

**GENERAL AGREEMENT
ON TARIFFS AND TRADE**

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**WORKING PARTY ON THE FREE TRADE AGREEMENTS BETWEEN THE
EFTA STATES AND THE CZECH REPUBLIC AND THE SLOVAK REPUBLIC**

Report

1. The Working Party was established by the Council at its meeting of 14 July 1992 to examine the Free Trade Agreement between the EFTA States and the former Czech and Slovak Federal Republic. Following the dissolution of the Czech and Slovak Federal Republic, two separate Protocols on succession by the Czech Republic and the Slovak Republic to the EFTA-Czech and Slovak Federal Republic Free Trade Agreement were signed, which as from 19 April 1993, formed the legal basis for the continued application of the Agreement between the EFTA States and the successor states. Two separate free trade agreements between the EFTA States and the Czech Republic and the Slovak Republic resulted from the respective Protocols of succession.

2. In order to take these changes into account and to allow the simultaneous examination of the two agreements, at its meeting on 16-17 June 1993, the Council modified the previous terms of reference of the Working Party to read: "to examine, in the light of the relevant provisions of the General Agreement, the Free Trade Agreements between the EFTA States and the Czech Republic and the Slovak Republic, and to report to the Council".

3. The Working Party met on 28 June 1993, 18 February, 9 March, 14 June and 30 November 1994 under the Chairmanship of Ambassador K. Kesavapany (Singapore). The terms of reference and membership of the Working Party appeared in L/7247/Rev.1.

4. The Working Party had before it the following documentation:

- (i) Communication from Iceland on behalf of the EFTA countries and the Czech and Slovak Federal Republic (L/7041)
- (ii) Text of the Free Trade Agreement between the EFTA States and the Czech and Slovak Federal Republic (L/7041/Add.1)
- (iii) Protocols of Succession by the Czech Republic and the Slovak Republic to the Free Trade Agreement between the EFTA States and the Czech and Slovak Federal Republic (L/7220 and Corr.1).
- (iv) Questions and replies (L/7379 and Add.1)

I. General Statements

5. In an introductory statement the representative of Sweden¹, stated that the Free Trade Agreement between the EFTA States and the former Czech and Slovak Federal Republic (CSFR) was signed on 20 March 1992. Following the dissolution of the former Czech and Slovak Federal Republic on

¹Sweden is spokesman for the State Parties to these Free Trade Agreements.

1 January 1993, the Parties agreed to apply the Free Trade Agreement between the EFTA States and the former CSFR on an interim basis. Two separate Protocols were subsequently signed by the EFTA States and the two successor states to the former CSFR in order to ensure the continued application of the Agreement. From 19 April 1993 these Protocols formed the legal basis for the continuation of free trade relations between the Parties to the former Agreement. The form and content of the Agreements, as well as the bilateral arrangements on agricultural products not covered by Protocol A and Annex II were the same as in the original Agreement and arrangements with the former CSFR.

6. The representative of Sweden went on to say that the Free Trade Agreements would support the integration of the Czech Republic and the Slovak Republic into the world economy by contributing to the creation of a European-wide free trade system and by providing the basis for further development of economic co-operation and trade relations between the EFTA States and countries of Central and Eastern Europe. The objectives of the Agreements were to promote the harmonious development of economic relations between the EFTA States and the Czech Republic and the Slovak Republic, to gradually establish free trade between them, to promote fair conditions of competition, to contribute to the harmonious development and expansion of world trade by removal of trade barriers and to improve co-operation between Parties to the Agreements.

7. The Free Trade Agreements covered trade in industrial products, fish and other marine products and processed agricultural products. The Agreements also contained provisions, *inter alia*, on state aid, state monopolies, competition, public procurement, intellectual property rights, services and investment. An evolutionary clause allowed for the extension of the Agreements to areas not currently covered. Under the Agreements the EFTA States would abolish duties and other barriers on imports of Czech and Slovak origin covered by the Agreements from the date of their entry into force, with some exceptions, for which trade barriers would be progressively abolished. The Czech Republic and the Slovak Republic would eliminate trade barriers during the transition period which ends on 30 June 2002.

