countries", *Journal of World Trade*, 24 October 1990, pp. 75-102; M. Rafiqzaman, "The optimal patent term under uncertainty", *International Journal of Industrial Organization*, 5 June 1987, pp. 233-246; and A.V. Deardoff, "Should patent protection be extended to all developing countries?", *World Economy*, 13:4 (December 1990), pp. 501-503.

<sup>296</sup> See C.A. Primo Braga, "The newly industrializing economies" in M.B. Wallerstein (ed.), *Global Dimensions of Intellectual Property Rights in Science and Technology* (Washington, D.C.: National Academy Press, 1993), p. 170.

<sup>297</sup> See E. Mansfield, *Intellectual Property Protection, Foreign Direct Investment and Technology Transfer*, International Finance Corporation, Discussion Paper No. 79 (Washington, D.C.: The World Bank, 1994), p. 20.

<sup>298</sup> U. Kumar, "Benefits of the industrial property system and the African developing countries", *World Competition Law and Economics Review*, Vol. 16, No. 3 (March 1993), pp. 71-90.

countries are likely to incur a net loss in the first stages of the reform of IPR regimes.<sup>299</sup>

## 2. Effects on transfer of technology

Adherence by all countries, notwithstanding their level of technological development, to a set of standards for stronger legal protection, would have important implications for the transfer and diffusion of technology in technology-importing countries.

It is possible that stronger protection may be used by foreign intellectual property holders, especially in developing countries, to preserve import rights rather than to work the technology locally or to licence it to other firms. This is borne out by the fact that only a minimal fraction of innovations protected in developing countries are actually exploited there. Even where suppliers are interested in transferring their protected technology, stronger protection would further enhance their bargaining power and allow them to charge higher prices.<sup>300</sup>

This affects all countries in the world.<sup>301</sup> But it affects developing countries more because they are to a far greater extent users rather than generators of technological innovations compared with industrialized countries.<sup>302</sup> Since one of the most important mechanisms for the diffusion of innovations to developing countries is the transfer of technology, this is tantamount to saying that the price ticket on imported technologies will have an overall tendency to be higher than before and that this will burden developing more than developed countries because they are technologically less developed and few, if any, of their own firms will be receiving the increased licensing and other technology-related payments. Increases in such payments are brought about

chiefly by reducing the potential number of imitators and therefore the potential number of competing suppliers of protected technologies.

On the other hand, given the importance attached by firms to protection of intellectual property in potential recipient countries, stronger protection could lead to greater willingness to transfer technology, particularly new technologies. There is growing evidence that the existence of a "protection gap" among countries may be leading to delays in technology transfer, with potential technology suppliers seeking adequate protection in the technology-importing country before proceeding with the relevant investment and technology transfer. For technology suppliers, inadequate or ineffective protection is increasingly conceived as unwillingness to play by the rules of the game.

A survey conducted by Professor Mansfield in the United States has shown that the presence of an intellectual property protection system does have some effect on decisions of transnational corporations to invest in a given country.<sup>303</sup> In this respect, a number of factors have been considered to be a sign of inadequacy of intellectual property protection, *inter alia*, the limited scope of protection and inadequate enforcement measures. Moreover, it has been pointed out that intellectual property plays a different role in each type of industry. For example, its role is considered to be significant in the pharmaceutical and chemical industries. It would be correct therefore to assume that an important expected consequence of the stronger protection provided by the Agreement could be a greater incentive for enterprises to invest in developing countries and to licence patented pharmaceutical and chemical inventions to entrepreneurs in these countries.

In so far as harmonized intellectual property standards might also be sufficient to

<sup>299</sup> Primo Braga, "The newly industrializing economies...", *op. cit.*, p. 172.

<sup>300</sup> See E.F. Emmert, "Intellectual property in the Uruguay Round: Negotiating strategies of the Western industrialized countries", *Michigan Journal of International Law*, Vol. 11, No. 4 (Summer 1990), pp. 1359-1362; Primo Braga, "The newly-industrializing economies...", *op. cit.*, p. 256, and K. Maskus, "Intellectual property" in J. Schott (ed.), *Completing the Uruguay Round: A Result-oriented Approach to the GATT Trade Negotiations* (Washington, D.C.: Institute for International Economics, 1990), p. 168; see also Indian Drug Manufacturers Association, "Dunkel draft: A national health disaster", Bombay; R. Dasgupta, "Subsidies, patents and market access in the Dunkel draft", *Economic and Political Weekly*, Vol. XXVII, No. 18 (May 1993), p. 855; and *Financial Times*, 30 March 1994.

<sup>301</sup> See also *Foreign Protection of Intellectual Property Rights and the Effects on the US Industry and Trade*, USITC Publication 2065, Investigation No. 332-245 (February 1988).

<sup>302</sup> See also Primo Braga, *ibid.*, p. 256.

<sup>303</sup> Mansfield, *op. cit.*, p. 5. As P. David also points out "...the would-be borrowers of technology have an interest in a regime of stronger protection for intellectual property, either through statutory measures, or judicial enforcement of trade secrecy rights", *Knowledge, Property and the System Dynamics of Technological Change*, World Bank Annual Conference on Development Economics, 30 April and 1 May 1992, Washington, D.C., p. 36; see also *Financial Times*, 17 March 1994.

promote the generation of new innovations, all countries - including developing countries - benefit from the new products and processes and the expansion in productivity resulting from these innovations.<sup>304</sup> Even those developing countries which may not be far enough advanced technologically to use the technologies themselves will be in a position to benefit from the new products that are generated and from the indirect trade and income effects of the expansion of world output that are a potential result of the application of an increased flow of innovations. In addition, new protection standards may lead to increased disclosure of inventions; all countries could benefit from the new knowledge thus made available which could stimulate the production of further improvements and new inventions based on those that have been disclosed.

Of course, the implications of stronger protection would not be same for all countries. For instance, firms in newly industrialized countries would be affected in two ways. First, stronger protection makes it more difficult to "imitate" (through reverse engineering and other means) innovations developed by the technological leaders like Japan and the United States. This has a tendency to dampen technological innovation in these countries which means fewer suppliers of the relevant technologies, less competition, fewer alternatives and, therefore, higher cost of access to these countries. Secondly, and this has been recognized in countries and territories like the Republic of Korea and Taiwan province of China, the adoption of intellectual property protection by them protects potential innovators there from infringement by competitors in their own and other countries. It would thus act as a potential stimulus to invention and innovation which would be beneficial to these countries. The two above-mentioned effects on technology generation are offsetting. However, on balance, it can be argued that, over the medium and long-term, intellectual property protection as envisaged in the Agreement will have positive effects

on the generation of innovations in these countries. Inasmuch as strengthened protection increases the generation of new technologies in the countries which are already very advanced technologically, it would also tend to increase the number of technology suppliers, thereby stimulating competition and improving other developing countries' access to technology. In the short run, however, the costs weigh more heavily than they do in the long run.<sup>305</sup>

### 3. Access to new technologies in the areas of biotechnology and information technology

With respect to biotechnology,<sup>306</sup> micro-biological advances routinely affect changes in the higher plant and animal world, with the result that legal distinctions between inventions said to be macrobiological processes or micro-biological processes in nature have not always been implemented with consistent or persuasive results. Nor has a firm consensus emerged concerning the application of patent-law mechanisms in this field. For example, disagreements exist with regard to the patentability of so-called "products of nature", as referred to in section C, the appropriate criteria for determining novelty and non-obviousness, the deposit and enablement requirements, and the proper scope for protection. The relevant provisions (Article 27:3(b)) must be reviewed four years after the entry into force of the Agreement and any realistic appraisal of long-term prospects must necessarily take into account the interests of developing countries. Meanwhile, studies suggest that some developing countries are fairly well-positioned to promote biotechnological innovation owing to such factors as climate and geography, which endow them with genetically diverse raw materials on which the developed countries increasingly depend.<sup>307</sup>

<sup>304</sup> As stated by Subramanian, *op. cit.*, p. 952: "IP regimes ... might be sufficient to influence the scale of technological creation in the industrialized world ... for example in development of drugs for treatment of tropical diseases or of technologies, such as seeds or chemicals, designed for tropical agriculture".

<sup>305</sup> See Sang-Gon Kim, Kong-Kyun Ro and Pyung-II Yu, "Intellectual property protection policy and technological capability", *Science and Public Policy, Journal of the International Science Policy Foundation*, Vol. 21, No. 2 (April 1994), pp. 121-130.

<sup>306</sup> See Reichman, "Implications of the draft TRIPs Agreement ..." *op. cit.*, p. 8. See also J. Van Wijk and G. Junne, "Intellectual property of advanced technology, changes in the global technology system: Implications and options for developing countries", Maastricht, UNU, INTECH Working Paper No. 10 (October 1993), pp. 13-31; and C. Correa, "The pharmaceutical industry and biotechnology: Opportunities and constraints for developing countries", *World Competition*, 16 December 1991, pp. 43-63.

<sup>307</sup> See SUNS, 18 April 1994 (The first meeting of the Intergovernmental Working Group on Global Forests, Kuala Lumpur, called for a joint strategy to prevent the exploitation of genetic resources by countries with advanced technologies: "there can no longer be unconditional and unlimited free access to these resources which represent the genes of flora and fauna available". It was stated that advanced countries were "highly protective of access to biotechnology"); see also Reichman, "Implications of the draft TRIPs Agreement ...", *op. cit.*, p. 9.

On the other hand, developed countries continue to enjoy advances in biotechnology which may become available to developing countries as a consequence of the Agreement. A number of developing countries may find their competitive status enhanced by the provision of proprietary rights in this field, including plant breeders' rights. Besides acquiring ownership rights, developing countries interested in promoting biotechnological pursuits need to conserve their natural genetic endowment for future exploitation. It would be useful to consider regulating the manner in which a firm obtains supplies of local germ plasm, with a view to sharing the proceeds of commercial exploitation. In the short run, it should be noted that much biotechnological innovation, especially processes for making end-products, will fail to meet the non-obviousness standards of domestic patent laws in industrialized countries. Such innovations could obtain protection only under a trade-secret law. Possibilities for reverse engineering are then enhanced by the self-reproductive properties characteristic of both natural and genetically refined organisms.

In the area of computer development and information technology, such rapid advances are being made that developing countries not in the market may find it increasingly difficult to catch up. Even those already in the market are handicapped by a lack of infrastructure and a shortage of high-level design skills. Mention should be made here of the growing trend towards computer-programme-related patents in some developed countries. Until recently, the software industry even in developed countries has been characterized by incremental innovation, technical dynamism and rapid product evolution, and those factors encourage entrepreneurs in developing countries to acquire market shares by adapting and improving techniques to local conditions. On the other hand, patent granting in this area could impede both the independent redevelopment of functional equivalents and reverse engineering, while enhancing the market power of large firms which, through cross-licensing agreements, might erect barriers to entry that smaller firms would find it difficult to overcome. It is generally recognized that domestic enforcement of foreign programme-related patents could restrict competition in the world market,<sup>308</sup> thereby adversely affecting computer users.

#### 4. Restrictive practices

One of the concerns of developing countries during the Uruguay Round negotiations was that the strengthening of intellectual property protection under the Agreement would open up opportunities for monopolistic abuses by suppliers of technology. In particular, they feared that suppliers would be in a stronger position to impose restrictive conditions on the licensing of technology which would distort international trade. However, the Agreement, in its final form, provides more ample safeguards against such abuses than might have been predicted at the outset of the Uruguay Round. For example, the basic principles of the Agreement suggest that regulatory action on the protection and enforcement of intellectual property rights should "contribute to the promotion of technological innovation and to the transfer and dissemination of technology, to the mutual advantages of producers and users ... in a manner conducive to social and economic welfare, and to a balance of rights and obligations" (Article 7). Similarly, the Agreement recognizes the need "to promote the public interest in sectors of vital importance to ... socio-economic and technological development" (Article 8). It allows, as examined in section C above, appropriate measures provided that they are consistent with the provisions of the Agreement to prevent "the abuse of intellectual property rights". Taken together, it seems that these provisions preserve and expand exceptions that Article 5A of the Paris Convention has long recognized, and explicitly entitle technology-importing countries to take measures to prevent recourse to practices that "adversely affect the international transfer of technology".

Even forfeiture or revocation of a patent becomes technically feasible under the Agreement, subject to an opportunity for judicial review. Therefore, the standard form of remedial action remains compulsory licensing, as it was under Article 5A of the Paris Convention, subject to important limitations introduced by Article 31 (Other Use Without Authorization of the Right Holder) of the Agreement. In principle, both the public interest exception and measures to prevent abuse, stipulated in Article 8 of the Agreement, would justify resorting to compulsory licensing. As underlined by Professor Reichman, the meaning of "abuse" has been the source of considerable controversy, while a few developed countries, notably the

<sup>308</sup> *Ibid.*, p. 12; see also J.H. Reichman, "Goldstein on Copyright Law: A realist's approach to a technological age", *Stanford Law Review*, 43, 991, pp. 970-976; and C. Correa, "Intellectual property in the field of integrated circuits: Implications for developing countries", *World Competition*, 15 December 1990, pp. 83-101.

United States, limit the concept to anti-competitive practices bordering on antitrust violations. Most countries consider the doctrine of abuse applicable if a patentee fails to work the patent locally in due course or "refuses to grant licences on reasonable terms and thereby hampers industrial development, or does not supply the national market with sufficient quantities of the patented product, or demands excessive prices for such products".<sup>309</sup> The Agreement merges this broad concept of abuse with the public interest exception for purposes of compulsory licensing under Article 8.<sup>310</sup> It should be emphasized that all compulsory licences are subject to the conditions of Article 31, as explained in section C above, which normally requires adequate remuneration, taking into account the economic value of the licence, and imposes reasonable restrictions on the export of the resulting products.

Moreover, the Agreement allows countries to address directly the primary concern of monopolistic pricing. To this end, Article 31(b) implicitly allows countries to impose compulsory licences when, despite negotiations with the right holders, the latter have failed to licence the patented technology "on reasonable commercial terms and conditions". Similarly, there is no established international norm governing the principle of exhaustion (Article 6), which implies that after the first distribution of a product (for which a patent, trademark or copyright protection is available), a title-holder will no longer be entitled to make use of his/her exclusive rights to prevent further distribution of the protected product in the domestic market. National legislation may, therefore, continue to allow parallel imports which lower prices<sup>311</sup> and encourage foreign patentees to establish themselves locally in order to monitor the market and adjust business strategies to changing conditions.

## 5. Administrative arrangements

In terms of the transitional arrangements (examined earlier in section C above), many countries would need to embark on the adoption or adaptation of new legislative in-

struments. As may also be noted, the Agreement provides only a broad direction to countries for the elaboration of national legislation in the many complex areas of intellectual property rights. Embarking upon such an exercise would be a costly undertaking, particularly for developing countries, necessitating the adequate allocation of specific resources for the adaptation of their legislation and institutional arrangements. In addition, in many countries, there is a lack of appropriate machinery for proper registration and management of intellectual property rights owing to the high cost and lack of expertise. Many of these countries will be confronted with the choice of establishing an "examination system" or a "registration system". The former is a system whereby the examination, for instance, of novelty for all patents, use of trademarks and related applications will be carried out. This requires an adequate infrastructure and highly skilled manpower. The "registration system" consists of establishing a procedural system for filing applications and for granting protection without examination of novelty. This latter system also entails a certain amount of cost, particularly in terms of eventual court litigations resulting from a larger number of titles not always valid. In today's increased commercial exchange between countries, copyright protection and trademark registration would require the eventual setting up of computerized information networks to facilitate the task of the enforcement authorities. It should also be noted that the same authorities may benefit from the income generated by application fees which, in some cases, after the start-up costs, may even lead to substantial revenues.

## 6. Measures to fight counterfeiting

In conjunction with the administrative arrangements, the customs authorities are directly involved in the enforcement of the Agreement. In many technology-importing countries, the emphasis of the customs inspection of imported goods is on product name, brand name, quality, specification, product serial number, model number, countries of manufacture, quantity, and net weight. Trademark

<sup>309</sup> See Reichman, "Implications of the draft TRIPs Agreement ...", *op. cit.*, p. 15 and Note 101.

<sup>310</sup> *Ibid.* See also P. Tandon, "Optimal patents with compulsory licensing", *Journal of Political Economy*, Vol. 90, No. 3 (1982), pp. 484-485.

<sup>311</sup> See also A. Christie, "Australia's proposals for computer software protection", *EIPR: European Intellectual Property Review*, Vol. 16, No. 2 (1994), p. 77. (In its Final Report on its inquiry into the price of computers, the Price Surveillance Authority recommended that the Copyright Act be amended to allow parallel importation of computer programs and their manuals); see also A. Yusuf and A. Moncayo Von Hase, "Intellectual property protection and international trade exhaustion of rights revisited", *World Competition*, 16 (1992), p. 130.

infringement does not generally fall within the scope of inspection. If trademark holders possess evidence of infringement or have obtained the necessary information, they may normally file a petition with the court for provisional attachment of the counterfeit goods, inform the prosecutor, or petition the trademark authorities. The customs will then be in a position to take action to seize such goods when so advised by the court or the intellectual property authority. In order for customs authorities to take measures on their own, a specific monitoring scheme would be needed for both imported and exported goods.

Normally, a court judgement or order would form the legal basis for customs action to seize products suspected of patent infringement. The property right holders may petition for the seizure of imports suspected of copyright infringement upon the posting of an appropriate bond, and customs would confiscate the imports when the court has finally confirmed the existence of infringement. However, the implementation of the Agreement requires that customs be given the authority to take action against counterfeit elements or parts that are imported for the purpose of assembling or producing a finished product to be exported to a third market. In order to cope with this kind of problem, many agencies may be involved. Questions of coordination and the necessary legal framework will arise, which would need to be further examined in developing countries that are complying with the obligations envisaged in the Agreement. However, experience shows that the problems faced at present by many developing countries tend to be on the enforcement side rather than with the legislation itself.

## 7. *The special case of LDCs*

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The strengthening of intellectual property protection would obviously require the allocation of a larger amount of resources in order to achieve the goal set out in the Agreement. The special needs and requirements of the least developed countries have been taken into account in the transitional period accorded to them in respect of the application of the Agreement. It explicitly recognizes the need for flexibility in order to create a viable technological base and calls on developed countries to "provide incentives to enterprises and institutions in their territories for the purpose of promoting and encouraging technology transfer" in order to enable the LDCs "to create a

sound and viable technological base" (Article 66:2).

