

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

L/5191 .

25 September 1981

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AGREEMENT BETWEEN THE EUROPEAN COMMUNITIES AND YUGOSLAVIA

Report of the Working Party

1. At the meeting of the Council on 25 March 1980 the CONTRACTING PARTIES were informed that on 25 February 1980 a Cooperation Agreement had been initialled between the European Economic Community and Yugoslavia. The Agreement would extend to cooperation in the economic, technical, financial, social and trade fields. The relevant clauses concerning the trade area would enter into force on 1 July 1980. Copies of the following instruments were transmitted to the secretariat and circulated to contracting parties in document L/5007 and Add.1:

- Interim Agreement between the European Economic Community and the Socialist Federal Republic of Yugoslavia on Trade and Cooperation, signed on 6 May 1980;
- Exchange of letters amending Annex A to the Interim Agreement between the European Economic Community and the Socialist Federal Republic of Yugoslavia on Trade and Cooperation.

2. At the meeting of the Council of 18 December 1980 a Working Party was set up with the following terms of reference:

"To examine in the light of the relevant provisions of the General Agreement the Interim Agreement between the European Economic Community and the Socialist Federal Republic of Yugoslavia on Trade and Cooperation signed on 6 May 1980, and to report to the Council (L/5095)."

3. The Working Party met on 15 and 21 September 1981 under the chairmanship of Mr. R. Hochörtler (Austria). It had available the texts of the instruments cited above, hereafter called "the Agreement", as well as replies by the parties to the Agreement to questions which had been asked by contracting parties (L/5148 and Add.1).

General Issues

4. In his opening statement, the spokesman for the European Communities recalled the main objectives of the Agreement. He said that the Agreement was one of a series of agreements which had been concluded by the Communities with countries in the Mediterranean region which formed part of a continuing approach to problems in this area. The Communities were strongly interested in promoting the political and economic stability of this region and pursued a balanced and global approach in this respect. It was the Communities' policy to strengthen the harmonious relations with these countries and to contribute to their economic and social development. These objectives were part of the general policy of the Communities in assisting developing countries. In this context he referred to the

Preamble of the Agreement where it was stated that the parties were trying to establish a solid foundation for cooperation between countries having different levels of economic development in the framework of the efforts of the international community to attain a more just and equitable economic order.

5. He further pointed out that the relations between the Communities and Yugoslavia dated back several years. Trade agreements had been concluded in 1970 and 1973. In 1976 the decision had been taken to deepen this relationship which resulted in a Cooperation Agreement signed on 2 April 1980. The Interim Agreement which was now under examination in the Working Party had put into force, as from 1 July 1980, the commercial provisions of the Cooperation Agreement which covered also many other areas like technical, industrial, scientific and financial cooperation as well as social, transport and tourism matters. The examination to be carried out had to be seen in this wider context. The Cooperation Agreement proper would still take some time to be ratified by all participating countries.

6. The spokesman for the European Communities stated that the Agreement provided for the unrestricted access of Yugoslav products to the EC market. The Agreement was based on the GATT provisions relating to the formation of free trade areas; the Communities would consequently respect all obligations under Article XXIV. Since the entry into force of the Agreement the Communities had eliminated customs duties on about 86-87% of imports from Yugoslavia, based on the reference period 1977 - 1979. It was clear that this percentage figure met the requirement of "substantially all the trade" as laid down in Article XXIV. The obligations undertaken by Yugoslavia in the Agreement were different from the ones undertaken by the Communities and took account of the economic situation of Yugoslavia. In order to achieve a more balanced trade between the EC and Yugoslavia the latter had not entered into any reciprocal obligations. Yugoslavia had granted the EC m.f.n. treatment which was a continuation of the system presently in force. Provision was made that in exceptional cases Yugoslavia could introduce new or raise existing duties if this was needed for its economic development. Article 58 of the Cooperation Agreement provided for a review after five years at which it would be decided whether further improvements to the Agreement could be made. This part of the Agreement was, in the view of the EC, consistent with the letter and spirit of Part IV of the GATT. The Agreement would also be technically adapted to take account of the accession of Greece to the EC.

7. In conclusion, the spokesman for the European Communities stressed that the main objective of the Agreement was the liberalisation of trade. He underlined that in the view of his authorities the objectives of economic development and more balanced trade relations which the parties had set themselves in the Agreement, were fully in line with the attainment of the objectives underlying the GATT and that the provisions laid down to that end were consistent with those of the General Agreement.