8. The representative of Sweden concluded his introductory statement by noting that because the EFTA States had no common agricultural policy, trade in agricultural products, not covered by Protocol A and Annex II, was covered by separate bilateral arrangements which formed part of the instruments creating a free-trade area between the EFTA States and the Czech Republic and the Slovak Republic. These arrangements covered a wide number of agricultural products of major importance to the Parties concerned. Together, the Agreements and the bilateral agricultural arrangements covered "substantially all the trade" between EFTA States and the former CSFR.

9. The representative of a group of countries which had its own regional integration arrangements with the Czech Republic and the Slovak Republic, and with the EFTA States, expressed his delegation's support for the Free Trade Agreements. One member said that his country, which had entered into a similar agreement with the EFTA States, shared the objectives of the Agreements. Another member stated his country's general stance towards free trade agreements. They constituted a major derogation from the most-favoured-nation treatment, one of the cardinal principles of GATT. Nevertheless, they were acknowledged by the GATT in so far as they contributed on the whole to the expansion of global trade and the welfare of parties and non-parties.

10. One other member said that examination of free trade agreements was important to ensure their consistency with Article XXIV of the General Agreement. Individual free trade agreements concluded by the European Union and the EFTA States had to be seen in the context of a wider move towards economic integration within Europe. Third countries, in particular, were concerned by the wide proliferation of derogations from Article I of the General Agreement in the form of preferences between countries in this region. To conform with Article XXIV of the General Agreement, free-trade areas were to be achieved within a reasonable length of time, not exceeding ten years; tariffs, duties, other

charges and restrictions on trade between parties were to be eliminated on "substantially all the trade" between the Parties, which was to include "import sensitive" sectors such as agriculture and textiles; the removal of restrictions within a free-trade area were to apply to safeguards or other import restrictive actions; parties to a free trade agreement were not to penalize other partners' efficiency by imposing safeguard or anti-dumping actions or other restrictive measures on their imports. Her delegation believed that should a derogation from the m.f.n. principle be sanctioned through a free trade agreement, the agreement must be based on the premise that the parties to it accepted the "costs" as well as the "benefits", since economic integration should aim at facilitating efficient use of resources.

11. Several other members supported the view that the increasing number of customs unions and free trade agreements called for careful examination of individual agreements to ensure their GATT consistency. One other member supported this view stating that free trade agreements should be trade creating, not trade diverting. They should not lead to regional blocks by restricting the trade of third parties. His delegation supported the transition efforts of the Czech Republic and the Slovak Republic and also supported the efforts made in the context of these Agreements for further integration of their economies into the world economy.

II. Examination of specific points relating to Free Trade Agreements

(i) Trade flows

12. In response to the request of several members for recent statistics on trade flows between the Parties to the respective Agreements, the representative of Sweden, speaking on behalf of the EFTA States and the Czech Republic and the Slovak Republic, said that it had not yet been possible to obtain statistics from the EUROSTAT which would have provided the basis for calculation of the trade flows between the EFTA States and the Czech Republic and the Slovak Republic for the year 1993. The major difficulty laid in obtaining statistical data relating to the trade flows with these partner countries taken separately because the statistical data up to the end of 1992 covered the former CSFR as a whole.

(ii) Coverage

13. With regard to the scope of the Agreements, the Working Party noted the information provided by the Parties that products that were permanently excluded from the coverage of the Agreements in Annex I accounted for a negligible share of total trade between the EFTA States and the Czech Republic and the Slovak Republic.

14. One member observed that the data supplied for 1992 (Attachment to document L/7379) indicated that EFTA countries' trade in agriculture with the Czech and Slovak Federal Republic had included trade in a number of products in HS Chapters 1-24 not listed in Protocol A to the Agreements.

(iii) Customs duties of a fiscal nature

15. In response to a request for further information on customs duties of a fiscal nature applied by the EFTA States, the representative of Sweden informed the Working Party that, as of 1 January 1994 Iceland had ceased the retention of such duties (Protocol C, Table I). The representative of Switzerland stated that in November 1993 the Swiss people had agreed to create the constitutional basis allowing the elimination of customs duties of a fiscal nature applied on mineral oils, fuels and certain motor vehicles. These duties would partially be replaced by internal taxes from 1 January 1997. The federal administration was drawing up the necessary technical and legal measures for the elimination of those customs duties of a fiscal nature. At the entry into force of these measures, foreseen on 1 January 1997, Table II to Protocol C of the Free Trade Agreements would thus become irrelevant.