In implementing the new intellectual property regimes, the LDCs would immediately be confronted with financial and administrative constraints. In terms of a time-frame, the LDCs would probably need to embark on two stages of adaptation, namely immediate tasks after the general entry into force of the Agreement, and tasks to be carried out during the 11-year transitional period. The immediate task would be to comply with the provisions on national treatment and those on most-favoured-nation treatment. Both need to be incorporated into the LDCs' national legislation. During the transitional period, the tasks would consist of the following: changes in national legislation in accordance with the standards laid down in the Agreement; elaboration of judicial procedures for enforcing laws and of an administrative framework including customs. The latter would not only deal with the upgrading of existing arrangements, but also with establishing additional administrative arrangements for areas not currently covered by the administrative machinery.

Given the type, nature and scope of the legal and institutional changes called for by the provisions of the Agreement, the tasks involved in such adaptation will indeed entail considerable costs for LDCs (see box 22).

## 8. *Concluding remarks*

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At this moment, a large number of developing countries are undergoing a process of wide-ranging economic reforms at significant cost. Among these, the changes being made in matters bearing on intellectual property would undoubtedly require complementary international support in the form of improved financial flows, investment and technology transfer. The process of economic reforms and the implementation of the Uruguay Round Agreements would provide increased opportunities for all countries through the expansion of world trade. It is in the common interest that this process should advance and be given the necessary support to ensure its success.

Developing countries in general and LDCs in particular are suffering from serious supply-side constraints as the result of inadequate investment trends, insufficient development of human resources and lack of adequate technological capacity. The cooperation of industrialized countries in financing the reforms

## Box 22

### COST OF ADAPTING NATIONAL INTELLECTUAL PROPERTY LAWS AND INSTITUTIONAL ARRANGEMENTS TO TRIPS PROVISIONS: THE CASE OF BANGLADESH<sup>1</sup>

For Bangladesh, bringing national laws and institutional set-ups and procedures in line with the provisions of the TRIPS Agreement poses a serious challenge. The existing legal and institutional arrangements in the country relating to IPRs are characterized by major gaps and inadequacies. Such a task will not be easy, and will involve substantial expenditure.

In Bangladesh, IPRs are protected through a number of legal instruments, namely, the Patent and Design Act of 1911, the Patent and Design Rule of 1933, the Trademark Act of 1940 and the Trademark Rules of 1963. Much of these instruments are outmoded. Their administration is scattered over three Ministries. Patent laws are administered by the Patent Office, which is a unit within the Ministry of Industry; trademarks are handled by a registry in the Ministry of Commerce; and copyright registration is carried out by the Copyright Office in the Ministry of Culture. In terms of size, visibility and institutional autonomy, all these units are on the periphery of the country's administrative framework. For example, the Patent Office - the largest of all three - has only three professional officers and five junior level technical officials, supported by a number of subordinate staff. The leadership of the Patent Office is at a relatively low level of the governmental hierarchy. Its work is seriously handicapped by the lack of the requisite equipment and training facilities. There is no systematic arrangement for enforcing the existing IPR laws and in particular for the prevention of infringements, including the relevant border control machinery.

Like other least developed countries, Bangladesh is required to implement the new intellectual property regime in the wake of the TRIPS Agreement in two phases. In the immediate future, the task would be to comply with the main international conventions and the provisions relating to national treatment and MFN treatment. During the 10-year transitional period, the country would need to incorporate the relevant provisions of the Agreement in its body of laws and regulations, substantially improve and enlarge the judicial, administrative and enforcement framework, including setting up the necessary customs and border control machinery, and mobilize and develop the requisite human resources.

The tasks of complying with the TRIPS provisions will undoubtedly involve considerable expenditure, much of it of a recurrent nature. To obtain a preliminary idea of the cost entailed, the estimated costs of a selected number of specific activities are listed as follows: (i) the establishment of an expert body with five experts and five supporting staff for identifying and drafting specific amendments in existing laws and specifying administrative and legal procedures for enforcement would require an estimated amount of \$150,000 at the current exchange; (ii) strengthening the judiciary framework (four trained judges, four arbitrators and 10 supporting staff) would imply an increase in the budget of the judiciary system of approximately \$200,000 per year; (iii) upgrading the IPR-related bodies for administering and monitoring the post-TRIPS national IPR regime (a three-fold increase in professional and other staff will be called for by the end of the transitional period) would necessitate an annual expenditure of \$500,000, while strengthening procedures and upgrading equipment would cost an additional \$200,000; (iv) setting up specialized enforcement units to report and investigate alleged infringements of IPRs would require at least \$200,000 per year; and (v) strengthening custom authorities for meeting special requirements for border measures would cost over \$50,000 per year. In addition, substantial resources will be required for training administrators, and enforcement and custom officials, including training in more advanced countries. The overall cost could rise as the country advances along the path of industrial and service sector development. In view of its persistent fiscal difficulties and lack of IPR-related technical expertise, Bangladesh would have to depend on external support in implementing the TRIPS provisions.

<sup>1</sup> Based on a study (forthcoming) prepared for UNCTAD by Nurun N. Rahman, "The cost of strengthening national capacity for the implementation of the TRIPS provisions of the Uruguay Round Final Act: Some preliminary estimates for Bangladesh".

is thus needed in order to assist developing countries, particularly LDCs, in overcoming obstacles which might hamper the implementation of the Agreement. Additionally, the prep-

aration and implementation of reforms could advance the integration of all countries into a new multilateral trading system. In this context, resorting to unilateral action in the area



of intellectual property rights would be in contradiction with the call for an integrated multi-lateral process in this area.<sup>312</sup> Moreover, such actions run the risk of creating arbitrary standards in international property that could well prove insufficient and trade-distorting over time.

In the post-Uruguay Round period, intellectual property rights protection is deemed to constitute an important component of an environment conducive to international transfer of technology, including FDI.<sup>313</sup> In this context, the integration of intellectual property into a new international economic environment will require marketing strategies that are consistent with the new legal order to be formulated. In the short and medium term, it seems clear that within this new environment much influenced by the Agreement developing countries in general would have to work harder to compete and to acquire technological improvements. However, if the appropriate strategies are adopted in both the public and private sectors, it is evident that any competitive effort that secures entry to the world market, and any effective transfer of technology achieved in the process, would probably yield greater potential returns than at present. To maximize these opportunities, developing countries must foster and reward entrepreneurship and evolve a regulatory environment conducive to technological innovation. In this regard, ingenuity in the use of all appropriate legal instruments should be the rule of the game. Developing countries, with appropriate cooperation from the international community, should resort to all available

instruments to enhance their technological development in the new scenario of the 1990s.

In this respect, the role of utility models as a protection mechanism for incremental innovation, which is not explicitly covered by the Agreement, should be explored, and the experience of countries such as Japan and Germany which have used this type of mechanism needs to be further examined. The adequate use of trade secrets legislation in developing countries also needs to be fully explored. Efforts to implement higher intellectual property standards will put increasing strains on competition law, which is only covered to a limited extent by the Agreement. Identifying the parameters of healthy competition that are valid for all players in an integrated world market will become an important task for the international community in the new economic environment. There is, in this respect, a great need for multi-lateral coordination and cooperation to ensure that all voices are heard in a collective endeavour to achieve a market-wide balance between incentives to generate technological innovation, and reasonable opportunities to imitate and improve on it.

In brief, the outcome of TRIPs has settled a number of long-standing issues in the domain of intellectual property. It opens a new phase in the evolution of intellectual property regimes which will require a continuous search for practical solutions to the implementation of the Agreement. The aim of creating a sound and viable technological base particularly in the least developed countries should guide these endeavours. ■

<sup>312</sup> See *Financial Times*, 28 April 1994.

<sup>313</sup> "Report of the Ad Hoc Working Group on Interrelationship between Investment and Technology Transfer" (TD/B/40(2), TD/B/WG.5/11), Geneva, 1994, para. 27.

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## DISPUTE SETTLEMENT

### A. General features of the Dispute Settlement Understanding

The Dispute Settlement Understanding (Understanding on Rules and Procedures Governing the Settlement of Disputes) was negotiated to give confidence to all participants that they would have the means to assure the proper fulfilment by other WTO members of the obligations set out in the Uruguay Round Agreements. The DSU is contained in Annex 2 to the Agreement Establishing the World Trade Organization (WTO). A number of other Agreements include dispute settlement provisions for specific subject areas. These are also a part of the overall solution found for the dispute settlement mechanism to be put in place to underpin the expanded rights and obligations resulting from the successful conclusion of the Uruguay Round.

Article II of the WTO Agreement states that GATT 1994 as specified in Annex 1A is legally distinct from GATT 1947 and that the agreements and legal instruments included in Annexes 1, 2 and 3 are integral parts of the Agreement, binding on all members. In this way, the "single undertaking" concept has been formally incorporated into the WTO, including the Dispute Settlement Understanding. The General Interpretative Note to Annex 1A determines that in the event of a conflict between a provision of GATT 1994 and a provision of another agreement in Annex 1A, the provision of the other agreement shall take precedence to the extent of the conflict.

Article III of the WTO Agreement establishes that the WTO will administer the DSU. This concept is further developed in Article IV of the WTO Agreement, where it is foreseen that the General Council will convene

as appropriate to discharge the responsibilities of the Dispute Settlement Body (DSB), which may have its own Chairman and will establish such rules of procedure as it deems necessary for the fulfilment of those responsibilities.

In the area of decision-making (Article IX of the WTO Agreement) a special regime is foreseen for dispute settlement. Decisions by the General Council when convened as the Dispute Settlement Body are to be taken only in accordance with the provisions of Article 2:4 of the DSU, which call for consensus. In regard to amendments, Article X of the WTO Agreement establishes that any member may initiate a proposal to amend the DSU by submitting the proposal to the Ministerial Conference. The decision to approve amendments will be taken by consensus and the amendments will take effect for all members upon approval by the Ministerial Conference. In this manner, the acceptance of amendments is dependent on the possibility given to every member to oppose the consensus and thus prevent the proposed amendment coming into force.

Article XIII of the WTO Agreement deals with the non-application of the Multilateral Trade Agreements between particular members. The DSU will not apply between any member and any other member if either of the members, at the time either becomes a member, has recourse to this Article.

Dispute settlement rules and procedures in GATT have been evolving since the United Nations Conference on Trade and Employment at Havana in 1947-1948. In this context, Article XVI:1 of the WTO Agreement states that,

except as otherwise provided for under the WTO or the annexed Multilateral Trade Agreements, the WTO will be guided by the decisions, procedures and customary practices followed by the contracting parties to GATT 1947 and the bodies established in the framework of GATT 1947. The previous GATT texts which provide a direct background for the DSU are (a) the Decision on Procedures under Article XXII on Questions Affecting the Interests of a Number of Contracting Parties, approved on 10 November 1958 by the GATT contracting parties, which clarified the ways in which recourse to Article XXII could take place; (b) the Understanding regarding Notification, Consultation, Dispute Settlement and Surveillance, adopted on 28 November 1979, which formed part of the Tokyo Round Agreements. This Understanding codified the dispute settlement procedures that had evolved over time, and incorporated in its Annex an Agreed Description of the Customary Practice of the GATT in the field of dispute settlement. The Understanding was complemented by a Decision of 29 November 1982, which was intended to improve the procedures and enable more effective use to be made of the existing mechanism. A further Decision of 30 November 1984 dealt with the formation and work of panels.

During the Uruguay Round an expanded version of the 1979 Understanding was adopted at the Montreal Mid-Term Review Meeting in 1988. It is in effect at present according to the Decision of 12 April 1989 and will remain so until the entry into force of the WTO according to the Decision of 22 February 1994.

The Ministerial Decision on the Application and Review of the DSU that is attached to the Uruguay Round Final Act is intended to

ensure a smooth transition between the end of the Round and the entry into force of the WTO Agreement. During this period, the rules and procedures of GATT 1947 will remain in effect. The relevant Councils or Committees will remain in operation for the purpose of dealing with those disputes for which a request for consultation was made before the date of entry into force of the WTO. The Decision includes a determination that a full review of dispute settlement rules and procedures under the WTO, as set out in the DSU, is to be completed within four years after its entry into force; and that a decision will be taken at the first Ministerial Meeting after the completion of the review as to whether to continue, modify or terminate such dispute settlement rules and procedures. Any change in the DSU must be made by consensus.

At many stages in the course of the Uruguay Round negotiations participants referred to the "intentions" of the drafters of this or that text. However, no formal minutes of meetings were kept, and in the event the participants frequently had only their own versions of what had been discussed. Consequently, apart from the summary records of the TNC, GNG and GNS, the Round did not provide the kind of detailed records that were left by the Preparatory Committee for the Havana Conference and the Conference itself, which have been invaluable in determining the background of different GATT provisions in regard to the WTO Agreement and its numerous annexes. What are generally available are only the final proposals made in each body by participants and the agreed final texts. It is logical, therefore, for the texts to be interpreted literally, at face value, subject to internationally agreed rules of interpretation of treaties.

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## B. Basic provisions

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Article 1:1 of the DSU establishes the wide area of its application. The "covered Agreements" are set out in Appendix 1 and include the WTO Agreement itself, the Multilateral Agreements on Trade in Goods, the General Agreement on Trade in Services and the Agreement on Trade-Related Aspects of Intellectual Property Rights. The Plurilateral Agreements on Trade in Civil Aircraft and on Government Procurement are included, as well

as the International Dairy Agreement and the International Bovine Meat Agreement, subject to the adoption of the appropriate decision by the signatories of each of these Agreements. Finally, the provisions of the DSU itself are subject to the application of the dispute settlement mechanism. Thus, the DSU has extremely broad application throughout the entire WTO system. Appendix 2 of the DSU identifies the special or additional rules and

procedures on dispute settlement contained in the covered Agreements on Anti-Dumping; Technical Barriers to Trade; Subsidies and Countervailing Measures; Customs Valuation; the Application of Sanitary and Phytosanitary Measures; Textiles and Clothing; the General Agreement on Trade in Services and its annexes on Financial Services and Air Transport Services; and the Decision on Certain Dispute Settlement Procedures for GATS. Article 1:2 establishes that to the extent that there is a difference between DSU rules and procedures and the special or additional rules and procedures set out in Appendix 2, the latter shall prevail.

If there is a conflict between the special or additional rules and procedures of more than one covered Agreement (for example, Agriculture and Subsidies), and the parties to the dispute cannot agree on the rules and procedures to be applied, the Chairman of the Dispute Settlement Body (DSB) in consultation with the parties, will determine the rules and procedures to be followed, on the principle that special or additional rules and proceedings should be used when possible, and the rules and procedures set out in the DSU should be used to the extent necessary to avoid conflict.

The DSB is entrusted with the administration of the DSU, as well as with the consultation and dispute settlement provisions of the covered agreements, except as otherwise provided in such agreements. It has the authority to establish panels, adopt panel and Appellate Body reports, maintain surveillance of implementation of rulings and recommendations and authorize suspension of concessions and other obligations under the covered agreements. The DSB will inform the relevant WTO councils and committees of developments in disputes and will meet as often as necessary. Its decisions will be taken by consensus (Article 2:4), a consensus being understood to exist when no member present at the meeting of the DSB when the decision is taken formally objects to the proposed decision. While the WTO Agreement establishes general voting procedures, they are replaced in the case of the DSU by the rule of consensus, which has become a custom in dispute settlement cases in GATT. The decision to agree on the rule of consensus is therefore a logical extension of a pre-existing practice, although it precludes (which was not the case previously) recourse to a vote under Article XXV of GATT, which was neither

amended or deleted in the course of the Uruguay Round negotiations. The WTO Agreement also recognizes the evolution towards decision-making by consensus in Articles IX and X. Basically, the DSB is the supreme dispute settlement organ of the WTO and all actions stem from it and eventually come back to it for whatever decision may be appropriate.

Article 3:2 establishes the cardinal rule that recommendations and rulings of the DSB may not add to or diminish the rights and obligations provided in the covered agreements. Dispute settlement solutions may not nullify or impair benefits accruing to any member under any of the covered agreements or impede the attainment of any objective of those agreements (Article 3:5). This clause further defines and clarifies the overall framework within which the DSU operates.

Conceivably there could be different interpretations of the provisions of a covered agreement, leading to equally different applications of the respective obligations. Under Article 3:9, members may seek an authoritative interpretation of the provisions of a covered agreement through the decision-making process under the WTO Agreement or a covered agreement. In the first case, Article IX:2 of the WTO is applicable, and the decision, to be approved, needs a three-fourths majority of the members of the WTO; in the second case, the applicable provisions of the covered agreement would apply. A three-fourths majority of WTO members constitutes a high threshold; this answers to the desire to prevent circumvention of the amendment provisions of the WTO through the use of the interpretations clause.

The DSU will apply only to new requests made on or after the date of its entry into force. In any complaint brought by a developing country member against a developed country member, however, the complaining party may invoke as an alternative to the provisions contained in Articles 4, 5, 6 and 12 of the DSU, the corresponding provisions of the Decision of the Contracting Parties to GATT of 5 April 1966. This provision was included in the DSU at the request of the developing countries, and it is intended to provide them with the option described above (paragraphs 11 and 12 of Article 3). Although the 1966 Decision has rarely been invoked, it offers the prospect of an accelerated procedure which in some cases would be of benefit to the complaining party.<sup>314</sup>

<sup>314</sup> The Decision on Procedures under Article XXIII recognizes that the impairment of benefits accruing to a contracting party directly or indirectly from the General Agreement can cause severe damage to the trade and economic development of the developing contracting parties and affirms the resolve to facilitate the solution of such situations while taking fully into account the need for safeguarding both the present and potential trade of developing contracting parties affected by such measures. If consultations do not lead to a satisfactory settlement, the developing contracting

## 1. Consultations

The first operative stage in the dispute settlement process, based on Article XXII of GATT, is the holding of consultations between the parties concerned, at the initiative of the party which feels a measure is being applied that affects its rights. Short time periods are established for replying to a request for consultations and also for entering into consultations (10 and 30 days, respectively). If there is no reply, the member which requested the consultations may request the establishment of a panel (paragraphs 1-3 of Article 4).

Requests for consultation will be notified to the DSB and the relevant Councils and Committees. Such requests must be submitted in writing, giving the reasons therefor and including identification of the measures at issue and an indication of the legal basis for the complaint (Article 4:4). Members are urged to make every effort to reach a satisfactory settlement at the consultative stage, which is confidential and does not prejudice the rights of either member in regard to any further proceedings (paragraphs 5 and 6 of Article 4).

If, after 60 days, the dispute has not been settled (or earlier, provided both parties agree) the complaining party may request the establishment of a panel (Article 4:7). In cases of urgency, including those which concern perishable goods, the periods are shortened: consultations will be entered into within 10 days of the request and the panel may be requested 20 days thereafter. The parties concerned, the panels and the Appellate Body must make every effort to accelerate the proceedings in cases of urgency (paragraphs 8 and 9 of Article 4). Article 4:10 establishes that during consultations members should give special attention to the particular problems and interests of developing country members. This paragraph has been worded so as to signify that such attention

should be paid irrespective of whether the developing country is a complainant or the object of a complaint.