8. The spokesman for Yugoslavia noted that economic cooperation between Yugoslavia and the Community operated in its entirety on a broad basis, consisting of long-term industrial cooperation, trade, and financial and technical cooperation, and that those many forms of cooperation were marked by the fact that more than 600,000 Yugoslav workers were temporarily

employed in EC countries. The importance of the EC, in view of geographical proximity and long-standing economic ties, in the totality of economic cooperation between Yugoslavia and the rest of the world was best illustrated by the following data. Over the last three years, the share of the EC region in all Yugoslav trade had averaged 35 per cent - 27 per cent for exports and 40 per cent for imports. EC firms accounted for more than 60 per cent of all the contracts on long-term production cooperation, joint ventures, technology transfer and technical cooperation which Yugoslav economic organizations had concluded with foreign firms. The share of the EC in credit and financing cooperation between Yugoslavia and foreign countries amounted to approximately 70 per cent. Lastly, some 75 per cent of all Yugoslavs temporarily working abroad were employed in EC member countries. He stressed that the Agreement between Yugoslavia and the EC was characterized by the fact that it applied to cooperation between partners at different levels of economic development. In that regard, the present Agreement was based on Part IV of the GATT and the results achieved in the final phase of the Tokyo Round in the matter of differentiated and more favourable treatment of developing countries. The Agreement was also in keeping with the objectives and actions initiated by the international community, and more especially by the developing countries, to bring about more just and equitable economic relations between developed and developing countries, and with the efforts being made for the establishment of the new international order. He observed that economic relations in general, and more particularly trade relations, between Yugoslavia and the Community were marked by imbalance, mainly in Yugoslavia's large permanent trade-deficit, which limited the expansion of mutual trade between the two parties. That fact was responsible for Yugoslavia's concern to seek new contractual solutions in trade cooperation with the Community that would improve existing trade flows. He pointed out that the Agreement constituted a contribution to the more harmonious development of trade between Yugoslavia and the EC by way of improved access for Yugoslav products to the Community market. To that end, the Agreement, taking into account the different levels of economic development, provided, in the first stage of application of its provisions on commercial cooperation and trade, for unilateral customs and trade concessions by the Community in respect of most Yugoslav exports, without reciprocity on the part of Yugoslavia. He also stressed the fact that, with the latest enlargement of the EC by the entry of Greece, the Agreement had become even more important, in view of the longer common borders between Yugoslavia and the Community, which increased the need for further promoting more harmonious economic and trade relations between the two parties. All of those specific aspects of cooperation covered by the Agreement had reflected consideration of Yugoslavia as a non-aligned European Mediterranean State and member of the Group of 77 developing countries.

9. One member of the Working Party stated that his authorities fully recognized the motivation behind the Agreement, as a result of which Yugoslavia was to benefit from improved conditions of access to the EC market. These benefits accruing to Yugoslavia would, however, in his view, have certain implications of a commercial nature for the trade of third countries, including his own. This aspect of the Agreement might thus pose certain problems. The major problem related, however, to the consistency

of the Agreement with the General Agreement. It appeared that the parties to the Agreement considered Article XXIV and Part IV to be the legal basis of the Agreement. Article XXIV, however, contained, as a basic principle, the concept of reciprocity. Thus, for a customs union or a free-trade area, the mutual elimination of duties and other restrictive regulations of commerce on substantially all the trade between the parties concerned was required. From the Agreement and from the replies to certain questions in doc. L/5148 and Add.1 it was, however, evident that the concept of reciprocity as a basic requirement under Article XXIV was totally lacking. The reply given in L/5148/Add.1 stated clearly that it was only the Community which eliminated duties and other restrictive regulations of commerce with respect to its trade with Yugoslavia but there was no mutuality of obligations in this respect. The parties would be merely seeking possibilities in the future for making progress towards further elimination of trade barriers. Consequently, it could not be argued that the elimination of trade barriers would apply to substantially all the trade between the two parties. In the view of his authorities there could therefore be no question that Article XXIV could in any way serve as justification for this Agreement. This member of the Working Party went on to say that he had some sympathy for the statement of the parties that the Agreement was consistent with the spirit of Part IV of the GATT but could not share the view that the Agreement was also consistent with its letter, as Part IV of the GATT, inter alia, exhorted developed contracting parties to accord high priority to the reduction or elimination of trade barriers on products of interest to developing countries in general and not on imports from just one of them. Indeed, to take such action in respect of one developing country raised serious problems with regard to the cornerstone on which the GATT was built, namely the m.f.n. principle of Article I. He recalled that the first contracting party which had granted non-reciprocal preferences to developing countries had sought and obtained in 1966 an Article XXV waiver from its GATT obligations in order to introduce a preferential scheme. This waiver was granted by the CONTRACTING PARTIES notwithstanding the fact that Part IV had been adopted the previous year (1965). Thus the CONTRACTING PARTIES did not regard Part IV as providing a derogation from other GATT obligations. More recently, the Enabling Clause had been adopted and this now provided the derogation for the granting of non-reciprocal preferences to developing countries. In his view, therefore, the Agreement also seemed not to be justifiable under Part IV. This member went on to express concern that an incorrect interpretation of Article XXIV and its misapplication in this instance would have the effect of weakening the force of Article XXIV to the detriment of the GATT as a whole. He suggested that the Agreement be presented to the CONTRACTING PARTIES in accordance with footnote 2 of the Enabling Clause which provided for joint action under Article XXV on matters which appeared to be relevant to this Agreement. As the parties would be aware, a precedent for the use of this avenue had recently been established.