(iv) Trade in agricultural products

16. In response to a question by a member, the representative of Sweden informed the Working Party that the Parties to the Agreements had agreed to hold the first biennial review, provided for under Article 4 of Protocol A, in autumn 1994. The bilateral trade in agricultural products between the individual EFTA countries and the Czech Republic and the Slovak Republic was subject to review under the specific clauses of the bilateral agricultural arrangements.

17. One member asked for clarification on the meaning of "foster harmonious development of trade in agricultural products" in Article 13.1 of the Agreements, a term which also appeared in the relevant provisions of several other free trade agreements between the EFTA States and third countries. He observed that such free trade agreements sanctioned the coordination of agricultural policies between the EFTA States and their free trade-area partners. He asked whether any provisions of the bilateral arrangements had been designed to foster trade in agricultural products or to coordinate agricultural policies. In response, the representative of Sweden stated that although the special agricultural arrangements had been negotiated bilaterally, for all practical purposes they formed part of the Free Trade Agreements. These arrangements were open to review and Parties could hold consultations for the improvement of their functioning and coverage. Any such arrangements could be considered as contributing towards harmonious development of trade in agricultural products between the parties concerned.

18. Another member expressed the reservation of his authorities regarding the exclusion of unprocessed agricultural products from the coverage of the Agreements. One other member acknowledged that the divergence in agricultural policies and trade regimes prevailing in individual EFTA States was the rationale given by the Parties for the particular treatment of agricultural trade in the free trade agreements concluded by the EFTA States. However, she wondered why this rationale was not relevant also to the industrial trade of the EFTA States. EFTA did not have a common industrial policy but had been able to conclude free trade agreements without special treatment for industrial products. She said that "common policies" between Free-Trade Area Parties were not necessary precursors for full free trade agreements and she did not accept the rationale given for agriculture as relevant to GATT rules for Free-Trade Areas. Her authorities wished to be informed about the prospects for any developments regarding these aspects of the Agreements in the medium to longer term.

19. This member also asked for an explanation of the particular reasons for excluding bulk agricultural products, such as grains, oilseeds, meats, dairy products, etc., from the coverage of the Agreements as well as from the subsidiary bilateral arrangements. In response, the representative of Sweden stated that in their negotiations of these bilateral arrangements the Parties had agreed to include only certain agricultural products of trade interest to them. These various arrangements could evolve in the light of further negotiations between interested parties. The member who asked for an explanation said that while the reply implied that there had been no trade interest in such products between the Parties to the Agreements, it would seem from her country's trade with the individual Parties that they could benefit significantly from free trade in this category of agricultural products. It appeared to this member that the Parties had wished to retain some degree of protection in the agricultural sector in the negotiation of the Agreements.

20. The same member further pointed out that even if, as the Parties had claimed, the bilateral agricultural arrangements were concluded under the framework of the Free Trade Agreements, the arrangements did not provide a plan and a schedule for the elimination of restrictions in this sector, including tariff quotas imposed by certain Parties, thereby not fulfilling the relevant requirements under Article XXIV. The agricultural sector was important to the production and trade of the Czech Republic and the Slovak Republic and greater efforts towards freer trade in this area would accommodate the mutual benefit of the Parties accruing from the Agreements. By way of general comments on the

interpretation of Article XXIV and the purpose of free trade agreements she said that, whether in the area of agricultural trade or in any other sector covered by a free-trade area, protection should be dismantled between parties in the short, medium or long term, either through negotiations or through recognition of mutual interest of parties. Her authorities based the examination of the derogations from Article I by parties to free trade agreements on this principle and therefore, they were concerned that such protection in agricultural trade should be a permanent feature of the present and other future agreements. While her country was a major exporter of agricultural products, her authorities had chosen to take a firm stance concerning the removal of restrictions to agriculture on a non-m.f.n. basis and the full coverage of agricultural sector under free-trade areas because they believed that any derogations sought under Article I should fulfil the objective of the removal of all trade barriers.