The question of third party interest is dealt with in Article 4:11. Members with a substantial trade interest may ask to join in the consultations and their request should be accepted provided that the party to which the complaint has been addressed agrees that the claim of substantial trade interest is well founded. If the reply is in the negative, then the applicant member will be free to request consultations under the appropriate provisions of Article XXII: 1 or XXIII: 1 of GATT 1994, or of Articles XXII: 1 or XXIII: 1 of the General Agreement on Trade in Services (GATS), or the corresponding provisions in other covered agreements (as listed in the footnote to Article 4:11). In other words, interested third parties may either join the original consultation or initiate their own consultation.

## 2. Good offices, conciliation and mediation

Procedures for good offices, conciliation and mediation are undertaken voluntarily if the parties to the dispute so agree. They are confidential and do not prejudice the rights of either party in any further proceedings under the DSU, and may be requested at any time by any party to a dispute. They can begin and terminate at any time and, once terminated, the complaining party may then request the establishment of a panel (paragraphs 1-3 of Article 5). Such procedures may continue while the panel process is under way, provided the parties to the dispute agree, and the Director-General of the WTO may, acting in an *ex-officio* capacity, offer good offices, conciliation or mediation with a view to assisting members to settle a dispute (paragraphs 5 and 6 of Article

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party complaining of the measures may refer the matter to the Director-General so that, acting in an *ex-officio* capacity, he may use his good offices with a view to facilitating a solution. The Director-General shall consult with the contracting parties concerned and with such other contracting parties or inter-governmental organizations as he considers appropriate with a view to promoting a mutually acceptable solution. If this solution is not reached, the Director-General shall at the request of one of the contracting parties concerned, bring the matter to the attention of the CONTRACTING PARTIES or the Council and submit a report on the issue involved. The Council will then appoint forthwith a panel to examine the matter and recommend an appropriate solution. The panel shall take due account, among other things, of the impact of the measures complained of, on the trade and economic development of affected contracting parties. The periods for the panel to submit its report (60 days) and for a contracting party to which a recommendation is directed, to report on the action taken by it (90 days) are shorter than would normally be the case. If there has not been full compliance with the recommendation of the CONTRACTING PARTIES or the Council, authorization may be promptly given to the affected contracting party to suspend in regard to the contracting party causing the damage, application of any concession or any other obligation under the General Agreement whose suspension is considered warranted. The CONTRACTING PARTIES shall also consider what additional measures should be taken to resolve the matter when their recommendation has not been properly applied by a developed contracting party. Finally, the Decision establishes a link between Article XXIII and the Decision itself on the one hand, and Article XXXV (Commitments) in Part IV of GATT, on the other (BISD, Fourteenth Supplement, 1966, pp. 18-20).

### STATUS OF CONCILIATION OF DISPUTES

As of 10 June 1994,<sup>1</sup> the status of the GATT dispute settlement mechanism, covering disputes brought both under the GATT 1947 and under the Tokyo Round agreements, was as follows:

- Twenty-three disputes were at the consultation/conciliation stage. Twenty-one of them involved the major trading countries (Canada, the European Union, Japan and the United States) as applicants or defendants. Developing countries and territories were involved in nine cases (in seven cases as applicants, and in three cases as defendants).
- Twenty-seven dispute cases were at the panel stage. Adoption of several panel reports had been pending for a period of more than two years. All of these cases involved the major trading countries either as applicants or defendants. Developing countries were parties to seven cases (in six cases, as applicants).
- Ten disputes were at the implementation stage (eight of them involving the major trading countries and four cases involving developing countries).

<sup>1</sup> GATT document C/188.

5) in the belief that the moderating and conciliatory intervention of a third party will often be instrumental in overcoming outstanding differences and reaching a mutually acceptable settlement (see box 23).

### 3. Rules and procedures relating to panels

Paragraphs 1 and 2 of Article 6 cover the establishment of panels, which are to be set up promptly unless the DSB decides by consensus not to do so. Any such negative consensus can obviously be prevented by the complaining party, so there is in effect an automatic procedure for the establishment of panels. This is a departure from past GATT practice, and represents a significant advance in dispute settlement. The written request for the establishment of a panel must include essential particulars of the case, somewhat along the lines of requests for consultations (Article 4:4). In practice, this communication would state whether consultations took place, identify the specific measures at issue and provide a clear summary of the legal basis of the complaint. If it is desired that the proposed panel should have other than standard terms of reference, an alternative text should be submitted.

The standard terms of reference for panels (Article 7:1) will be utilized unless the parties to the dispute agree otherwise within 20

days from the establishment of the panel. These terms of reference are broad in scope and provide leeway for the panel to consider all aspects of the matter at issue. Whenever other than the standard terms of reference are agreed upon, any member may raise any point relating thereto in the DSB. This allows interested third parties to satisfy themselves that the terms of reference have not been drafted in such a way as to impair their own interests or to divert the proceedings along lines alien to the proper functioning of the DSU.

Panelists may come from the official or private sectors, but they must be well-qualified and include persons who have had direct experience in the sphere of GATT or WTO, taught or published on international trade law or policy, or served as a senior trade policy official of a member State (Article 8:1). The GATT roster of individuals possessing the necessary qualifications is to be continued. Members may suggest the names of governmental and non-governmental individuals for inclusion on the indicative list, of which the roster will be a part, to be approved by the DSB.

Panels will normally consist of three members, unless the parties to the dispute agree, within 10 days from the establishment of the panel, to its enlargement to five members (Article 8:5). Article 8:10 provides that when a developing country enters into a dispute with a developed country, at the request of the former at least one panelist shall come from a developing country member.

It may often happen that more than one member requests the establishment of a panel relating to the same matter (Article 9:1). In such cases, the tendency is not to set up multiple panels but to establish a single panel to deal with the matter, taking into account the rights of all the members concerned. Article 9:2 stipulates that a single panel must organize its examination and present its findings to the DSB in such a way that the rights members would have enjoyed under separate panels are in no way impaired. If any party to the dispute so requests, the panel will submit separate reports on the dispute. In many disputes, third party interests are of considerable importance; Article 10:1 stipulates that the interests of the parties to a dispute and those of other members under a covered agreement at issue in the dispute shall be fully taken into account during the panel process. Any such third party may ask to be heard by the panel and to make written submissions to it. These will be given to the parties to the dispute and be reflected in the panel report (Article 10:2). In addition, third parties are to receive the submissions made by the parties to the dispute to the first panel meeting (Article 10:3). If any third party considers that a measure that is already the subject of a panel proceeding nullifies or impairs benefits accruing to it under any covered agreement, it may have recourse to normal dispute settlement procedures under the DSU. Whenever possible, such a dispute shall be referred to the original panel.

The function of panels as defined in Article 11:1 is to assist the DSB in discharging its responsibilities. Accordingly, a panel should: (i) make an objective assessment of the matter before it, including the facts of the case, and the applicability of and conformity with the relevant covered agreements; and (ii) make such other findings as will assist the DSB in formulating the recommendations or in giving the rulings provided for in the covered agreements.<sup>315</sup>

The Working Procedures for panels, which are set out in Appendix 3 to the DSU, are to be followed unless the panel decides otherwise after consulting the parties to the dispute (Article 12:1). They consist of two parts: rules on the conduct of the panel deliberations; and a standard timetable. The Working Procedures are intended to ensure prompt panel action, while the successive stages contained in a maximum 34-week period are in-

tended to prevent delaying tactics and guarantee complainants that the dispute settlement system will function effectively.

Paragraphs 2 and 3 of the Working Procedures ensure the confidentiality of the panel proceedings. The panel meets in closed session and interested parties are present only upon invitation. The deliberations and the documents submitted to the panel are confidential. However, a party to a dispute may disclose statements of its own position to the public, and will also, at the request of a member, provide a non-confidential summary of its written submission to the panel that could be disclosed to the public.

Before the panel's first substantive meeting with the parties, both parties to the dispute shall transmit to it written submissions in which they present the facts of the case and their arguments (paragraph 4 of the Working Procedures). At the first substantive meeting of the panel with the parties, the complainant will present its case and the defendant will then give its point of view (paragraph 5). Interested third parties are invited to present their views during a session of the first substantive meeting of the panel set aside for that purpose, and all such parties may be present during the whole of that session (paragraph 6). At the second substantive meeting of the panel, formal rebuttals are made (paragraph 7). The order is reversed, in that the party complained against has the right to take the floor first, followed by the complainant. Both parties are required to submit written rebuttals to the panel, prior to the meeting.

Transparency is further ensured by paragraphs 9 and 10 of the Working Procedures, which establish that the parties to the dispute, as well as third parties, shall supply the panel with a written version of their oral statements. Furthermore, the presentations, rebuttals and statements are to be made in the presence of both parties, and each party's written submissions, comments on the descriptive part of the report and responses to panel questions will be made available to the other party or parties.

In the standard timetable for a panel it is foreseen, except for unexpected developments, that panel members will meet among themselves as often as they deem necessary. The panel will then submit the descriptive part of its report to the parties, which will have two weeks in which to transmit their comments on it. The

<sup>315</sup> In GATT practice, panels have based themselves on the information provided by the parties to the dispute, and it may be presumed that the differing interests ensure that all pertinent particulars are laid before the panel. Therefore, panels have not normally carried out their own investigation of the facts pertaining to a dispute; the information has been supplied by the parties, often supplemented, if the panel so requested, as it advanced in its analysis. This practice has been departed from to some extent in the DSU, as will be seen later when Article 13 is discussed.



panel will consider their comments and take them into account whenever it considers it desirable. After another 2-4 weeks, the panel will submit its interim report to the parties, including the findings and conclusions. This is a crucial stage, since the panel's recommendations to the DSB are now set out in detail. Any one of the concerned parties then has one week in which to request a review of any part of the report. The panel has a two-week period for review, in the course of which it may meet again with the parties. It will normally meet with them if a review of the report has been requested. After another two weeks, the panel will submit the text of the final report to the parties, for circulation to members after a further three weeks.

The panel findings are to be submitted in written form (Article 12:7). The report shall set out: (a) the factual findings; (b) the applicability of relevant provisions; and (c) the basic rationale behind the findings and recommendations of the panel. Whenever the parties to a dispute agree on a settlement, at however late a stage in the panel process, the panel report will be confined to a brief description of the case and to reporting that a solution has been reached (Article 12:7).

One of the concerns which the DSU is intended to overcome is the prolongation of a panel's work for an unduly long time. The Working Procedures allow panels some flexibility in this respect, but Article 12:8 establishes as a general rule that panels are to conclude their work within six months, or three months in cases of urgency. Some leeway is granted in Article 12:9, but whenever panels are unable to comply with the normal time-limit they are required to inform the DSB in writing of the reasons for the delay and provide an estimate of when they expect to submit their report. In no case should such a period exceed nine months.

Articles 12:10 and 12:11 provide more favourable treatment for developing country members and may agree to an extension of the consultation period (established in paragraphs 7 and 8 of Article 4) when a measure taken by a developing country is at issue. The Chairman of the DSB will decide on the length of the extension, after consulting with the interested parties. In addition, panels will accord a developing country sufficient time to prepare and present its case when it is a defendant. Devel-

oping countries sometimes lack the rapid administrative and technical responses that are required to defend a dispute settlement case. However, the DSU will grant interested developing countries a certain margin of time in which to study the issues and prepare their submissions. Article 12:11 establishes that where one or more of the parties to a dispute is a developing country member, the panel report must indicate explicitly the form in which account has been taken of the relevant provisions on differential and more favourable treatment that form part of the covered agreements raised by the developing country member in the course of the proceedings. The interested developing country would be required to refer to these provisions in its favour in the course of the panel proceedings to ensure their full recognition.

The complaining party may ask the panel to suspend its work at any time for a period of up to 12 months (Article 12:12). The timeframes for the panel's activities will be correspondingly extended. However, should the work of the panel be suspended for more than 12 months, the authority for its establishment will lapse.

Article 13:1 establishes a panel's right to seek information and technical advice from any individual or body it deems appropriate. This is an important innovation, as in the past panels have based themselves upon the information supplied by the parties to the dispute, and should serve to strengthen the position of developing countries which may be handicapped by having less access to information than their developed country opponents. Such requests addressed to any individual or body within the jurisdiction of a member will be notified to that member. A panel's capacity to gather information is further reinforced by Article 13:2, which states that the panel may have recourse to any relevant source and may also consult experts to obtain their opinion on certain aspects of the matter. With respect to factual issues concerning a scientific or other technical matter, a panel may request an advisory report in writing from an expert review group. Rules for the appointment and functioning of these groups are set out in Appendix 4 to the DSU.<sup>316</sup> Deliberations are confidential, panel reports will be drafted without the presence of the parties to the dispute, and opinions expressed by individual panelists will be anonymous.

<sup>316</sup> In the future it may be necessary for panels to call on expert advice of various sorts more than in the past. One reason is the increasingly complex nature of the subject-matter that will be dealt with under the DSU. The WTO will encompass not only trade in goods (like GATT), but also intellectual property and services issues. Further, each one of the services areas is a world in itself, requiring its own expertise. The detailed contents of many of the Understandings and Agreements that form part of WTO will undoubtedly need specialized and expert knowledge of a variety of subjects.

Panel reports are normally detailed and often raise questions of principle and set precedents. Such reports will not be considered for adoption by the DSB until 20 days after they have been issued to the members (Article 16:1). Any member that has objections to a panel report must convey them in writing for circulation at least 10 days prior to the DSB meeting at which the report is to be considered (Article 16:2). Parties to a dispute may participate fully in the consideration of the panel report by the DSB, and their views will be fully recorded (Article 16:3).

The meeting of the DSB is therefore an opportunity for any party to restate its case, to question the panel's interpretation of the facts, or its findings and conclusions, and to attempt to influence public opinion.

The automatic nature of the panel report approval process is enshrined in Article 16:4. This feature is one of the most important improvements in the dispute settlement system, and is aimed at preventing the recurrence of situations in which a party has obstructed approval of the panel report and therefore also its implementation. Within 60 days after the circulation of a panel report to the members, the report will be adopted at a DSB meeting unless one of two things happens: either a party to the dispute formally notifies the DSB of its decision to appeal, or the DSB decides by consensus not to adopt the report.

#### **4. Appellate review**

Appellate Review is an innovation in the dispute settlement system in GATT. The basic reasons for its adoption include (a) the notion that appeal is a logical part of what is in essence a legal process, and (b) the recognition of the political benefits of a system that will allow governments to have recourse to a final stage to present their case and seek to secure satisfaction.

A standing Appellate Body will be established by the DSB to hear appeals from panel cases (Article 17:1). It will have seven members, but only three (serving in rotation) will serve on any one case. They will be appointed for a four-year term and may be reappointed once (Article 17:2). Thus, Appellate Body members will have a somewhat higher status than ordinary panel members, and there would seem to be some risk that the purpose of this Body could be to modify legally correct but politically unacceptable decisions or recommendations by panels.

An appeal may be made only by a party to a dispute; however, recognized third parties (Article 10:2) may make written submissions and be heard by the Appellate Body (Article 17:4). This entitlement for third parties is basically similar to their rights in regard to panel procedures, and allows them to present their own views directly to the Appellate Body.

The overall automatic nature of the DSU is covered in Article 17:5, which establishes, as a general rule, that the appeal procedure will not exceed 60 days from the date a party formally notifies its intent to appeal to the date the Appellate Body issues its decision. In cases of urgency (Article 4:9) the Appellate Body will determine the timetable accordingly. Just as panels may extend their activities beyond the normal duration, the Appellate Body may prolong its work up to a maximum of 90 days; but it must inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report. Article 17:6 defines the scope of the Appellate Body's activity: an appeal will be limited to the legal issues covered in the panel report and legal interpretations developed by the panel.

As regards panel and Appellate Body recommendations (Article 19:1) when either body concludes that a measure is inconsistent with a covered agreement, it will recommend that the member concerned bring the measure into conformity with that agreement. The panel or Appellate Body may also suggest ways in which the member concerned could implement the recommendations. In addition, the member may receive concrete suggestions as to how to implement the recommendations addressed to it.

Unless otherwise agreed to by the parties to the dispute, the period from the establishment of the panel by the DSB until it considers the panel or appellate report for adoption will not as a general rule exceed nine months when the report is not appealed or 12 months in the event of an appeal. This is subject to the additional time that a panel or the Appellate Body may request to conclude its work under Articles 12:9 or 17:5 of the DSU, which will be over and above the periods established by the general rule.

#### **5. Implementation of recommendations and rulings**

Article 21:1 states that prompt compliance with recommendations or rulings of the DSB is essential to ensure effective resolution of disputes. In a number of cases in GATT history, governments have unduly delayed the

remedial actions required of them by panel reports. Specific monitoring measures intended to avoid a repetition of such episodes have therefore been established.

Article 21:2 establishes that particular attention should be paid to matters affecting the interests of developing country members with respect to measures which have been subject to dispute settlement. The commitment exists to provide developing country members with the means both to press for the early removal of third-country measures that are harmful to their export trade, and to claim leeway in terms of their own import measures that have been found to be inconsistent with their obligations.

No later than 30 days from the adoption of the panel or Appellate Body report, the member concerned will normally notify the DSB of its intentions in respect of its implementation of the recommendations and rulings approved by the DSB (Article 21:3). However, as immediate compliance may be impracticable for the member in some cases (for example, if a measure is contained in a law, and the executive power has no option but to apply it), the member will be allowed a "reasonable period of time" in which to comply. This concept is set out in three variants in Article 21:3:

- the period of time proposed by the member concerned, provided it is approved by the DSB; or, in the absence of such approval,
- a period of time mutually agreed by the parties to the dispute within 45 days following the adoption of the recommendations and rulings; or, in the absence of such agreement,
- a period of time determined through binding arbitration within 90 days of the adoption of the recommendations and rulings.

As DSB decisions are taken by consensus, in the first option set out above the complainant could block approval of the time period proposed by the member concerned if it considers it is not adequate in the circumstances. The second option, which calls for mutual agreement by the parties to the dispute, and which would normally follow from a disagreement on the time period proposed in the first option, has to be exercised promptly, since it has to be completed within 45 days of the adoption by the DSB of the recommendations and rulings. Moreover, the period will be reduced by the number of days (a maximum of 30) used to call the meeting of the DSB in which the party concerned made its original proposal on implementation. Finally, if the

disagreement persists, the matter will be referred to arbitration (Article 21:3(c)). In this case, if the parties cannot agree on an arbitrator within 10 days after arbitration was resorted to, an arbitrator (either an individual or a group) will be appointed by the Director-General of the WTO within a further 10 days, after consulting the parties. The arbitrator will be guided by the criterion that a reasonable period of time in which to implement panel or Appellate Body recommendations should not exceed 15 months although particular circumstances may justify a longer or shorter period.