10. Another member of the Working Party stated that, when examining the Agreement her authorities had found that it was not in every detail of substance, and in its broader context, exactly like any other of the several trade agreements concluded by the EC. At the same time, the Agreement taken together with the responses in L/5148 and Add.1, raised questions which had been faced before as to the requirements of the General

Agreement for such agreements. Her authorities supported efforts towards improved economic and trade cooperation and had concluded bilateral agreements with several trading partners. At the same time, there existed well-known concerns over those aspects of such agreements which did not meet the requirements set out in the General Agreement to ensure the full and healthy maintenance of the multilateral nature of the GATT system. Her delegation did not consider that the Agreement met the requirements of Article XXIV for free-trade areas or for an interim agreement leading to a free trade area. It also did not agree that Part IV of the General Agreement constituted an exception to the requirements of Articles I and XXIV and it continued to be concerned over the proliferation of preferential agreements, both in terms of its own trade interests and in terms of the integrity of the multilateral system and m.f.n. principle of the GATT. Her delegation would be prepared to examine how the provisions of the Enabling Clause could be brought to bear on the Agreement in a way which would cover the legal concerns. In conclusion, she emphasized that her authorities fully appreciated and supported the efforts made by the parties to the Agreement. She suggested that the parties undertake to report to the CONTRACTING PARTIES in the normal biennial schedule, and that those contracting parties which had concerns as to the compatibility of the Agreement with the General Agreement reserved their position in this regard.

11. One member of the Working Party stated that various free-trade agreements of a similar kind had been examined in GATT. It appeared that none of these agreements had corresponded fully to the provisions of the General Agreement and in particular to Article XXIV. The Agreement under examination seemed slightly different from other agreements since it was concluded among parties with different levels of economic development, a fact which had to be taken into account in the examination. While his authorities considered it very important that the principles of Article XXIV were followed, it was also important to keep in mind the general objectives of the General Agreement and its Part IV. Having this aspect in mind, his authorities had found that the objectives of the Agreement met in the long term the requirements of Article XXIV in spite of the fact that the time period foreseen for reaching them fully was unusually long.

12. Another member of the Working Party stated that his delegation supported the goals and objectives of the Agreement. He expressed concern, however, that the preferential access to the EC market accorded to Yugoslavia under the Agreement might adversely affect his country's and other third countries' exports. He would expect the EC to seek appropriate solutions should difficulties for his country's trade interests arise. He furthermore said that, in spite of the absence of reverse preferences under the Agreement, his delegation was concerned that trade diversion could occur through the application of the origin rules contained in the Agreement. He expected the parties to the Agreement to report biennially to the CONTRACTING PARTIES on its operation. As to the compatibility of the Agreement with the provisions of the General Agreement his delegation was reserving all its rights under the GATT.

13. After the general discussion set out above, the Working Party proceeded to an examination of the Agreement based on the questions and

replies in document L/5148 and Add.1. The main points made during the discussion are set out below.

Questions and replies

14. Referring to the replies given to questions 1, 2, 3 and 7 and commenting on the general statements made by some other delegations, the spokesman for the European Communities said that the parties had not presented the Agreement under any particular provision of the GATT although they were of the view that, among others, Article XXIV, Part IV and the Enabling Clause were relevant in this regard. While the Agreement might, at the present stage, not be fully in line with all relevant provisions of the General Agreement, it had to be seen in the context of its ultimate objective laid down in Article 58 of the Cooperation Agreement, which was the progressive removal, to be carried out in stages, of barriers affecting substantially all the trade between the parties, i.e. the creation over time of a free-trade area. In his view a certain deviation from the basic GATT m.f.n. rule had already been recognized by the CONTRACTING PARTIES through the adoption of Part IV of the GATT and the Enabling Clause. In practice, the GATT did recognize a certain differential treatment of contracting parties, a fact which was also manifested by the very existence of Article XXIV. At any rate the parties to the Agreement did not intend to request a waiver. In the case of similar agreements presented earlier on by the EC, no unanimity of views had emerged supporting a change in the legal basis on which the Community was presenting these Agreements to GATT. Indeed the majority of contracting parties had been prepared to accept that these Agreements were evolutive in nature and that their final objectives could be achieved only over time. The spokesman for the European Communities finally welcomed the fact that several delegations had expressed support for the motivation lying behind the Agreement and its eventual objectives even if they had reserved their position on certain legal aspects.