21. Several members expressed doubts as to the consistency of the bilateral arrangements with the requirements of Article XXIV since most of the products falling within HS Chapters 1-24 were thereby excluded from the coverage of the Free Trade Agreements. They further noted that the bilateral arrangements appear more oriented to facilitating trade than to achieving free trade for the products concerned, although for the products which were covered by the arrangements free trade would be a goal. The representative of Sweden maintained that the arrangements should be regarded as linked to the free trade agreements and thus as a contribution towards free trade. He furthermore drew attention to the provisions of Article XXIV:4, according to which the purpose of a free-trade area should be to facilitate trade between constituent territories. The representative of Sweden stated the Parties' view that the Agreements were consistent with the relevant provisions of the General Agreement, in that the statistics on trade flows between the Parties indicated that the Agreements, including the bilateral agricultural trade arrangements, covered "substantially all the trade" as required by Article XXIV:8(b). He pointed out that this provision did not require that free trade agreements cover substantially all the trade in all sectors or products.

22. One member asked for information on the conditions under which the Czech Republic and the Slovak Republic applied variable import levies on processed agricultural products from the EFTA States as provided for in Article 2 of Protocol A, and whether the same arrangement was applied by the EFTA States *vis-à-vis* products of Czech and Slovak origins. In reply to her question on the application of such levies by the Czech and Slovak Republics, the representative of the Czech Republic said that the mechanism of variable levies for products contained in Protocol A had not been enforced in these countries since the entry into force of the Agreements. The EFTA States apply such levies in accordance with Article 2 of Protocol A.

23. Another member asked how the provisions concerning variable levies in the Free Trade Agreements and the subsidiary bilateral agricultural arrangements would be adapted to the requirements of the Agreement on Agriculture in the Final Act. She also asked whether the Parties intended to remove the variable levies between the parties at a more accelerated rate than their multilateral commitments. In response, the representative of the Czech Republic, reflecting the views of all the Parties concerned, said that the adaptation of the relevant provisions to the results of the Uruguay Round in the Final Act was a question of a general nature. This matter could be addressed in further consultations between the Parties.

24. In response to a question concerning export subsidies, the representative of Sweden said that the use of export subsidies on trade in agricultural products varied between products and countries. The Parties to the Agreements would abide by their commitments in the Final Act and in Article XVI of the General Agreement regarding export subsidies. Information on subsidies in agricultural trade in individual EFTA States had been notified to Contracting Parties. The Parties did not apply on agricultural products any subsidies which were specific to their mutual trade.

(v) Emergency actions

25. One member raised the question of the relationship between the application of Article XIX and Article XXIV of the General Agreement. She noted that while certain other free-trade area agreements reflected the stance of their parties on this matter, the present Agreements did not contain clear guidelines on the operation of the provisions on safeguard measures, similar to those in Article XIX and other related instruments. The questions remained as to whether free-trade area partners would be exempted from the emergency actions imposed on third parties to the respective Agreements; and whether the safeguard measure would be invoked solely by the Party affected or on a free-trade area-wide basis? While there were differing views on the interpretation of the relationship between Article XIX and XXIV of the General Agreement, her delegation wished to know how safeguard actions were applied in practice among parties to various free trade agreements in Europe. The representative of Sweden stated that the Parties to the Agreements under review maintained their interpretation of the relationship between Article XIX and Article XXIV:8. The questions should be considered as being of a hypothetical nature until actual situations as those described in them had occurred. On such occasions, the Parties would have to decide whether any future emergency action would be taken under GATT Article XIX or under the safeguard provisions of the Free Trade Agreements. Consequently, the present answer would also have to be hypothetical. In a situation where the increase in imports originated in a Free Trade Agreement party, the safeguard provisions of the Agreements would apply, and consequently safeguard action would be imposed, only on goods from the party which was the source of injury. In a situation where there was a general increase in imports from several sources, the provisions of Article XIX would be applied on imports from third party countries, and the safeguard provisions of the Free Trade Agreements on imports from Parties to the Agreements. In this connection he drew attention to the Preambles of the Agreements which stated that no provisions of the Agreements may be interpreted as exempting the Parties from their obligations under the General Agreement. With regard to whether a safeguard measure would be invoked solely by the Party affected or on a free-trade area-wide basis, the representative of Sweden said that a State Party could take recourse to a safeguard measure in an individual capacity.