Article 21:5 deals with a particularly delicate issue of compliance; i.e. when there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings. It might happen that a member required to modify a measure by a recommendation or ruling would do so, but in so doing would put into effect a new version of the measure, or a new measure, that might not be consistent with its obligations under the respective covered agreement. These cases will be decided through recourse to the DSU and the original panel will be resorted to whenever possible. Normally such situations would arise over a foreseeable and fairly limited time-span, and the original panel members would therefore be available. When this is not the case, new appointments to the panel would need to be made. The panel will issue its decision within 90 days after referral of the matter to it, but may request the DSB in writing for an additional period of time, with an explanation of the reasons therefor.

The permanent monitoring of the implementation of adopted recommendations or rulings is another feature of the DSU, established in Article 21:6. This will be entrusted to the DSB. The issue of implementation of recommendations or rulings may be raised by any member at any time at the DSB, following their adoption. Unless the DSB decides otherwise, which would call for a negative consensus, the issue of implementation must be placed on the agenda of the DSB meeting after six months following the establishment of the "reasonable period of time" and remain on the agenda until the matter is resolved. At least 10 days prior to each such DSB meeting, the member concerned will provide the DSB with a status report of its progress in implementation. This requirement exerts permanent pressure on the member concerned and has the added advantage of giving every member the means to make such comments as it sees fit in the course of DSB meetings. In particular, the party concerned, and any interested third parties, thus have a regular opportunity to recall the matter to the attention of the DSB, and to encourage

the member concerned to complete its implementation process as early as possible.

Articles 21:7 and 21:8 incorporate the concept of differential and more favourable treatment for developing country members that have brought a dispute settlement case. In the course of its surveillance activities, the DSB is required to consider what further action it might take that would be appropriate to the circumstances. In this connection, the DSB will take into account not only the trade coverage of the measures complained of, but also their impact on the economies of developing country members concerned. The DSB's mandate is very broad (Article 21:7) and may therefore give rise to different kinds of requests by interested developing countries (acceleration of the implementation process, special consideration for particular products, application of import procedures and rules, etc.) (see box 24).

## **6. Compensation and suspension of concessions**

When a member involved in a dispute settlement case fails to bring the measure concerned into conformity with the respective covered agreement, compensation and the suspension of concessions or other obligations could be authorized. Article 22:1 establishes that these are temporary measures available in the event that recommendations and rulings are not implemented within a "reasonable period of time", and are not to be preferred to full implementation of a recommendation to bring a measure into conformity with the covered agreements. The stress is clearly laid on the fulfilment of obligations; this is the essential aim of the DSU, and only when a member fails to comply with a recommendation within the prescribed reasonable period of time does the prospect of compensation or suspension of concessions arise.

While compensation is voluntary (and must be consistent with the covered agreements), it may be requested by a party that has invoked the dispute settlement procedures no later than the expiry of the reasonable period of time, if the respective recommendation and ruling have not been complied with in that period. While there is no reference in Article 22:2 to the possibility that the member concerned could on its own initiative offer temporary compensation pending compliance, it is certainly not excluded by the text. There is no limitation on the area in which compensation could be offered. It would appear therefore that the member concerned could negotiate

compensation in sectors or agreements other than that in which there had been non-compliance.

If no satisfactory compensation has been agreed within 20 days after the expiry of the reasonable period of time, any party that has invoked the dispute settlement procedures may request the DSB for authorization to suspend the application to the member concerned of concessions or other obligations under the covered agreements. According to Article 22:2, the duration of compensation negotiations depends fundamentally on the initiative of the complaining party.

Highly detailed principles and procedures have been worked out in regard to the suspension of concessions or other obligations (Article 22:3). There are three successive stages in determining the suspension. The complaining party should first seek to apply it with respect to the same sector or sectors in which a violation or other nullification or impairment has been found. If the complainant feels that it is not practicable or effective to do so, it may seek to apply the suspension in other sectors under the same agreement. Thirdly, if this also is not practicable or effective, and the circumstances are serious enough, the suspension may be sought under another covered agreement. This procedure is open to all members. While it was widely felt in the course of the negotiations that large developed countries were most likely to benefit from the capacity to suspend across agreements, it should be kept in mind that smaller countries, including developing countries, can also act on these lines. Whenever the circumstances are serious enough, the possibility of suspending concessions or other obligations under another agreement may very well have a deterrent effect on the continued enforcement of the measure that originally gave rise to the dispute settlement case concerned. The concept of withdrawal of concessions across covered agreements (cross-retaliation) was strongly resisted by a number of countries, but it was finally incorporated into the DSU although with a number of checks and controls intended to prevent its improper use.

In applying the principles set out in Articles 22:3 (a), (b) and (c), the party that seeks to suspend concessions is required to take two factors into account. One is the trade in the sector or under the agreement in question, and the importance to it of such trade. The other refers to the broader economic elements related to nullification or impairment, and the economic consequences of suspending concessions or other obligations. These two factors, especially the latter, open up wide areas of discussion. While the first one is reasonably

**SPECIAL OR ADDITIONAL DISPUTE SETTLEMENT RULES AND PROCEDURES  
CONTAINED IN THE COVERED AGREEMENTS**

Appendix 2 to the DSU sets out these special provisions. While it would have been desirable to conclude the Uruguay Round with one single dispute settlement mechanism of universal application to all areas of the WTO, the great diversity of the subject-matter and the course of the negotiations in specific areas led to the establishment of special or additional provisions. In any case, the multilateralization of the Tokyo Round Agreements in the Uruguay Round has had the effect of substantially rationalizing their dispute settlement provisions. It should be recalled that to the extent that there is a difference between the rules and procedures of the DSU and the special or additional rules of procedure set forth in Appendix 2, the latter will prevail.

In the case of the Agreement on Textiles and Clothing, a dispute settlement role is given to the Textiles Monitoring Body (TMB). Indeed, in addition to the paragraphs shown in Appendix 2, there are others in this Agreement which also seem to touch on dispute settlement by the TMB. However, Article 8:10 of this Agreement leaves it open to members to have recourse to the DSU when a matter remains unresolved.

The Agreement on Technical Barriers to Trade (TBT) foresees in Annex 2 the setting up of Technical Expert Groups to assist in questions of a technical nature, requiring detailed consideration by experts. These provisions are fairly similar to those that apply to Expert Review Groups under the DSU. Article 14 of the Agreement on TBT covers the contents of Annex 2.

The Agreement on Implementation of Article VI of GATT 1994 (Anti-Dumping) incorporates a significant condition when the DSB establishes a panel. The panel, in its assessment of the facts of the matter, will determine whether the authorities' establishment of the facts was correct and their evaluation of those facts was unbiased and objective. If the establishment of the facts was correct and the evaluation was unbiased and objective, even though the panel might have reached a different conclusion, the evaluation will not be overturned. Further, the panel will interpret the relevant provisions of the Agreement in accordance with customary rules of interpretation of public international law. Where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation, the panel will find the authorities' measure to be in conformity with the Agreement if it rests upon one of those permissible interpretations. These provisions contrast with Article 11:1 of the DSU (Function of Panels) and they clearly give increased leeway to the authorities of the importing country on the imposition of an anti-dumping duty. This is one of the issues that was discussed up to the end of the Uruguay Round and that led to a difficult compromise among participants.

The special decision on review of Article 17:6 of the Anti-Dumping Agreement states that the standard of review in Article 17:6 of the Agreement shall be reviewed after a period of three years with a view to considering the question of whether it is capable of general application. This text was negotiated in the concluding stages of the Uruguay Round, and incorporated into the Final Act at the last moment. It was not dealt with in the course of the negotiations for the DSU, which ended well before the Anti-Dumping Agreement was finalized. Earlier proposals for a standard of review similar to the one brought into this Agreement and intended to be of universal application did not find favour in the negotiations for the DSU.

The Agreement on Implementation of Article VII of GATT 1994 (Customs Valuation) has special provisions in Article 19 and Annex II. These refer to the Technical Committee on Customs Valuation, to which specific dispute settlement responsibilities are given.

The Agreement on Subsidies and Countervailing Measures has a number of special or additional provisions relating to dispute settlement. In Article 24, a Committee on Subsidies and Countervailing Measures and a Permanent Group of Experts (PGE) are set up, and both are given a role in dispute settlement. For example, Article 4 states that when a member which has reason to believe that a prohibited subsidy is being granted or maintained by another member, and no mutually acceptable solution has been reached within 30 days of the request for consultations, may refer the matter to the DSU for the establishment of a panel. The panel may request the assistance of the PGE with regard to whether the measure in question is a prohibited subsidy and the PGE's conclusions in this connection will be accepted by the panel without modification. While the panel is not obliged to consult the PGE, if it does so the latter's basic conclusion as to whether the subsidy in question is prohibited or not cannot be modified. This constitutes a departure from normal panel proceedings under the DSU. In addition, time periods as contained in the DSU are considerably shortened under Article 4, and other DSU procedures are adapted to the aims of the Agreement on Subsidies and Countervailing Duties.

**Box 24 (concluded)**

Equivalent clauses to Article 4 are contained in Article 7 (Actionable Subsidies). With respect to Non-Actionable Subsidies, Article 9 sets out procedures for consultations. Whenever these are not successful, the requesting member may refer the matter to the above-mentioned Committee, which may address recommendations to the subsidizing member. Should these recommendations not be followed after six months, the Committee will authorize the requesting member to take appropriate countermeasures. In this case, no reference is made to the DSU. Annex 5 of the Agreement spells out the duties of the Committee or its subsidiary bodies in developing information concerning serious prejudice. This is an important stage in dispute settlement within this Agreement. Article 30 states that the DSU will apply to consultations and the settlement of disputes under the Agreement, except as otherwise specifically provided therein. As mentioned above, this Agreement contains significant provisions of a special or additional nature and any intended action should be preceded by a very thorough analysis of the inter-relationship between the contents of the Agreement and the DSU.

While Article 38 of the Agreement on Safeguards states that the DSU applies to consultations and the settlement of disputes under that Agreement, it should be pointed out that Article 17 foresees the suspension of concessions or other obligations, provided the Council for Trade in Goods does not disapprove.

In the General Agreement on Trade in Services, Articles XXII and XXIII cover, respectively, Consultation and Dispute Settlement and Enforcement. Basically, the DSU is applicable, with certain additional provisions, which include the participation of the Council for Trade in Services in consultations in general and in disagreements over the specific issue of double taxation, where it will refer the matter to binding and final arbitration. The Annex on Financial Services states in paragraph 4.1 that panels on prudential issues and other financial matters will have the necessary relevant expertise. This requirement is obviously common to all dispute settlement cases. Paragraph 4 of the Annex on Air Transport Services establishes that the dispute settlement procedures may be invoked only where obligations or commitments have been assumed by the members concerned and where dispute settlement procedures in bilateral and other multilateral arrangements have been exhausted. Given the extremely wide network of agreements of all sorts that exists in the area of air transportation, this is a logical provision.

Part V of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) deals with dispute prevention and settlement. Article 63 sets out a series of requirements on transparency, with which members must comply. Article 64 affirms the applicability of the DSU to this Agreement, except as otherwise specifically provided therein (paragraph 1). Paragraphs 2 and 3 of the same Article provide the solution that was finally reached after intensive, protracted and inconclusive negotiations in the Uruguay Round, regarding paragraphs 1(b) and 1(c) of Article XXIII of GATT 1994, which refer to non-violation and "any other situation", respectively. These paragraphs will not apply to the settlement of disputes under this Agreement for a period of five years from the entry into force of the WTO Agreement. During this five-year period, the TRIPS Council will examine the scope and modalities for these complaints made pursuant to the Agreement, and submit its recommendations to the Ministerial Conference of WTO for approval. Any decision of the Ministerial Conference to approve such recommendations or to extend the five-year period will be made only by consensus, and approved recommendations will be effective for all members without any further formal acceptance process. Therefore, unless a consensus develops over the five-year period on whatever is to be agreed for the future, paragraphs 1(b) and 1(c) of Article XXIII would cease to apply to the TRIPS Agreement.

The Council for Trade-Related Aspects of Intellectual Property Rights (Article 68) includes among its responsibilities that of providing any assistance requested by members in the context of dispute settlement procedures.

It should be noted that Appendix 2 of the DSU does not include a reference to the above-mentioned provisions of the TRIPS Agreement.

Appendix 2 of the DSU states that the competent bodies of Annex 4 Plurilateral Agreements (Agreement on Trade in Civil Aircraft, Agreement on Government Procurement, International Dairy Agreement and International Bovine Meat Agreement) may notify the DSB of any special or additional rules or procedures they agree upon. None of these Agreements has as yet made any formal determination to this effect.

straightforward and can normally be presented clearly, with the necessary statistical attachments, the second lends itself to more complex reasonings that in turn could give rise to differing interpretations and conclusions.

If a party decides to request authorization to suspend concessions or other obligations pursuant to Article 22:3 (b) or (c), it will state its reasons therefor to the DSB, and these reasons will also be transmitted to the relevant WTO councils and, in the case of Article 22:3 (b), to the relevant WTO sectoral bodies. All interested organs of the WTO will thus be fully advised of any such request. Consequently, the request will be duly considered by each one and transparency will be assured. There is no unilateralism in regard to suspension of concessions, the entire multilateral machinery is involved.

Article 22:3 (f) establishes the necessary definitions of 'sector'. References to goods mean all goods. In respect of services, a principal sector is one that is identified in the "Services Sectoral Classification List". Concerning trade-related intellectual property rights, the reference is to each of the categories shown in sections 1, 2, 3, 4, 5, 6 or 7 of Part II, or the obligations under Parts III or IV of the Agreement on Trade-Related Aspects of Intellectual Property Rights. The sections in question cover Copyright and Related Rights, Trademarks, Geographical Indications, Industrial Designs, Patents, Layout-Designs (topographies) of Integrated Circuits, and Protection of Undisclosed Information.

The definition of "agreement" is contained in Article 22:3 (g). For goods, it refers to Annex IA to the WTO Agreement, which comprises all agreements on trade in goods, as well as the agreements listed in Annex 4 to the same Agreement (Plurilateral Trade Agreements which have limited membership) in so far as the relevant parties to the dispute are parties to these agreements. In regard to services, the reference is to the General Agreement on Trade in Services, and, in the case of intellectual property rights, to the Agreement on TRIPs. These definitions of sector and agreement signify that, subject to the principles established in Article 22:3 (a) to (e), the suspension of concessions may occur in any sector of any Agreement in response to non-compliance in any sector of any Agreement.

Two additional conditions for suspension are set out in Articles 22:4 and 22:5. The level of the suspension authorized by the DSB will be equivalent to the level of the nullification or impairment and the DSB will not authorize

suspension of concessions or other obligations if this is prohibited by a covered agreement. The covered agreements that prohibit suspension are the Agreement on Agriculture (Part VII, paragraphs 1(c) and 2(c) of Article 13, provided that the domestic support measures conform fully to the provisions of Annex 2 of the same Agreement) for a limited period of time, the General Agreement on Trade in Services (Articles XXII and XXIII limit the recourse to dispute settlement in some cases of double taxation), and the Agreement on Trade-Related Aspects of Intellectual Property Rights (Article 64 states that sub-paragraphs 1(b) and 1(c) of Article XXIII of GATT 1994 shall not apply to the settlement of disputes under the Agreement on TRIPs for a period of five years from the date of entry into force of the WTO Agreement, and that this matter will be studied in the meantime and recommendations submitted in due course to the Ministerial Conference). The Agreement on Safeguards should also be seen in this connection.

The determination of the exact level of the nullification or impairment is a delicate matter which lends itself to subjective interpretation. It will often happen that the parties concerned disagree on the proper level of suspension of concessions in regard to a particular case of non-compliance. Article 22:6 deals with this question. Initially, the concept of automatic action is established. The DSB will, at the request of the complaining party, grant authorization to suspend concessions or other obligations within 30 days of the expiry of the reasonable period of time (i.e. when the effort to negotiate compensation has failed), unless it decides by consensus to reject the request. Since a negative consensus requires that the party making the request should join in it, this case is very unlikely to occur. However, if the member concerned objects to the level of suspension proposed, or claims that the principles and procedures set forth in Article 22:3 have not been followed, the matter will be referred to arbitration. This procedure is a further check on any danger of abusive use of the faculty to suspend concessions, and it is to be expected that interested parties will often call for arbitration, particularly when they feel that the request for suspension is excessive and can be demonstrated to be so. The arbitration will be carried out by the original panel if the members are available, or by an arbitrator (either an individual or a group) appointed by the Director-General of the WTO. It would seem that the most appropriate way to proceed would be to convene the original panel members, or at least those who are available for the arbitration, appointing new members to fill any vacancies.

The arbitration process is to be completed within 60 days of the expiry of the reasonable period of time. In actual fact the arbitrator(s) will have fewer than 60 days in which to complete their task, since the request to the DSB to suspend concessions will be made within 30 days of the expiry of the reasonable period of time. This means that if the complaining party makes its request to the DSB 10 days before the expiry date, the arbitrator(s) will only have 40 days to carry out their task, less the time taken by the Director-General to appoint them. Concessions or other obligations will not be suspended during the course of the arbitration (final sentence of Article 22:6). Thus, any unilateral action is excluded.

The duties of the arbitrator(s) are set out in Article 22:7. It is established that the nature of the proposed suspension will not be examined. The arbitrator's responsibility is to determine whether the level of such suspension is equivalent to the level of nullification or impairment. The arbitrator(s) may also determine if the proposed suspension is permissible under the covered agreement in question. This determination is intended to cover situations in which there is a difference of opinion between the parties concerned as to whether the respective covered agreement permits the suspension of concessions or other obligations. The arbitrator(s) will also examine any claim made to the effect that principles and procedures have not been followed and, if it is concluded that they have not been respected, the arbitrator(s) will make the corresponding determination and the complaining party will apply it.

The arbitration decision is final and the parties concerned may not seek a second arbitration. The DSB will be promptly apprised of the arbitration decision and will, at the request of the complaining party, grant authorization to suspend concessions or other obligations where the request is consistent with the decision of the arbitrator, unless the DSB decides by consensus to reject the request.