15. Following a question put by an observer concerning the nature of the Cooperation and Interim Agreements between Yugoslavia and the EC, the parties confirmed that the final objective of these agreements was the formation of a free-trade area with mutual undertakings as referred to in Article 58 of the Cooperation Agreement. Yugoslavia's status as a developing country did not in their view stand in the way of its concluding a free-trade agreement with an economically more developed party. The spokesman for the European Communities added that there did not seem to exist any provision in the GATT which would inhibit a developing contracting party from assuming obligations beyond the ones it had at present, once its state of economic development permitted it to do so. These were the problems to be discussed in the review foreseen in the Cooperation Agreement.

16. Referring to question 5 in doc. L/5198 one member of the Working Party stated that in the view of his delegation the Agreement did not establish a free-trade area under Article XXIV. It would seem difficult to justify an arrangement as a free-trade area if only one of the parties assumed obligations concerning the removal of barriers to their mutual trade. The provision for a review in five years could not satisfy the requirements of Article XXIV. In fact, in the view of his delegation the Agreement did not

even meet the requirements for an interim agreement. With reference to the reply given to question 28, where it was stated that tariff reductions were applied only to 5,68% of total exports of Yugoslavia to the EC in 1979 under the Agreement, his delegation considered that the criteria that substantially all the trade should be covered was not met.

17. In reply the spokesman for the European Communities stated that the figure of 5,68% related only to products subject to tariff reductions under the Agreement. There were, however, many products on which tariffs were no longer applied and, as he had stated earlier, about 86-87% of imports from Yugoslavia entered the EC market without imposition of duties, as could be seen from the reply to question 22(c). If all products on which duties had been reduced or eliminated were taken together, this percentage would increase to over 90%.

18. One member of the Working Party thought that the reply to question 13 was helpful as far as agricultural products were concerned. However, he remained to be convinced that the interests of third countries would not be damaged by the Agreement. As that part of the question dealing with raw materials appeared not to have been answered, he sought further details.

19. In reply, the spokesman of the European Communities pointed out that EC duties on raw materials were generally very low and any preferences for Yugoslavia in this field could not have a major impact on third-country suppliers. He was prepared to provide further information in this respect.

20. Referring to the replies to questions 17, 18 and 19, one member of the Working Party expressed concern about the potential prejudicial effects on, and possible damage to, the trade interests of other contracting parties by the terms of Protocol 2 of the Agreement under which raw materials and semi-fabricated materials originating in the EC and Yugoslavia were considered originating products of Yugoslavia once they were further processed whereas the same products from third countries faced content requirements. He suggested that the first biennial report to the CONTRACTING PARTIES should also examine the effects of the origin rules on trade interests of third countries.

21. The spokesman for the European Communities, referring to previous discussions and consultations on this subject, said that the EC was ready to consider any requests or complaints that might be presented. So far there had never been any request for consideration of these questions in connexion with the biennial reports. He recalled that rules of origin were necessary in order to assure that only the parties to a preferential arrangement benefitted from it. If considered necessary, modifications could always be introduced and had in fact been introduced in the past in the context of similar agreements.

Conclusions

22. There was widespread recognition among members of the Working Party of the purposes and objectives underlying the Agreement, given the particular considerations relevant to Yugoslavia's economic development and the need

for better balanced economic relations that had led to the conclusion of the Agreement.

23. The parties to the Agreement considered that the Agreement was consistent with the objectives and the relevant provisions of the General Agreement taken as a whole, and that it constituted a positive contribution to solving the economic development problems of Yugoslavia. One member of the Working Party found that the objectives of the Agreement met in the long term the requirements of Article XXIV in spite of the fact that the time period foreseen for reaching them fully was unusually long.

24. Other members of the Working Party held the view that the Agreement was not entirely compatible with the requirements of the General Agreement. Some of these members reserved their rights under the GATT with respect to the Agreement.

25. The Working Party noted that the parties to the Agreement were prepared, in accordance with the normal procedure for the examination of biennial reports on regional agreements, to supply all appropriate information on the implementation of the Agreement on a periodic basis. One member urged that the examination of those reports include an analysis of the impact of the rules of origin on third countries' trade.