26. By way of general comments on the issues of application of Article XIX and free trade agreements, the same member said that while any free trade agreement was primarily about the relations between the parties to it, the rights and interests of third parties to the agreement should also be safeguarded as required under the relevant Article of the General Agreement. She expressed her delegations' view that safeguard measures and other emergency actions should not be applied between members of a genuine free-trade area. The continuation of any safeguard action between parties was inconsistent with both the purpose of free-trade areas and with the wording of Article XXIV.

(vi) Other matters

27. A member wondered about the implications for the Free Trade Agreements and the bilateral agricultural arrangements of the future accession of several EFTA States to the European Union since the acceding countries would automatically be bound by the international treaties concluded by the European Union, including the Association Agreements between the European Union and the Czech Republic and the Slovak Republic. In response, the representative of Sweden stated that in terms of the relevant provisions of the Agreements (Article 38) any EFTA member which withdrew from the EFTA Convention would *ipso facto*, on the same day as the withdrawal took effect, cease automatically to be a Party to the Agreements. Individual bilateral agricultural arrangements would also terminate between the Parties to the arrangements at the date of effect of their withdrawal. In the case of, for instance, Sweden and the Czech Republic or the Slovak Republic there was a legal link between the Free Trade Agreements and the bilateral agricultural arrangements. The latter would be terminated at the date of effect of the withdrawal of either of the two Parties from the Agreement.

III. Conclusions

28. The Working Party welcomed the information on the Free Trade Agreements provided by the EFTA States and the Czech Republic and the Slovak Republic in accordance with Article XXIV:7(a).

29. The Working Party noted that the Free Trade Agreements under examination were among the increasing number of free-trade area and customs union agreements concluded between countries within the region in recent years as part of the process of creating a European-wide free trade system. It was also recognized that the Agreements would contribute to further development of economic co-operation and trade relations between the EFTA States and the Czech Republic and the Slovak Republic and would thus advance economic activity and bring about an expansion of overall trade.

30. The Working Party noted that the EFTA States had eliminated customs duties and other import and export barriers on most products covered under the Agreements originating in the Czech Republic and the Slovak Republic on the date of entry into force of the Agreements, with the exception of certain specific products on which import restrictions would be abolished not later than 1998. The Czech Republic and the Slovak Republic had also abolished customs duties on a specified list of products originating in the EFTA States and the restrictions on the remaining products would be phased out within the transitional period of ten years.

31. The Parties to the Agreements, supported by a number of members, considered that substantially all the trade was covered by the Agreements. They noted furthermore that the agricultural bilateral arrangements, concluded within the framework of the Agreements, contributed to facilitating trade between the Parties and did not raise barriers to the trade of other contracting parties with the Parties to the Agreements. However, in this respect, some other members had doubts as to the consistency of the Agreements with the definition of a free-trade area in Article XXIV:8(b) and as to whether it covered substantially all the trade between the Parties.

32. The Working Party noted the assurance given by the Parties that while the relevant provisions of the Agreements did not contain specific guidelines on a possible course of action regarding emergency actions referred to in paragraphs 25 and 26 of the present report involving third parties, the Preamble to the Agreements contained the commitment by the Parties that no provisions of the Agreements may be interpreted as exempting the Parties from their obligations under the General Agreement. Some members, however, pointed to their divergence of views with the Parties to the Agreements regarding the relationship of Article XXIV to Article XIX of the General Agreement.

33. The Parties to the Agreements, supported by a number of members, were of the view that the Free Trade Agreements were consistent with the relevant provisions of the General Agreement. Some other members held, however, the view that there were questions about the full consistency of the Free Trade Agreements between the EFTA States and the Czech Republic and the Slovak Republic with respect to the relevant provisions of the General Agreement, including Article XXIV, and therefore reserved their GATT rights.

34. The Parties to the Agreements are invited, in accordance with the decision of the CONTRACTING PARTIES (BISD 18S/38), to furnish biennial reports on the operation of the Agreements, the first such report to be submitted in 1996.