The whole process of suspension has been carefully devised to exclude any possibility of unilateralism. All stages are clearly set out, the DSB is required to act at the appropriate time, its decisions are always reached by consensus, and binding arbitration is a final and definitive recourse that rounds out the system. It is conceivable, although extremely unlikely, that the complaining party will request the DSB to authorize a suspension that other parties consider to be inconsistent with the arbitration decision, and because the rejection of such a request calls for consensus, it will impede that consensus with its own vote. Theoretically, in terms of the DSU text, the complaining party could put

the suspension into effect. Alternatively, the defendant could initiate its own dispute settlement procedure by asking for a panel.

Article 22:8 reiterates the principle that the suspension of concessions or other obligations will be temporary. It will be applied until such time as:

- the original measure found to be inconsistent with a covered agreement has been removed, or
- the member that must implement recommendations or rulings provides a solution to the nullification or impairment of benefits, or
- a mutually satisfactory solution is reached.

There are therefore three ways for the member concerned to put an end to the suspension of concessions or other obligations applied to it. Not only are the suspensions of a temporary nature, but the party to which they are being applied may seek at any time to put an end to them through the means set out above. In this way, the concept of retaliation is endowed with flexibility in that the member concerned is given every opportunity to work out reciprocally satisfactory solutions. The DSB will keep under surveillance the implementation of adopted recommendations or rulings, including those cases where compensation has been provided or concessions or other obligations have been suspended but the recommendations to bring a measure into conformity with the covered agreements have not been implemented. In other words, the DSB will pursue each case to its conclusion and, so long as this has not been closed, will keep it under active surveillance.

## **7. Strengthening of the multilateral system**

During the whole process of negotiation of the DSU many participants expressed their concern about the dangers of unilateralism. They considered that all members of the WTO should feel confident that the dispute settlement system would be of a truly multilateral nature in all respects and, as such, a solid safeguard against unilateral action by any member. This point of view led to many proposals, which were vigorously discussed in the course of the negotiations. As the drafting of the overall text of the DSU advanced, and successive provisions ensuring the multilateralism of the system were incorporated into it, members were increasingly reassured. However, it was generally agreed that certain essential commit-



ments regarding the strengthening of the multilateral system should be retained, and these are contained in Article 23. These commitments should be read in conjunction with the final sentence of Article 1:1 of the DSU, which states that its "rules and procedures ... shall also apply to consultations and the settlement of disputes between members concerning their rights and obligations under the provisions of the Agreement Establishing the World Trade Organization (WTO) ... and of this Understanding taken in isolation or in combination with any other covered agreement". In other words, a violation of Article 23 by any member is, in itself, cause to invoke the DSU against that member. It is true that in actual practice unilateral action by any government cannot be impeded by others, even though it violates its treaty commitments, but what is possible, and this safeguard has been incorporated into the DSU, is that it will have to answer to the other members for any violation of obligations that its unilateral action implies.

## 8. Non-violation

The issue of non-violation gave rise to lengthy debates in the process of negotiation of the DSU. Its subtlety and the differing views on its treatment added to the difficulties of the negotiations. There have been few cases of non-violation in the history of GATT, and it was even felt by some that it was not particularly necessary to provide for the possibility that they might arise in future. Another view was that the DSU should be comprehensive and foresee all eventualities. This position led to the text of Article 26 of the DSU.<sup>317</sup> Complaints of the type described in Article XXIII:1(b) of GATT 1994 are dealt with in Article 26:1. Where these provisions are applicable to a covered agreement, a panel or the Appellate Body may only make rulings and recommendations when a party to the dispute considers that any benefit accruing to it directly or indirectly under the relevant covered agreement is being nullified or impaired, or the attainment of any objective of that agreement is being impeded as a result of the application by a member of any measure, whether or not it conflicts with the provisions of that agreement. Where and to the extent that such a party considers, and a panel or the Appellate Body determines, that a case concerns a measure that does not conflict with the provisions of a covered agreement to which Article XXIII:1(b) is applicable, the procedures of the DSU will ap-

ply, subject to four conditions which are set out below. In other words, in cases of non-violation where there is a presumed nullification or impairment of benefits, or the attainment of any objective of the respective agreement is being impeded, the four additional conditions need to be observed.

These conditions are as follows:

- (a) The complaining party should present a detailed justification in support of its complaint. Since this justification relates to a measure which does not conflict with the relevant covered agreement, the presentation will go into broader aspects of the matter and may bring out any discrepancy between the stated objectives of the covered agreement and the kind of measures (in this case, the measure objected to) which are authorized under it.
- (b) Where it is found that the measure in question does in fact nullify or impair benefits under, or impede the attainment of objectives of, the relevant covered agreement but without violation thereof, there is no obligation to withdraw the measure, i.e. any such measure takes precedence over the stated objectives of the covered agreement. However, the panel or the Appellate Body shall recommend that the member concerned make a mutually satisfactory adjustment. This adjustment may refer to the measure which has been objected to, or to any other formula that may be agreed between the parties concerned.
- (c) Notwithstanding the provisions on Surveillance of Implementation of Recommendations and Rulings (Article 21), arbitration provided for in Article 21:3, at the request of either party, may include a determination of the level of benefits which have been nullified or impaired, and may also suggest ways and means of reaching a mutually satisfactory adjustment. However, such suggestions will not be binding upon the parties.
- (d) Notwithstanding the provisions of paragraph 1 of Article 22 (Compensation and the Suspension of Concessions), compensation may be part of a mutually satisfactory adjustment as final settlement of the dispute.

In conclusion, in cases of non-violation, the party applying the measure objected to may continue to keep it in force even if it is under considerable pressure to withdraw it or to offer compensation. ■

<sup>317</sup> Future panels will be required to determine whether or not a covered agreement contains a non-violation provision.

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## FUTURE ISSUES

The outcome of the Uruguay Round establishes an institutional framework for managing increasingly complex trade relations in a more competitive and integrated world economy. The Multilateral Trade Agreements contain elaborate review mechanisms and notification requirements, as well as a programme for future negotiations aimed at negotiating substantive provisions of Agreements, bringing improvements into the text of Agreements or verifying the practical implementation of their substantive provisions. The first annex in this chapter outlines what may be considered as a built-in future work programme for the World Trade Organization. Most of the reviews of the provisions and the future negotiations will take place within five years of the entry into force of the WTO. In other words, the agenda for another round of multilateral trade negotiations beginning in 1999-2000 is already provided in the text of the Agreements themselves.

During the final stages of the Uruguay Round, particularly after the conclusion of the negotiations in December 1993, initiatives were taken to make acceptance of the results conditional upon decisions to place certain new issues on the work programme of the WTO Preparatory Committee. The link between trade and environment, trade and competition and trade and labour standards was prominent among these issues. At the Marrakesh Ministerial Meeting, a Decision was taken to establish a Sub-Committee (to the Preparatory Committee) on Trade and Environment. Furthermore, Ministers representing a number of participating delegations stressed the importance they attached to their requests for an examination of "the relationship between the trading system and internationally recognized labour standards, between immigration policies and international trade, trade and competition policy, including rules on export financing and restrictive business practices, trade and invest-

ment, regionalism, the interaction between trade policies and policies relating to financial and monetary matters, including debt, and commodity markets, international trade and company law; the establishment of a mechanism to compensate for the erosion of preferences, the link between trade, development, political stability and the alleviation of poverty, and unilateral or extraterritorial trade measures". As part of a negotiated compromise, it was agreed that the WTO Preparatory Committee would discuss suggestions for the inclusion of additional items on the agenda of the WTO's future work programme, within its scope and functions.<sup>318</sup> In this regard, it is of particular interest that the Committee will take all its decisions by consensus. Therefore, to be able to include an additional item on the WTO's work programme, the item in question should be within the WTO's scope and meet the consensus requirement.

Some of these issues had already been raised at Punta del Este. The Punta del Este Declaration stated that one of the objectives of the Uruguay Round negotiations would be to contribute towards continued, effective and determined efforts to improve the functioning of the international monetary system and the flow of financial and real investment resources to developing countries. Furthermore, the serious difficulties in commodity markets should be taken into account. However, the Chairman's summing up at Punta del Este noted that there were certain issues raised by delegations on which consensus to negotiate could not be reached at the time. Such issues included the export of hazardous substances, commodity arrangements, restrictive business practices and workers' rights.<sup>319</sup>

Some of the items in the Marrakesh summing up had been partially addressed in the course of the Uruguay Round. The progress of the negotiations in the areas of trade and investment has been noted in earlier chapters

<sup>318</sup> GATT document MTN.TNC/MIN(94)6, 15 April 1994.

<sup>319</sup> GATT, *Basic Instruments and Selected Documents (BISD)*, Thirty-third Supplement, Geneva (1987).

in this Supplement, while the interaction between investment policies (where no multilateral obligations exist) and multilateral trade obligations has been codified in greater detail in the TRIMs Agreement. Obligations with respect to the rights of investors *per se* emerged in the General Agreement on Trade in Services (GATS) where commercial presence commitments (often reflecting the qualifications contained in national legislation) were negotiated at the sectoral and subsectoral levels, in return for reciprocal concessions in other sectors and "modes of supply" as well as in other areas of the final package. GATS implicitly recognizes the right of the governments of "home" countries to defend the interests of their corporations established in foreign countries, under the dispute settlement mechanism. GATS would thus seem to have established a framework for the negotiation of commitments on investment which ensure that developing "host" countries are entitled to receive reciprocal concessions for any multilateral commitments they may accept with respect to the treatment of investors.

As noted in chapter I of the Supporting Papers, the Uruguay Round of negotiations attempted to deal with a situation in which the scope of regional agreements, not only in geographical terms but also with respect to the number of issues covered, had extended far beyond anything foreseen by the drafters of GATT Article XXIV. The Uruguay Round resulted in a substantial reduction and often elimination of the tariff margins exchanged by members of regional agreements and the multilateralization of many provisions of those agreements through the acceptance of the Multilateral Trade Agreements. However, regional agreements (particularly those between countries at different levels of development) include obligations on issues such as labour rights, environment and investment on which multilateral agreements could not be negotiated. Tariff margins remain high in certain key sectors of particular export interest to developing countries, and rules of origin can exacerbate their distorting impact on trade and investment flows. What is perhaps required is a mechanism for examining and comparing the provisions of each regional agreement in the light of their compatibility with the WTO instruments.

The issues of compensation for the erosion of preferences in favour of developing countries have to be considered differently in the context of the Generalized System of Preferences (GSP) (applied autonomously to all developing countries) and preferential schemes of limited scope which are incorporated in contractual trade agreements (notably the

Lomé Convention). As noted above, the reduction of MFN tariff rates was a desired result of the Uruguay Round, but some developing countries may have difficulty in facing intensified competition. The extension of regional arrangements has perhaps reduced the significance of GSP margins as a greater percentage of trade is taking place at zero rates among developed countries. In certain product categories, however, GSP margins have provided developing country suppliers with the cost advantage necessary to successfully enter new markets. The tariffication process in the agricultural sector provides the opportunity for introducing meaningful GSP margins. The erosion of rates of some limited preferential schemes has affected the ability of certain poorer developed countries to compete with more advanced, competitive developing countries and countries in transition. Compensation in this area would seem best accomplished through various forms of technical and financial assistance aimed at increasing the productive capacity of these countries and their ability to export their products on a global basis.

With respect to the other issues, the recognition that the globalization of the world economy is leading to ever-growing interactions between the economic policies pursued by individual countries, including interactions between the structural, macroeconomic, trade, financial and development aspects of economic policy making, led to the suggestion of including the trade/monetary/financial link in the future agenda. The objective here is to achieve greater coherence in global economic policy making, especially with regard to achieving stability in exchange rates and integrated management of these three aspects of international economic cooperation. Such coherence would necessitate the reform of the Bretton Woods institutions to enable them to respond to the impact of the financial/monetary policies of the developed countries. The current situation described in Part One of the TDR 1994, in which countries experiencing the greatest difficulty in emerging from the recession find their currencies appreciating compared to those where a strong recovery is taking place, can only add to this concern.

Many of the issues proposed for the WTO work programme have been under discussion in other international forums as, for example, UNCTAD, IMF and the ILO, in the course of which a wide range of economic and political matters have been covered. The highly controversial issue of labour standards is the most illustrative example of this kind. On the other hand, more traditional issues such as trade and competition policy have also been under international discussion for some time,

including in UNCTAD, and could be considered as candidates for a consensus-building effort within a post-Uruguay Round trade agenda.

A new trade agenda is thus beginning to take shape, among which environment and competition policy are perhaps the most clearly defined issues at present. This chapter, drawing on previous work in UNCTAD and elsewhere, attempts to provide a clearer understanding of the evolution of selected issues that have been proposed for inclusion in the future agenda of the WTO. These issues are not the subject of international consensus, and some remain highly controversial and sensitive. A common desideratum for multilateral negotiations on these issues within the WTO context is "levelling the playing field" through the inclusion of certain minimum norms in domestic policies that impinge on economic competitiveness. However, other countries, including most developing countries, are concerned that linking such issues to multilateral trade disciplines will open the door to a whole new generation of "trade remedies" which would be applied with protectionist intent, mainly against developing countries.

The interrelationship between trade and environment has become a source of increasing disquiet to the international community in recent years. Some of the Uruguay Round Agreements, in particular those on Subsidies and Countervailing Measures, Technical Barriers to Trade and Sanitary and Phytosanitary Measures contain provisions that affect countries' ability to take measures to protect the environment. Annex 2 in this chapter analyses that interrelationship and outlines some of the aspects that disturb the developing countries. The question of the interrelationship has arisen in several contexts, as, for instance, in UNCTAD, which has a mandate to consider "sustainable development", in the context of UNCED, in several disputes brought to GATT over the present environmental laws of certain major trading nations, in the negotiation of some regional free trade agreements such as NAFTA, and in last-minute demands by developed countries that the issue should be taken into account in the Uruguay Round. In the context of the Final Act, the Ministerial Decision on Trade and Environment provides for the establishment of a Committee on the subject at the first meeting of the General Council of the WTO to coordinate policies in the field of trade and environment that may result in significant trade effects for the members.

Many statements made at Marrakesh proposed a strong role for the WTO in drafting and enforcing international competition rules covering subsidies, cartels and merger policy. The Havana Charter had included a chapter on restrictive business practices, and the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices negotiated under the auspices of UNCTAD covers certain issues in this area. Some of the Agreements in the Final Act of the Uruguay Round such as those on Subsidies, Anti-Dumping, Safeguards, TRIMs, TRIPs and GATS address competition issues in a somewhat piecemeal manner. As tariff and non-tariff barriers are reduced and eliminated, these private barriers to trade are increasingly becoming the major obstacles to trade expansion; in TRIPs, therefore, to take one example, common minimum standards for restrictive business practices could be developed to structure the links between trade and competition in a global and coherent manner and provide an adequate mechanism for consultation and dispute settlement. It is also of interest to note that the Uruguay Round Agreement on TRIMs provides for the possibility of complementary rules on investment and competition.

On trade and labour standards, some developed countries have pressed for discussion of common international standards and their linkage to the multilateral trading system, but this has been strongly opposed by developing countries on the grounds that it is an excuse for protectionism and will undermine their comparative advantage. The question was recently considered at the 81st Session of the International Labour Conference in June 1994, and resulted in the establishment, within the ILO, of a working party to discuss all relevant aspects of the social dimensions of the liberalization of international trade.<sup>320</sup> Developing countries have proposed the inclusion of the relationship between immigration policies and international trade in the WTO future agenda.

The extent to which WTO's scope may be extended so as to impose multilateral disciplines in additional trade-related areas will depend on the willingness of countries to accept contractual obligations that could expose their policy measures in additional fields to the threat of possible trade sanctions. The subjects envisaged for inclusion in the WTO work programme include wider economic, social and political issues that may both influence, and be influenced by, trade flows. The question arises

<sup>320</sup> "Reply by the Director-General to the discussion of his Report", International Labour Office Governing Body document (GB.260/4/3), and "Questions arising out of the 81st Session of the International Labour Conference", International Labour Office Governing Body document (GB.260/3/7).

as to whether further multilateral negotiations should aim at establishing disciplines in all areas where the lack of sound rules can affect competitiveness in international trade, in other words achieving a "level playing field". Extending the links between multilateral trade obligations and diverse economic and political issues could place severe strains on the multilateral trading system. A widespread concern is also how to address socio-economic, political and other problems that may arise from changes in the size and direction of trade flows, and how best to assist countries that will be unable to compete effectively in order to preserve and strengthen the multilateral trading system.

The emerging trade-related issues need to be analysed from a development perspective so as to enable developing countries to take an active role in determining the future agenda and to support them in their substantive and institutional preparations for future trade negotiations. Through its debates, analysis and technical cooperation programmes, UNCTAD has been able to contribute to the identification of the interests of developing countries and to their effective participation in the Uruguay Round. With its strengthened interdisciplinary mandate, UNCTAD will be in a position to further the coherence of global policy making and to assist in building a consensus for the development of a manageable and transparent new trade agenda. ■

## PROVISIONS ON FURTHER NEGOTIATIONS AND REVIEWS

### A. Further negotiations

#### 1. Agreement on Agriculture

This Agreement provides for a continuation of the reform process, with due recognition of the long-term objective of substantial progressive reductions in support and protection. The negotiations for continuing this process will be initiated one year before the end of the implementation period (i.e. in 1999).

#### 2. General Agreement on Trade in Services (GATS)

GATS provides that members will enter into successive rounds of negotiations, beginning not later than five years from the date of entry into force of the WTO Agreement, i.e. also in 1999. The negotiations will be directed to reducing or eliminating the adverse effects on trade in services of restrictive measures, with a view to providing members with effective market access as well as to increasing the general level of their specific commitments under GATS. GATS lays down several basic parameters for the future negotiations (e.g. respect for national policy objectives and the level of development of individual members, flexibility for individual developing countries, and the establishment, for each round of negotiations, of negotiating guidelines and procedures that will,

in turn, determine modalities for the treatment of liberalization undertaken autonomously by members since previous negotiations, as well as for the special treatment of the least developed countries).

GATS also foresees negotiations on (1) emergency safeguard measures based on the principle of non-discrimination, the results of such negotiations to enter into effect not later than three years from the entry into force of the WTO Agreement; (2) government procurement in services within two years from the entry into force of the WTO Agreement; (3) subsidies aimed at developing the necessary multilateral disciplines to avoid trade-distortive effects of subsidization in services and addressing the appropriateness of countervailing procedures, while recognizing the role of subsidies in the development programmes of developing countries and taking into account the needs of members, particularly developing countries, for flexibility in this area. The modalities and time-frames of the negotiations should be determined by the future work programme.

The Decision on Negotiations on Basic Telecommunications provides for an early resumption of negotiations within a newly established Negotiating Group on Basic Telecommunications, i.e. no later than one month from the date of the Decision. The negotiations should conclude no later than 30 April 1996.

The Decision on Financial Services envisages that members will finalize their posi-

tions relating to MFN exemptions in this sector no later than six months after the entry into force of the WTO Agreement.

The Decision on Movement of Natural Persons provides for the establishment of a Negotiating Group on Movement of Natural Persons to bring about further liberalization in this respect with a view to the achievement of higher levels of commitments by members. The

negotiations should conclude no later than six months after the entry into force of the WTO Agreement.

The Decision on Negotiations on Maritime Transport Services establishes a Negotiating Group, which should conclude the negotiations on the Schedules of Commitments in this sector no later than June 1996.

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## B. Special reviews or work programmes

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The WTO Agreement provides for a regular review of the exemption given to a member not to apply the provisions of GATT 1994 to measures under specific mandatory legislation enacted by that member before it became a contracting party to GATT 1947 ("grandfather clause"). Such exemptions will be reviewed by the Ministerial Conference not later than five years after the entry into force of the WTO Agreement and thereafter every two years for as long as the exemptions are in force for the purpose of examining whether the conditions which created the need for the exemptions still prevail.

The Understanding on the Interpretation of Article XVII of GATT 1994 envisages the establishment of a working party to review notifications and counter-notifications in respect of the activities of state-trading enterprises. The working party will also review the adequacy of the 1960 questionnaire on state trading and the coverage of state-trading enterprises, and draw up an illustrative list showing the relationships between governments and enterprises, and the nature of the activities engaged in by the latter.

Under the Agreement on the Application of Sanitary and Phytosanitary Measures, a procedure will be developed to monitor the process of international harmonization and the use of international standards, guidelines or recommendations in this area. Members will also cooperate in the Committee on Sanitary and Phytosanitary Measures to develop guidelines for the implementation of the concept of an appropriate level of sanitary and phytosanitary protection against risks to human life or health, or to animal and plant life or health.

The Agreement on Technical Barriers to Trade provides for regular reviews of its opera-

tion and implementation with a view to recommending any necessary adjustments to the rights and obligations therein and proposing amendments to its text.

The Agreement on Trade-Related Investment Measures envisages a review of its operation not later than five years after the date of entry into force of the WTO Agreement. At that time, it will be considered whether to complement the Agreement with provisions on investment policy and competition policy.

With regard to the Agreement on Anti-Dumping, a separate Statement on standards of review for dispute settlement panels provides for a review, after three years, to consider the question of its general applicability. Another Statement on anti-circumvention refers this matter to the Committee on Anti-Dumping Practices for resolution, given the desirability of applying uniform rules in this area as soon as possible.

The Agreement on Preshipment Inspection stipulates that the Ministerial Conference may amend its provisions as the result of a review to be conducted at the end of the second year from the entry into force of the WTO Agreement and every three years thereafter.

The Agreement on Rules of Origin provides for a work programme on harmonization of rules of origin to be initiated as soon as possible after the entry into force of the WTO Agreement and to be completed within three years.

The Agreement on Subsidies and Countervailing Measures envisages that some of its provisions such as the definition of serious prejudice to the interests of another member caused by the use of a subsidy, and



identification of non-actionable subsidies, will apply for five years, beginning with the date of entry into force of the WTO Agreement. Not later than 180 days before the end of this period, the Committee on Subsidies and Countervailing Measures will review the operation of these provisions in order to determine whether to extend them in their present form or to modify them.

The GATS Annex on Article II Exemptions provides that all exemptions granted for a period of more than five years will be reviewed by the Council for Trade in Services. The first review will take place no later than five years after the entry into force of the WTO Agreement.

The GATS Annex on Air Transport Services provides for periodical reviews, at least every five years, of developments in the air transport sector, and of the operation of the Annex with a view to considering the further application of GATS in this sector.

The Decision concerning Professional Services provides for the immediate implementation of the work programme on domestic regulations, as established in GATS. A working party will be set up to examine and report, with recommendations, on the disciplines necessary to ensure that measures relating to qualification requirements and procedures, technical standards and licensing requirements in the field of professional services do not constitute unnecessary barriers to trade. As a matter of priority, the working party will make recommendations for the elaboration of multi-lateral disciplines in the accountancy sector.

The implementation of the Agreement on TRIPs will be reviewed after the expiration of the transitional period of five years allowing developing countries and countries in transition to delay, with some exceptions, their application of the Agreement. Reviews may also be

undertaken in the light of new developments that might warrant modification or amendment of the Agreement.

The Decision on Measures in Favour of Least Developed Countries stipulates that the specific needs of these countries will be kept under review, and that positive measures to facilitate the expansion of trading opportunities in their favour will be sought.

The Declaration on the Contribution of the WTO to Achieving Greater Coherence in Global Economic Policymaking invites the Director-General of the WTO to review, with the Managing Director of the IMF and the President of the World Bank, the implications of the WTO's responsibilities for its cooperation with the Bretton Woods institutions as well as the forms such cooperation might take, with a view to achieving greater coherence in global economic policymaking.

The Decision on Notification Procedures stipulates that the Council for Trade in Goods will undertake a review of notification obligations and procedures under the Agreements in Annex 1A to be carried out by a working group to be established immediately after the entry into force of the WTO Agreement. The working group should make the necessary recommendations not later than two years thereafter.

The Decision on the Application and Review of the Understanding on Rules and Procedures Governing the Settlement of Disputes provides for a full review of dispute settlement rules and procedures under the WTO to be completed within four years after the entry into force of the WTO Agreement. A decision should also be taken at the first Ministerial Meeting after the completion of the review regarding continuation, modification or termination of the dispute settlement rules and procedures. ■

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## TRADE AND ENVIRONMENT

Each country has the right to control the environmental effects of domestic production and to protect its own environment against damage from the consumption and disposal of domestically produced or imported products. In addition, all countries have a common but differentiated responsibility for global environmental problems. The recognition that the protection of the environment is a global concern has given rise to the important question of whether multilateral trade obligations conflict with the achievement of an appropriate level of domestic environmental protection, in accordance with their national priorities, and whether they permit transborder and global environmental concerns to be addressed in a way that takes account of the common but differentiated responsibilities of all countries.

The problems associated with trade and environment have essentially three components: (i) the use of trade measures to ensure that imported products conform to environmental standards and regulations, a matter covered by the Agreements on Technical Barriers to Trade and on the Application of Sanitary and Phytosanitary Measures; (ii) the use of trade measures to ensure that processes in force in foreign countries are consistent with the protection of the global environment (which has given rise to the dispute case in GATT on United States Restrictions on Imports of Tuna). This relates to the existence of international environmental agreements and to the possibility of establishing links between these agreements and the multilateral trade obligations of the WTO; (iii) the possibility that differences in national standards for environmental protection may be portrayed as providing unfair advantages to producers located in countries with lower standards (i.e. the so-called "eco-dumping" or subsidization).

Article XX (General Exceptions) permits countries to depart from their GATT obligations to serve legitimate policy objectives which include measures necessary to protect human, animal or plant life or health and the conservation of exhaustible natural resources. The Agreement on Technical Barriers to Trade, based on the fundamental principles of MFN and national treatment, requires that technical regulations and standards should not be formulated or applied in such a manner as to constitute unnecessary obstacles to trade. For this purpose, technical regulations should not be more trade restrictive than necessary to fulfil a legitimate objective. Such objectives include that of protecting the environment.

GATT panels have considered cases involving environmental issues, e.g. disputes involving the United States and Canada over fishing, the United States Superfund levy and the GATT panel ruling against the United States over Mexican tuna fishing and subsequent panels on Tuna.<sup>321</sup> The Tuna panels' rulings were based on a number of issues, including attempts to exercise extra-territoriality for the United States environment protection laws. In the 1991 case involving Mexico, the panel considered that if the broad interpretation of Article XX(b) suggested by the United States was accepted, each contracting party could unilaterally determine the life or health protection policies from which other contracting parties could not deviate without jeopardizing their rights under GATT. GATT would then no longer constitute a multilateral framework for trade among all contracting parties but would provide legal security only in respect of trade between a limited number of contracting parties with identical internal regulations. The panel also pointed out that any environmental protection or conservation of natural resources beyond national jurisdictions should

<sup>321</sup> See United States-Restrictions on Imports of Tuna (DS29/R), United States-Restrictions on Imports of Tuna (DS21/R), United States-Prohibition of Imports of Tuna and Tuna Products from Canada, *BISD*, Twenty-ninth Supplement (1983), p. 93, Canada-Measures affecting Exports of Unprocessed Herring and Salmon *BISD*, Thirty-fifth Supplement (1989), p. 98, United States-Taxes on Petroleum and Certain Imported Substances, *BISD*, Thirty-fourth Supplement (1988) p. 136.

be sought through international cooperation and agreements in multilateral forums and not unilaterally. In the 1994 Tuna case involving the EC and the Netherlands as co-complainants, the panel stated that the issue was whether, in the pursuit of its environmental objectives, the United States could impose trade embargoes to secure changes in the policies pursued by other parties within their own jurisdiction. The panel found that the contracting parties, in agreeing, under Article XX(b), to give each other the right to take trade measures necessary to protect the health and life of plants, animals and persons or aimed at the conservation of exhaustible natural resources, did not agree to accord each other the right to impose trade embargoes for such purposes.

At the regional or global level, a number of International Environmental Agreements (IEAs) include trade provisions.<sup>322</sup> Some doubts

are being expressed as to whether certain trade provisions in international environmental agreements are, strictly speaking, consistent with GATT. Links could be drawn between these Agreements and the multilateral trade obligations of the WTO in a manner similar to that established for intellectual property rights under the TRIPs Agreement.

Developing countries are concerned that changes in GATT rules could mask protectionist intentions, and thus urge that there should be sufficient analysis and debate before any changes in GATT rules are foreseen. UNCTAD's role in this context is to conduct background research and analysis and to build consensus among member States on trade and environment issues, as well as to increase the capability of developing countries to participate in international deliberations on trade and environment.

## A. Environmental provisions from the Uruguay Round Final Act

In the Preamble to the Agreement Establishing the World Trade Organization (WTO) the parties recognize the need to "...protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development". In addition, specific associated agreements explore the scope of trade rules in meeting the objectives of sustainable development.

Rules governing the use of product standards are contained in the Agreement on Technical Barriers to Trade (TBT).<sup>323</sup> This Agreement brings technical regulations adopted for environmental objectives more explicitly within its scope. The preamble to the Agreement recognizes "that no country should be prevented from taking measures necessary" *inter alia* "for the protection of human, animal or plant life or health" or for the protection "of

the environment"... , "at the levels it considers appropriate, subject to" requirements that

- they do not "constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail" or
- "a disguised restriction on international trade" and
- that they are "otherwise in accordance with the provisions of this Agreement".

The Agreement then defines technical regulations as referring to "product characteristics and their related production methods" (PPMs). It encourages countries to follow international standards, except when such standards would be an ineffective or inappropriate means for the fulfilment of the legitimate objectives pursued (Article 2, paragraph 2.4). In these cases, member States are required to

<sup>322</sup> These Agreements include the Montreal Protocol on Ozone Depleting Substances of 1988; the Basle Convention on Hazardous Substances; the Convention on Biological Diversity; and the Convention on International Trade in Endangered Species (CITES).

<sup>323</sup> The GATT Secretariat has undertaken a statistical analysis of the TBT notifications of environmental technical regulations and standards, where the objective and the rationale have been given as the protection of the environment for the period 1980-1994. The total number of such notifications was 349, which represented 8.4 per cent of the total number of notifications made under TBT. For further details see PC/SCTE/W/1, 28 July 1994.

notify their standards or regulations (transparency requirements), if such standards are likely to have significant trade effects. Voluntary standards are also subject to the transparency/notification obligations; this requirement is particularly important in the case of eco-labelling schemes.

The Agreement requires technical regulations not to be more restrictive than necessary to fulfil a legitimate objective, taking into account the risks non-fulfilment would create.<sup>324</sup> In assessing such risks, relevant elements of consideration are, *inter alia*, available scientific and technical information, related processing technology and intended end-uses of products (Article 2, paragraph 2.2).

Differential and more favourable treatment of developing countries is focused on giving developing countries more time to comply with the obligations of the Agreement, i.e. the notification of their domestic regulations. It does not give them a differential schedule for meeting standards in OECD countries. Further, while there are provisions for harmonizing measures or accepting the rules of other countries as equivalent, the establishment of equivalence may well be a slow process. Moreover, environmental measures used by countries may have trade-limiting effects - what is important is to discover how these will have such effects.

A separate Agreement on the Application of Sanitary and Phytosanitary Measures (SPS) includes, among other things, any measure applied to protect human or animal life or health within the territory of the importing country from risks arising from additives, contaminants, toxins or disease-causing organisms in foods, beverages or feedstuffs, as well as to prevent the establishment or spread of pests. SPS provisions differ from those of the TBT Agreement in three important aspects. First, while the latter requires product regulations to be applied on a MFN basis, the SPS Agreement permits measures to be applied selectively provided they "do not arbitrarily or unjustifiably discriminate between countries where identical or similar conditions prevail". Secondly, the provisions of this Agreement allow countries greater flexibility to deviate from international standards than the TBT Agreement. Thirdly, the SPS Agreement introduces the Precautionary Principle, enabling member countries to adopt SPS measures on a "provisional basis", in cases where "relevant scientific evidence is insufficient" by taking into account "pertinent information" that may be available with them or in the relevant international organizations.

This Agreement, like the TBT Agreement, may reflect a concern that rules which are identical may be trade distorting in their application, and not provide "equivalent competitive opportunities" to imported products as to like domestic products. However, Article 9 of the SPS Agreement does provide for technical assistance for developing countries, and Article 6 allows exporters to adapt to regional pest-and disease-free conditions or to "areas of low pest or disease prevalence". Article 10:2 recognizes that it may take developing countries longer to comply with new regulations. It remains to be seen how this concern will be translated into the national legislation of importing countries. Time-limited exceptions to the obligations under Article 10:3 may be of some help to developing countries, but invoking this Article will not be in their export interest.

The Agreement on Subsidies and Countervailing Measures (SCM) divides subsidies into two categories, viz. prohibited and other subsidies. Other subsidies are again divided into two categories: those that are actionable by the importing countries and those that are non-actionable. "Non-specific" subsidies are non-actionable. Certain specific subsidies are also considered non-actionable on environmental grounds. The specificity rule may be more favourable to countries with highly developed economies with an ability to deliver remedies through the income tax system or other broadly based systems. Footnote 2 of the Agreement provides for an exclusion to specificity rules by selecting beneficiaries on the basis of objective criteria and conditions which may be horizontal in application, such as number of employees or size of enterprise. It appears that these selection criteria were intended to designate small businesses, but this is not stated in the Agreement.

Article 6, paragraph 6.7 (f) poses an interesting issue in relation to non-actionable subsidies. Member countries cannot invoke the serious prejudice provisions against import replacement subsidies where the exporter fails to comply with the standards and other requirements of the importing country. This means, in effect, that the importing country could introduce packaging guidelines and provide financial assistance to local firms to meet the regulations while other member countries would be denied the possibility of claiming serious prejudice under Article 6. Article 8 on Identification of Non-Actionable Subsidies (paragraph 2(c)) provides exemptions on a MFN basis to all member countries for assist-

<sup>324</sup> It has sometimes been stated that this provision is intended to ensure proportionality between regulations and the risks that non-fulfilment of legitimate objectives would create.

ance in promoting the adaptation of existing facilities to new environmental requirements imposed by law and/or regulations that result in greater constraints and financial burdens on firms under certain specific conditions. Paragraph 8.4 provides that such assistance will be under review, thereby injecting uncertainty into the Agreement.

The Agreement on Trade-Related Intellectual Property Rights is expected to encourage more research and innovation and better access to new technology, including environmental technology, for all countries. The WTO Committee on Trade and Environment will consider the relevant provisions of the TRIPs Agreement. Of particular interest in this regard is Article 27 on Patentable Subject Matter. Paragraph 2 of this Article provides that members may exclude from patentability inventions, whose commercial exploitation within their territory needs to be prevented in order to protect *ordre public* or morality, including to

protect human, animal or plant life or health or to avoid serious prejudice to the environment, provided that such exclusion is not made merely because the exploitation is prohibited by their law. Paragraph 3 (b) further provides that members may also exclude from patentability plants and animals other than micro-organisms, and essentially biological processes for the production of plants or animals other than non-biological and microbiological processes. However, members should provide for the protection of plant varieties either by patent or by an effective *sui generis* system. The provisions of this subparagraph will be reviewed four years after the entry into force of the WTO Agreement. This subparagraph which is of particular importance for developing countries, relates to the protection of indigenous community rights and biodiversity and leaves the question of their protection to any combination of a patent and a *sui generis* system.

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## B. Conceptual issues on trade and environment

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In the debate on trade and environment a variety of issues arises. One issue is concerned with the possible impact of standards and regulations on market access and competitiveness.<sup>325</sup> Another relates to the question of whether there are advantages, from the trade and environmental points of view, in harmonizing standards. A third relates to the mechanisms that are most appropriate for internalizing environmental costs without distorting trade. These mechanisms should also target the expansion of market opportunities for environmentally friendly goods and services. The current debate on internalization of environmental costs could provide more arguments for protectionist interests.

Environmental externalities can be internalized, for example, through the establishment and enforcement of appropriate environmental standards and regulations.<sup>326</sup> Internalization means that the cost of compliance with such standards should be reflected in market prices, so that standards and regu-

lations influence the behaviour of firms or individuals. It does not mean that standards should be the same in all countries. For example the Polluter Pays Principle (PPP), as defined by the OECD, provides only a limited indication of the appropriate level of environmental standards. Indeed, the PPP merely requires countries to ensure that the environment is "in an acceptable state". A political decision at the local, national and international levels determines the norms and standards which correspond to an acceptable state of the environment. As a result, standards (both ambient environmental standards and emission standards) may vary as justified by such factors as differences in the pollution assimilative capacities, degrees of industrialization, population densities, or social objectives and priorities attached to the environment.

The ability of developing countries to internalize environmental costs will be strongly influenced by the conditions in which they are able to export their products. In order to sup-

<sup>325</sup> UNCTAD, "Sustainable development: Trade and environment - the impact of environment-related policies on export competitiveness and market access (TD/B/41(1)4), Geneva, 1994.

<sup>326</sup> UNCTAD, "The effect of the internalization of external costs on sustainable development" (TD/B/40(2)/6), Geneva, 1994.

port sound environmental policies in developing countries, international cooperation is needed to remove trade distortions, improve commodity prices and the terms of trade of developing countries, reduce indebtedness and increase financial assistance. Developing countries have been less successful than developed countries in ensuring that export prices reflect environmental costs and resource values. To the extent that environmental costs are reflected in the prices that developed countries must pay for their imports, developed country consumers bear at least part of the environmental protection costs in other countries. However, if environmental costs in developing (or, indeed, any other) countries are not incorporated in the prices of their exports, such costs continue to be borne entirely domestically, largely in the form of damage to human health, property and ecosystems.<sup>327</sup> In this context, internalizing environmental costs could bring additional benefits to developing countries. On the assumption that the demand for their natural-resource-based exports is price-inelastic, if most developing countries included the costs of environmental protection in their exports, consumers in the industrialized world would be paying a larger share than previously of the environmental costs associated with their consumption patterns.<sup>328</sup>

Trade can contribute to the internalization of external costs in developing countries by providing them with the means needed to finance environmental improvements. In addition, trade can make direct contributions to cost internalization. Furthermore, UNCTAD's research shows that trade contributes to the diffusion of environmental standards. For example, the environmental requirements of large overseas markets give developing countries important incentives to improve product standards and regulations in their domestic markets. Trade liberalization in both developed and developing countries will facilitate the diffusion of environmentally beneficial goods and services and contribute to the transfer of environmentally sound technologies and environmental management skills to developing countries. UNCTAD's research shows that internalizing environmental costs may entail much higher capital costs but lower running costs than previously. As the opportunity cost of capital is very high in developing countries, future work will focus not only on the extent

of the impact of environmental regulations on competitiveness but also on the differential impact, if any, between developing and developed countries in this respect.

Environmental regulations and standards have an important role to play in protecting the environment and promoting trade provided developing countries participate effectively in the process of standard setting. Further work on this issue should concentrate on positive mechanisms and initiatives on international certification, which will enable developing countries to acquire greater market access and to be more competitive in markets for environmentally friendly products.

The impacts of environmental standards and regulations on market access conditions have not yet been fully assessed. UNCTAD is undertaking a number of studies on the possible impacts on developing countries of regulations of this kind in the major markets. Preliminary results indicate that in some cases newly enacted environmental regulations have unintended trade effects. Lack of timely and precise information about emerging environmental regulations in external markets has also created certain problems. However, by and large, environmental regulations in the OECD countries have so far not led to major trade distortions.

Potential adverse effects of environmental product standards and regulations can be mitigated or avoided by adequate transparency and notification procedures (see the TBT Agreement, Article 10, paragraphs 6-9, and 7 in particular). This could help to reduce uncertainty about environmental requirements in external markets and to ensure that impacts on trading partners, in particular exporters in developing countries and countries in transition, are taken into account as early as possible in the development of new standards and regulations. In some cases, initial problems resulting from emerging environmental regulations have been resolved through bilateral cooperation.

Harmonization of product standards and regulations provides advantages from the standpoints of trade and transparency. As mentioned earlier, the Agreement on Technical Barriers to Trade encourages countries to base technical regulations on international standards. It recognizes that, subject to certain

<sup>327</sup> The World Commission on Environment and Development, *Our Common Future* (Oxford, New York: Oxford University Press, 1987), p. 83.

<sup>328</sup> Robert Repetto of the World Resources Institute has observed that if, for example, environmental costs averaged roughly 2 per cent of production costs, as they do in the United States, then US\$ 500 billion in annual exports from developing countries would include payments of up to \$10 billion by importers, mostly in the industrialized countries, to help defray the costs of environmental protection. See R. Repetto, *Trade and Environment Policies, Achieving Complementarities and Avoiding Conflicts* (Washington, D.C.: World Resources Institute, July 1993).

conditions, no country should be prevented from taking measures at the level it considers appropriate, including those which are necessary for the protection of the environment. It follows that a balance has to be struck between the advantages of harmonization, from the point of view of trade and transparency, and the advantages, from an environmental point of view, of allowing legitimate differences in national standards. Standards may be more efficient and easier to enforce when they reflect the environmental and developmental conditions to which they apply (see the above comments on the TBT and SPS Agreements).

In the case of packaging and labelling requirements that incorporate criteria based on products, processes and production methods (PPMs), concern has been expressed that applying the requirement of national treatment in a narrowly defined sense may not be sufficient to ensure that unnecessary obstacles to trade are avoided, as the PPM in question may not be suitable to conditions in the exporting country. Other issues that will need consideration in this area are the scope for standardization or harmonization and mutual recognition, complications that may arise for trade through the setting of requirements in terms of PPMs rather than product characteristics, and the special difficulties and additional costs that may face small-size foreign suppliers, in particular from developing countries. Developing countries may lack the capital and the technology to adapt their PPMs to those considered acceptable in their main markets for gaining an eco-label. The diversity of eco-labelling schemes in different markets, and the problems that this can cause for all multi-market suppliers, especially relatively small ones, is another area that needs further consideration. Concern is now focused on the impact of PPMs on production costs. In a static analysis, the need for a particular firm to comply with PPM-related standards simply adds to its production costs. Thus, if a firm in one country has to comply with more stringent standards than similar firms elsewhere it may

be expected to suffer a competitive disadvantage. It has, in fact, been argued that competitive concerns tend to prevent the adoption of more stringent environmental standards. A related concern is that countries may deliberately adopt lax environmental standards, or neglect to enforce standards, in order to promote their exports or to attract investment. Some have called for measures to "level the competitive playing field".

Theoretical and empirical analyses indicate, however, that concerns about "eco-dumping" are exaggerated.<sup>329</sup> Empirical studies referring to industrialized countries indicate that the cost effects of environmental process standards to date have been, on average, relatively small.<sup>330</sup> While innovation in expanding industrial sectors may prevent differences in process standards from having any significant effects on international competitiveness, this may not be true of sectors that are natural-resource intensive or are highly dependent on price as a factor of competitiveness. In these cases even relatively small differences in standards will have a significant effect.

Even in the case of product policies such as eco-labelling, the establishment of certain PPM-related criteria in the light of environmental conditions and priorities in the importing country may be irrelevant or inappropriate for exporters in the producing countries. While the majority of eco-labelling schemes are voluntary, since they are designed to differentiate products on the basis of their environmental characteristics they can have a major influence on conditions of competition in a market. UNCTAD's research shows that producers in developing countries may find it difficult to qualify for the label or may be induced to make adjustments that do not contribute to significant environmental improvements.<sup>331</sup> Effective access for foreign suppliers to domestic labelling schemes, namely having the opportunity to participate and express their trade concerns in the process through which product criteria and threshold levels for awarding eco-labels are de-

<sup>329</sup> On this issue see, for example, UNCTAD, "Trends in the field of trade and environment in the framework of international cooperation" (TD/B 40(1)6), 6 August 1993, and Robert Repetto, "High (and low) priority trade and environment issues facing the WTO", paper delivered at the EU/US Roundtable on Environment and Trade, The Hague, 27 January 1994.

<sup>330</sup> One shortcoming of most studies is that they focus on industrial pollution control costs. The cost effects may increase when environmental costs are more fully internalized. Also, methodological and data constraints have prevented most studies from picking up micro-impacts. For a summary of limitations of different studies, see Congress of the United States, Office of Technology Assessment (OTA), *Trade and Environment, Conflicts and Opportunities*, Appendix E, (OTA/BP ITE/94) (Washington, D.C.: U. S. Government Printing Office, May 1992).

<sup>331</sup> To date, the effects of eco-labelling on exports of developing countries may be small since few products of export interest to developing countries are covered (paper being one). However, the EC, for example, is in the process of establishing eco-labels for products such as textiles, clothing and footwear. Products such as textiles and footwear tend to have important "upstream" environmental impacts, which may be as significant as those at the consumption or disposal state, or even more so. Therefore, PPM-related criteria and thresholds may become relatively more important in the future.



cided, as well as access for their products to certification systems and the award of labels on the same terms as domestically produced goods, will be of major importance. In the case of process-related instruments in particular, there is also a need to ensure that attention is given to the specific environmental and developmental conditions of the producing countries.

Concern has been expressed, however, that criteria and thresholds designed in eco-labelling programmes on the basis of environmental conditions and priorities in consumer countries do not always take account of the potential environmental improvements in the producing countries. In this context, UNCTAD's Trade and Development Board has concluded that "eco-labelling programmes should, to the extent possible, take into account the trade and sustainable development interests of producing countries, particularly developing countries and countries in transition. International cooperation on, and further study of, such programmes is required."<sup>332</sup> It is to be noted that this forms one of the impor-

tant agenda items in the WTO's work on trade and environment.

With respect to trading opportunities for developing countries, one question is whether and under what conditions the expansion of trading opportunities for "environmentally friendly" products could provide incentives to developing country producers to introduce environmental improvements. If products can be certified as environmentally friendly or if technology switching results in reduced running costs, an increase in the volume of exports, without price increases, may offer sufficient incentives. In other cases "price premiums" may need to be obtained. Environmental premiums are more likely to be available in environmentally conscious consumer markets in the OECD area than in the home markets of developing country producers. Thus, the most promising way to capture environmental premiums is through increased exports to OECD countries. This issue will also be examined by the WTO Committee on Trade and Environment.

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### C. Future work

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The Ministerial Meeting at Marrakesh decided to direct the first meeting of the General Council of the WTO to establish a Committee on Trade and Environment in the autumn of 1994 (see box 25). The Committee would report to the first biennial meeting of the Ministerial Conference after the entry into force of the WTO, when its work and terms of reference would be reviewed, in the light of the recommendations of the Committee. Pending the entry into force of the WTO, the work of the Committee will be carried out by the Sub-Committee on Trade and Environment. The Sub-Committee will take up items 1, 3 and 6 of the Committee's terms of reference in the autumn of 1994. One of the pressing problems mentioned at the first two meetings of the Sub-Committee was the trend towards unilateral action in addressing extra-jurisdictional environmental problems, which could be tackled by way of an international consensus for global transboundary problems. Another problem is the need to find an equilibrium between promoting multilateral solutions when

dealing with environmental problems on the one hand, and ensuring, on the other hand, that WTO members will not be arbitrarily affected either by disguised protectionism or the imposition of environmental values through trade policy action; a key element in this would be to define multilateral trade agreements and consider the trade effects of measures taken for environmental purposes. On the question of charges and taxes for environmental purposes, it has been suggested to focus on emission charges, tradeable permits and waste management and recycling requirements, all of which relate to the concept of cost internalization and the "Polluter Pays Principle".

Analytical work on a number of these or related issues has already begun in UNCTAD. In its Mid-Term Review, the Trade and Development Board established an Ad Hoc Working Group on Trade, Environment, and Development. Its terms of reference are directed at analysing the effects of environmental policies, standards and regulations on market access and

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<sup>332</sup> Conclusion 407(XL), para. 3(d).

## Box 25

## TERMS OF REFERENCE OF THE WTO COMMITTEE ON TRADE AND ENVIRONMENT

The Decision of the Trade Negotiations Committee of 15 December 1993 which reads, in part, as follows, constitutes, along with the preambular language of the Ministerial Decision on Trade and Environment, the terms of reference of the Committee:

- (a) "to identify the relationship between trade measures and environmental measures, in order to promote sustainable development;
- (b) to make appropriate recommendations on whether any modifications of the provisions of the multilateral trading system are required, compatible with the open, equitable and non-discriminatory nature of the system, as regards, in particular:
  - the need for rules to enhance positive interaction between trade and environmental measures, for the promotion of sustainable development, with special consideration to the needs of developing countries, in particular those of the least developed among them; and
  - the avoidance of protectionist trade measures, and the adherence to effective multilateral disciplines to ensure responsiveness of the multilateral trading system to environmental objectives set forth in Agenda 21 and the Rio Declaration, in particular Principle 12; and
  - surveillance of trade measures used for environmental purposes, of trade-related aspects of environmental measures which have significant trade effects, and of effective implementation of the multilateral disciplines governing those measures;"
  - that, within these terms of reference, and with the aim of making international trade and environmental policies mutually supportive, the Committee will initially address the following matters, in relation to which any relevant issue may be raised:
    - (1) the relationship between the provisions of the multilateral trading system and trade measures for environmental purposes, including those pursuant to multilateral environmental agreements;
    - (2) the relationship between environmental policies relevant to trade and environmental measures with significant trade effects and the provisions of the multilateral trading system;
    - (3) the relationship between the provisions of the multilateral trading system and:
      - (a) charges and taxes for environmental purposes
      - (b) requirements for environmental purposes relating to products, including standards and technical regulations, packaging, labelling and recycling;
    - (4) the provisions of the multilateral trading system with respect to the transparency of trade measures used for environmental purposes and environmental measures and requirements which have significant trade effects;
    - (5) the relationship between the dispute settlement mechanisms in the multilateral trading system and those found in multilateral environmental agreements;
    - (6) the effect of environmental measures on market access, especially in relation to developing countries, in particular to the least developed among them, and environmental benefits of removing trade restrictions and distortions;
    - (7) the issue of exports of domestically prohibited goods.

competitiveness, in particular of the developing countries; emerging environmental policy instruments with a trade impact, bearing in mind the need for international cooperation towards

ensuring transparency and coherence in making environmental and trade policies mutually supportive; exploring market opportunities and implications for exporters which may flow from

the demand for "environmentally friendly" products, taking into account the benefits and costs associated with reducing the negative environmental effects of production processes and consumption; eco-labelling and eco-certification schemes, and possibilities for international cooperation in this field, taking into account the trade and sustainable development interests of producing countries, particularly developing countries and countries in transition. The discussions of the Ad Hoc Working Group will draw upon the research and findings of UNCTAD's technical assistance activities. UNCTAD has also undertaken considerable work on how an international system of tradeable entitlements could limit the worldwide growth of the carbon dioxide emissions which cause global warming. UNCTAD's proposal on this subject has two main aspects: a market-based instrument for controlling such emissions at minimum cost; and an effective mechanism for transferring environmentally-

sound technologies and financial resources to developing countries, to enable them to contribute to the global effort to control greenhouse gases without holding back their own development.<sup>333</sup>

The discussions in the Ad Hoc Working Group, as well as the deliberations of the UNCTAD Trade and Development Board on the following subjects: "Trends in the field of trade and environment in the framework of international cooperation" and "The impact of environment-related policies on export competitiveness and market access") at its autumn sessions in 1993 and 1994 respectively should help to further the consensus-building process as well as contribute to a better understanding of the concerns of developing countries. This could in turn enable developing countries to take an informed position in international discussions on trade and environment matters in the GATT/WTO and elsewhere. ■

<sup>333</sup> *Combating Global Warming: An UNCTAD Study on a Global System of Tradeable Carbon Emission Entitlements* (UNCTAD/RDP/DFP/1), 1992.

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## COMPETITION POLICY AND THE TRADING SYSTEM

### A. Pre-Uruguay Round multilateral negotiations or agreements on restrictive business practices

The international community, recognizing that restrictive business practices (RBPs) engaged in by enterprises can impede or negate the realization of benefits that should arise from the liberalization of tariff and non-tariff barriers affecting world trade, has long attempted to agree upon and implement a multilateral instrument covering RBPs. However, little account has so far been taken at the multilateral level of competition policy in a broad sense, comprising both RBPs of enterprises and governmental measures restricting competition, and the interrelationships existing between them.

Chapter V of the Havana Charter provided that member States should take appropriate measures to prevent business practices affecting international trade which restrained competition, limited access to markets or fostered monopolistic control, whenever such practices had harmful effects on the expansion of production and trade and the maintenance in all countries of high levels of real income or impaired any of the purposes of the International Trade Organization (ITO).<sup>334</sup> A list of such practices was provided, and the ITO would have been competent to arrange for consultations between member countries, to listen to complaints, and to recommend remedial measures. As is well known, the only part

of the Charter to be adopted was chapter IV, which is embodied in the present General Agreement on Tariffs and Trade. A Committee under the aegis of the United Nations Economic and Social Council subsequently formulated a draft convention on control of RBPs in 1953, but again no agreement could be reached on this instrument.<sup>335</sup>

The issue was then explored by GATT. In the decision that was adopted in 1960, the Contracting Parties, while recognizing that RBPs may hamper the expansion of world trade and economic development in individual countries, and thereby frustrate the benefits of tariff reduction and removal of quantitative restrictions ... and that international cooperation is needed to deal effectively with harmful restrictive practices in international trade, considered that in the present circumstances it would not be practicable for the contracting parties to undertake any form of control of RBPs or to provide for investigations.<sup>336</sup> However, provision was made for consultations among contracting parties on a bilateral or multilateral basis as appropriate. The party to which a request for consultations was addressed should accord sympathetic consideration to such a request and afford adequate opportunity for consultations with the requesting party, with a view to reaching mutually satisfactory

<sup>334</sup> United Nations Conference on Trade and Employment, Havana Charter for an International Trade Organization, *Final Act and Related Documents*, 1948, chap. V, Article 46.

<sup>335</sup> See United Nations, *Report of the Ad Hoc Committee on Restrictive Business Practices to the Economic and Social Council* (E/AC.27/3), 1953, p. 5.

<sup>336</sup> Decision of 18 November 1960. See GATT, *BISD*, Ninth Supplement (1961), pp. 173-174.

conclusions. If it agreed that harmful effects were present, it should take such measures as it deemed appropriate to eliminate those effects. The outcome of any such consultations was to be conveyed to the contracting parties.

No notification pursuant to the 1960 Decision has so far been made to the contracting parties. Under the general dispute settlement procedure of GATT Article XXIII, the EC made a request in 1983 for the establishment of a panel, claiming that the benefits of trade negotiations with Japan had not been realized because of, *inter alia*, the concentration and interlinking of the structure of production, finance and distribution in Japan, which made it difficult for foreign suppliers to establish distribution channels.<sup>337</sup> However, this request was eventually dropped.

During the Tokyo Round negotiations, a general notification on RBPs of multinational corporations was included in the Inventory of Non-Tariff Measures.<sup>338</sup> When the negotiating mandate was being elaborated for the Uruguay Round, an attempt was made by some countries to include the issue of RBPs on the agenda, but no consensus could be reached on its inclusion at that time.<sup>339</sup>

The main initiative so far for the adoption and implementation of a multilateral instrument on competition has been taken by UNCTAD. After many years of negotiation, the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices<sup>340</sup> was adopted unanimously by General Assembly resolution

35/63 of 5 December 1980. The Set is not legally binding, but has the authority of an instrument representing the broad consensus of the international community on the fundamental importance of competition principles. The Set applies to RBPs adversely affecting international trade, particularly that of developing countries, and the economic development of these countries. It is universally applicable to all countries and enterprises, and to all transactions in goods and services, although it provides for preferential or differential treatment for developing countries in some respects. It establishes principles and rules for both enterprises and States, provides for international measures for consultation and cooperation, and creates an UNCTAD Intergovernmental Expert Group (IGE) on Restrictive Business Practices as the institutional machinery for the Set.

The analytical work and deliberations undertaken by the IGE, as well as the technical cooperation activities pursued under the umbrella of the Set, have contributed to the present widespread recognition of the importance of competition principles, and to the adoption or reform of competition legislation by a rapidly increasing number of developing countries<sup>341</sup> and countries in transition,<sup>342</sup> as well as China - a trend which is linked with the virtually universal movement towards economic liberalization and market orientation. The Set has thus furnished a stepping-stone to the elaboration of a legally binding instrument on competition linked to the rules of the international trading system.

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## B. The Uruguay Round Agreements and competition

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In a broad sense, all the provisions of the Uruguay Round Agreements have a bearing upon competition since the encouragement of international competition is the basic rationale of trade liberalization. Some provisions directly relevant to competition policy and RBPs in different subject areas are reviewed below:

- The Agreement on Trade-Related Investment Measures (TRIMs) (Article 9) pro-

vides that, not later than five years after the date of entry into force of the WTO Agreement, the Council for Trade in Goods shall review the operation of the Agreement on TRIMs and, as appropriate, propose amendments to the text. In the course of this review, the Council will consider whether the Agreement should be complemented with provisions on investment policy and competition policy.

<sup>337</sup> See GATT document L/5479.

<sup>338</sup> GATT document MTN/3B/1, notification 84.

<sup>339</sup> See *GATT Activities 1986*, p. 29.

<sup>340</sup> UNCTAD document TD/RBP/CONF/10 Rev.1 (United Nations publication, Sales No. 81.II.D.5), 1981.

<sup>341</sup> Including Argentina, Brazil, Chile, Colombia, Côte d'Ivoire, Fiji, Gabon, Kenya, India, Jamaica, Mexico, Pakistan, Peru, Republic of Korea, Sri Lanka, Thailand, Tunisia and Venezuela.

<sup>342</sup> Including Bulgaria, the Czech Republic, Hungary, Lithuania, Poland and the Russian Federation.

- The Agreement on Implementation of Article VI of GATT 1994 (Anti-Dumping) is relevant to the control of RBPs because the trade practices that anti-dumping regimes seek to restrain are essentially the same as the two RBPs of predatory pricing and discriminatory pricing. However, compared to the balanced and equitable manner in which RBP control regimes evaluate such practices at the national level, anti-dumping regimes apply different and more stringent criteria and procedures to the control of such practices when they occur at the cross-border level. Indeed, anti-dumping proceedings may facilitate tacit collusion between import-competing firms and foreign exporters, although the Agreement does tighten somewhat the conditions to be followed in settling proceedings through price undertakings by the exporting firm (Article 8).
- The Agreement on Subsidies and Countervailing Measures is also relevant to competition policy because subsidies can distort the terms of competition among enterprises. Recognizing this, the European Union's competition regulations impose stringent controls upon subsidies granted by Member States of the EU, which can distort the conditions of competition within the Community market.
- The Agreement on Safeguards provides (Article 11:2) that a member shall not seek, take or maintain any voluntary export restraints, orderly marketing arrangements or any other similar measures on the export or import side; examples of similar measures include export moderation, export or import surveillance, compulsory import cartels and discretionary export or import licensing schemes. It also provides (Article 11:3) that members shall not encourage or support the adoption or maintenance by public and private enterprises of equivalent non-governmental measures.
- The General Agreement on Trade in Services (GATS) provides (Article VIII) that each member will ensure that any monopoly supplier of a service in its territory does not, in supplying the monopoly service in the relevant market, act in a manner inconsistent with that member's obligations relating to MFN treatment under Article II and specific commitments. Where a monopoly supplier competes, either directly or through an affiliated company, in the supply of a service outside the scope of its monopoly rights, which is subject to the member's specific commitments, the member will ensure that such a supplier does not abuse its monopoly position to act in its territory in a manner inconsistent with such commitments. These provisions also apply to cases of exclusive service suppliers, where a member, formally or in effect, authorizes or establishes a small number of service suppliers and substantially prevents competition among these suppliers in its territory. Article VIII:3 provides for the Council for Trade in Services to act in connection with a complaint by a member against a monopoly supplier of a service of any other member, by requesting information from the latter member relating to the supplier's conduct, while Article VIII:4 provides for notifications by members to the Council of the grant of monopoly rights regarding services covered by their commitments. The Annex on Telecommunications contains specific provisions concerning access to and use of public telecommunications transport networks and services.
- Under Article IX of GATS, members recognize that certain business practices of service suppliers, other than those falling under Article VIII, may restrain competition and thereby trade in services, and undertake to enter into consultations, at the request of any other member, with a view to eliminating such practices. The member addressed shall accord full and sympathetic consideration to such a request and cooperate by supplying relevant publicly available non-confidential information, as well as other information (subject to its domestic law and to the conclusion of a satisfactory agreement concerning the safeguarding of its confidentiality).
- The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), including trade in counterfeit goods, recognizes as a principle (Article 8), that appropriate measures - consistent with the provisions of the Agreement - may be needed to prevent the abuse of intellectual property rights by right holders or recourse to practices which unreasonably restrain trade or adversely affect the international transfer of technology. In Article 40 (Section 8 on Control of Anti-Competitive Practices in Contractual Licences), members agree that some licensing practices or conditions pertaining to intellectual property rights which restrain competition may have adverse effects on trade and impede the transfer and dissemination of technology. It is provided that nothing in the Agreement shall prevent members from specifying in their national legislation li-

censing practices or conditions that may in particular cases constitute an abuse of intellectual property rights that have an adverse effect on competition in the relevant market, or from adopting (consistently with the Agreement) appropriate measures to prevent or control such practices, which may include, for example, exclusive grantback conditions, prevention of challenges to validity, and coercive package licensing. Procedures for consultations are established similar to those in Article IX of GATS. It is established, for the purposes of dispute settlement, that nothing in the Agreement (subject to the provisions on national treatment and MFN) may be used to address the issue of the exhaustion of intellectual property rights (Article 6).

- In the specific area of patents, the Agreement (Article 31) exempts members from applying a number of conditions to be observed in respect of other use without authorization of the right holder (including use by the government or by third parties authorized by the government), where such use is permitted to remedy a practice determined after judicial or administrative process to be anti-competitive. The need to correct anti-competitive practices may be taken into account in determining the amount of remuneration in such cases, and competent authorities may refuse termination of authorization if and when the conditions which led to such authorization are likely to recur.

### C. Possible multilateral agreement on trade and competition

From the above review, it is apparent that, while the provisions of the Uruguay Round Agreements dealing with competition represent a considerable achievement in bringing closer together the trade and competition paradigms, they address competition issues in a somewhat piecemeal manner. The links with some competition issues are explicitly recognized in certain areas, but other competition issues are neglected, while some are sketchily treated or not mentioned at all in areas to which they are equally relevant. Thus, for example, the SCM Agreement contains no recognition of the obvious overlap between its subject-matter and competition policy, while the Anti-Dumping Agreement does contain some limitations on price undertakings. The Agreement on Safeguards proscribes Members from encouraging or supporting measures by enterprises having effects equivalent to quantitative restraints, but does not require them to prevent such measures. The Agreement on TRIMs prohibits some performance requirements laid down for investors by governments without recognizing that enterprises may impose RBPs having equivalent effects and simply leaves open the possibility for future negotiations on competition issues. The Agreement on TRIPs permits members to take measures against RBPs in licensing agreements, but mentions only a few out of the many RBPs that are often inserted in such agreements (although it does not purport to establish an exhaustive list); moreover, the important issue of parallel

importation is left open (linked to the exhaustion of intellectual property rights). In GATS, governments are required to prevent abuse of monopoly rights, with the telecommunications sector singled out, but no equivalent obligations are established relating to RBPs in non-monopoly sectors. Compared to the 1960 decision applying to trade in goods, the consultation obligations written into GATS are stronger in some respects and weaker in others.

Nor do the Uruguay Round Agreements attempt to deal with such competition issues as exemptions from competition laws, notably for export cartels; market exclusion (whether by dominant firms, through collusion or because of the nature of distribution structures and practices); and the interrelationship between RBPs and governmental rules and restrictions (except to a limited extent in GATS), such as government rules restricting competition in the distribution sector, or export subsidies allowing predatory pricing. There is scope for creating better mechanisms both for addressing RBPs affecting competition at the global level and for encouraging trade regimes to draw upon competition concepts and philosophies to mitigate protectionist or trade-distorting behaviour. This would help to ensure a "level playing field" for all trading firms and countries, particularly developing countries and their firms. There is also scope for improving consultation procedures so as to



ease to a greater extent the tensions likely to arise from extra-territorial and/or concurrent exercises of jurisdiction; difficulties in overseas information-gathering or enforcement (including by developing countries); conflicts between competition and trade policies; uses of competition policy for furthering trading interests; departures from the principles of national treatment or MFN treatment; or allegations that unfair trading advantages are being obtained through inadequate enforcement.

The basic objectives of trade liberalization and competition policy are the same: to increase consumer welfare and economic efficiency. Following the reduction of governmental trade barriers to be brought about by the Uruguay Round Agreements, the dismantling of private barriers to markets is a logical step forward in the progressive liberalization of international trade. Thus, a key role in the post-Uruguay Round scenario should be provided for negotiations on an agreement to structure the links between trade and competition in a global and coherent manner (with appropriate cross-references to provisions in specialized agreements), and to provide adequate mechanisms for consultations and dis-

pute settlement. This would at last allow the prolonged efforts made by the international community in this area to bear fruit. Otherwise, there is a strong risk that the benefits from the trade liberalization to be effected by the Uruguay Round Agreement will be eroded by anti-competitive practices by enterprises and by related government measures (or failure to take appropriate measures). In fact, there appears to be a general consensus among States that negotiations should be undertaken on an agreement on trade-related competition policy under the aegis of the World Trade Organization.

However, the groundwork needs to be laid for such negotiations. UNCTAD would be well placed to contribute towards the necessary analytical work and consensus building; this would be in line both with UNCTAD's broader role and with its specific mandate on competition laid down in the Set of Principles and Rules. The next session of the five-yearly Review Conference on the Set, which is scheduled for 1995, would provide a good occasion to address the modalities for bringing about greater convergence between trade and competition policies. ■

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## RELATIONSHIP BETWEEN THE TRADING SYSTEM AND INTERNATIONALLY RECOGNIZED LABOUR STANDARDS

The attempts to link labour standards to international trade have a long history that can be traced back to the first half of the nineteenth century, and have been dealt with fairly comprehensively in the specialized literature.<sup>343</sup>

The "GATT history" of the attempted linkage begins with the unsuccessful effort to create the International Trade Organization (ITO) in the late 1940s. Article 7 ("Fair Labour Standards") of the 1948 Havana Charter for an ITO stated that "all countries have a common interest in the achievement and maintenance of fair labour standards related to productivity, and thus in the improvement of wages and working conditions as productivity may permit" and that "unfair labour conditions, particularly in production for export, create difficulties in international trade, and, accordingly, each Member (of the ITO) shall take whatever action may be appropriate and feasible to eliminate such conditions within its territory". It was further stipulated that in all matters relating to labour standards the ITO would consult and cooperate with the ILO.

The only mention in GATT 1947 is in Article XX(e), where there is a provision related to labour standards which permits contracting parties to adopt or enforce measures "relating to the products of prison labour". Since then several proposals to link international labour standards and international trade have been made in GATT bodies, mainly by the United States, supported by some other contracting parties.<sup>344</sup> However, the GATT contracting parties were not able to reach consensus on any of them.

The discussion on the relationship between labour standards and international trade, especially at the 81st Session of the International Labour Conference in June 1994, has revealed serious differences among governments on this issue. On the one hand, many developing countries, while not opposing the establishment of international labour standards (see box 26) as such provided that they would reflect differences in levels of development, called upon the ILO to resist the introduction of the "social clause" in international trade. They re-

<sup>343</sup> See, for example, G. Hansson, *Social Clauses and International Trade* (London: Croom Helm Ltd., 1983).

<sup>344</sup> For example, in 1979 the United States made a proposal to consider in GATT minimum international labour standards as a means of pursuing the objective laid down in the GATT Preamble of "raising standards of living". The two substantive elements of this proposal were: (a) differential standards favouring export sectors within a given country, and (b) certain working conditions which were dangerous to life and health at any level of development. The imposition of uniform labour standards on all trading nations was not the purpose of the proposal.

During the preparations for the launching of the Uruguay Round the United States had proposed that the issue of workers' rights be included in the negotiations. However, as the Chairman of the Ministerial Meeting at Punta del Este pointed out, upon the adoption of the Ministerial Declaration, a consensus to negotiate this issue, as well as certain other issues, could not be reached at this time (document MIN.DEC/Chair of 20 September 1986).

In 1987, the United States made several submissions to the GATT Council suggesting the establishment of a working party to examine the possible relationship of internationally recognized labour standards to international trade and to the attainment of the objectives of GATT. The international labour standards to be addressed by such a working party were: (a) freedom of association; (b) freedom to organize and bargain collectively; (c) freedom from forced or compulsory labour; (d) a minimum age for the employment of children; and (e) measures setting minimum standards in respect of conditions of work (GATT documents L/6196 of 3 July 1987 and L/6243 of 28 October 1987). The GATT Council was unable to reach a consensus on this proposal.

In 1990, the United States requested the GATT Council to establish a working party with amended terms of reference to include only three international labour standards: (a) freedom of association; (b) freedom to organize and bargain collectively; and (c) freedom from forced or compulsory labour (GATT document L/6729 of 21 September 1990). Again, there was no consensus on the proposal.

## Box 26

## INTERNATIONAL LABOUR STANDARDS

The term "international labour standards" is usually understood to include Conventions and Recommendations adopted by the International Labour Organisation (ILO) and comprising the International Labour Code. The Constitution of the ILO sets detailed rules and procedures for adoption of such standards by member States. At present, over 170 Conventions and more than 170 Recommendations have been adopted that set international labour standards in the following broad areas:

- Basic human rights
- Employment
- Social policy
- Labour administration
- Industrial relations
- Conditions of work
- Social security
- Employment of women
- Employment of children and young persons
- Older workers
- Migrant workers
- Indigenous workers, tribal populations and workers in non-metropolitan territories
- Workers in special categories.

In a narrower sense, the labour standards most widely ratified by member States of the ILO can be viewed as forming the core of internationally recognized minimum standards. These are:

- Freedom of Association and Protection of the Right to Organize Convention, 1948 (No. 87) - ratified by 109 countries.
- Right to Organize and Collective Bargaining Convention, 1949 (No. 98) - ratified by 123 countries.
- Forced Labour Convention, 1930 (No. 29) - ratified by 135 countries; and Abolition of Forced Labour Convention, 1957 (No. 105) - ratified by 112 countries.
- Equal Remuneration Convention, 1951 (No. 100) - ratified by 120 countries; and Discrimination (Employment and Occupation) Convention, 1958 (No. 111) - ratified by 118 countries.
- Minimum Age Convention, 1973 (No. 138) - ratified by 46 countries.
- Labour Administration Convention, 1978 (No. 150) - ratified by 37 countries.<sup>1</sup>

There is also a large number of ILO Conventions and Recommendations that relate to minimum wages and their protection, limits on hours of work, medical care and health protection, occupational safety and social security.

The ILO Constitution and its Annex (Philadelphia Declaration of 1944) make a distinction between different countries in setting labour standards and applying the more general principles of the ILO. Thus, Article 19, paragraph 3, of the Constitution states that "in framing any Convention or Recommendation of general application the Conference (General Conference of the ILO) shall have due regard to those countries in which climatic conditions, the imperfect development of industrial organization, or other special circumstances make the industrial conditions substantially different and shall suggest the modifications, if any, which it considers may be required to meet the case of such countries". The Philadelphia Declaration, in Part V, stipulates that, while fundamental principles on which the ILO is based are fully applicable to all peoples everywhere, "the manner of their application must be determined with due regard to the stage of social and economic development reached by each people".

The flexibility of international labour standards has been reviewed on a number of occasions in the ILO, usually by special working parties on such standards. The important conclusion emerging from such reviews is that international standards should represent realistic targets for countries at different levels of development, and that particular attention should be paid to ensuring their adaptation to the special needs of developing countries.

Another relevant factor is the state of acceptance and enforcement of international labour standards by various countries. The ILO does not have direct enforcement powers, particularly through imposition of sanctions, but it has extensive review procedures relating to observance of such standards. The state of acceptance of international labour standards varies from country to country, which could be a problem in defining what constitutes an internationally recognized labour standard.<sup>2</sup>

<sup>1</sup> See List of Ratifications by Convention and by country (as at 31 December 1993), ILO, Geneva, 1994.

<sup>2</sup> For example, Argentina has ratified 67 ILO Conventions, Australia 53, Bangladesh 31, Belgium 84, Brazil 73, Canada 28, Chile 41, Egypt 60, France 114, Germany 73, Hungary 52, India 36, Indonesia 10, Italy 102, Japan 41, Kenya 46, Rep. of Korea 3, Malaysia 11, Mexico 76, Morocco 41, New Zealand 56, Nigeria 28, Norway 99, Pakistan 30, Philippines 23, Poland 78, Singapore 21, Sweden 84, Switzerland 50, United Rep. of Tanzania 28, Thailand 11, United Kingdom 80, United States 11, Uruguay 97, Venezuela 52 (See Lists of Ratifications by Convention and by country, ILO, 1994).

garded attempts to invoke ILO standards in this respect as a protectionist device to restrict the free flow of trade and to pressure developing countries to adhere to rigid labour standards as a new condition for market access,<sup>345</sup> thus denying developing countries the comparative advantage they have acquired in production and exports.

On the other hand, several developed countries strongly supported joint ILO/WTO work on this issue, recognizing that it raises complex and sensitive questions which can only be addressed over time. Varying criteria were proposed for determining whether low wages and poor working conditions resulted from bad economic conditions or from political choices. Basic labour standards would become "the reference point" for the future work of the WTO in this area. Some developed countries em-

phasized that it would be preferable for any intervention in this area to be authorized and implemented multilaterally rather than on a unilateral basis, while emphasizing that the "social clause" was not about protection of trade but the protection of people, and did not seek to establish minimum wages across the world.

As a result of the discussion at the ILO Conference, a consensus emerged in the sense that all countries should try to abolish labour practices that violated fundamental human rights. On trade and labour standards, the proposal of the Director-General of the ILO to set up an ILO working party to discuss all relevant aspects of the social dimensions of the liberalization of international trade was adopted.■

<sup>345</sup> See, for example, the resolution submitted by Indonesia, Malaysia, Philippines, Singapore and Thailand, *Provisional Record*, International Labour Conference, 81st Session, Geneva, 1994.

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