

**GENERAL AGREEMENT
ON TARIFFS AND TRADE**

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WORKING PARTY ON THE PROTOCOLS REGARDING TEMPORARY ARRANGEMENTS
ON TRADE AND ECONOMIC CO-OPERATION BETWEEN FINLAND AND
ESTONIA, LATVIA AND LITHUANIA

Draft Report

1. The Working Party was established at the Forty-Eighth Session of the CONTRACTING PARTIES held on 2 December 1992 with the following terms of reference: "to examine, in the light of the relevant provisions of the General Agreement, the temporary arrangements on trade and economic co-operation between Finland and Estonia, Latvia and Lithuania, and to report to the Council".
2. The Working Party met on 3 June, 5 July and 8 November 1993 under the Chairmanship of Ambassador J. Seade, Deputy Director-General. The terms of reference and membership of the Working Party appeared in L/7177/Rev.1
3. The Working Party had before it the following documentation:
 - (i) Communication from Finland (L/7130)
 - (ii) Texts of the Protocols Regarding Temporary Arrangements (L/7130/Add.1 and Add.2)
 - (iii) Questions and replies (L/7196)

I. General Statements

4. In an introductory statement the representative of Finland outlined the background to the Protocols Regarding Temporary Arrangements on Trade and Economic Co-operation. In order to support the transition of Baltic countries to market economies and to avoid the erection of any new barriers to trade, Finland started negotiations on trade arrangements with Estonia, Latvia and Lithuania immediately after their independence. On account of the socio-economic situation in these countries his country began to implement the previous trade regime in industrial goods on a unilateral and interim basis, even before the conclusion of negotiations on these arrangements.
5. The representative of Finland went on to point out the changes which had taken place since the Protocols were signed. Originally, provisions on rules of origin allowed for the fact that a large part of the economy of the Baltic countries depended on inputs from various parts of the former Soviet Union. However, changes in Russia and the other Republics of the Commonwealth of Independent States that took place since the formulation of the Protocols had altered this situation. The Joint Commissions governing the Protocols had consequently revised the provision of the Protocols on rules of origin, bringing them into line with the agreements Finland had concluded with other countries within the framework of EFTA. The new rules of origin had been incorporated in the Latvian Arrangement. The arrangements with Estonia and Lithuania, entered into force on 1 May 1993 and 1 July 1993 respectively.

6. One member stated that his government supported the transition of the Baltic countries to market economies. These Protocols were a further step towards their integration into the world economy. Another member recognised the political, social and economic rationale for the Protocols and supported the Baltic countries in their efforts towards trade liberalization as well as the efforts of contracting parties to assist them. Even though her country's trade with the Baltic countries was small her delegation considered that an examination of the GATT consistency of these Protocols was necessary.

7. The representative of a group of countries said that his delegation supported these Protocols, seeing in them an appropriate response by Finland to the economic, social and political situations of the Baltic countries as well as a continuation of a free trade arrangement that had already existed between Finland and the former USSR. A special relationship existed between this group of countries and the countries signatories to these Protocols since Finland was a prospective member of this group. In view of the triangular relationship this group had with both the Nordic and Baltic Countries, the present Protocols were a logical evolution of the geopolitical situation now existing in Europe.

8. Another member expressed his delegation's satisfaction with the Protocols concluded by Finland with the three Baltic States welcoming them as a building block in the regional integration process in Europe. His delegation recognised the rationale agreed within the context of European Free Trade Association for such agreements, which was to respond to the economic difficulties as well as the social and political problems currently encountered by economies in transition in general and the Baltic countries in particular. He went on to say that his delegation considered it fundamental that the regional trade agreements concluded within the framework of European integration were in keeping with the obligations under the General Agreement for these types of arrangements and in particular with Article XXIV. The examination of free trade agreements in the Working Parties should focus essentially on two aspects: that the free trade agreements did not create obstacles to the trade of third parties but rather encouraged the growth of trade; and that the agreements covered substantially all the trade between the parties. His delegation considered that the Protocols between Finland and the Baltic States fulfilled those requirements in Article XXIV, and in particular paragraphs 4 and 8(b).

9. One other member expressed his delegation's continuing support for trade integration agreements in Europe provided they were consistent with the GATT requirements. Furthermore, his authorities encouraged the development of appropriate trade rules and policies by the governments of the Baltic countries which would allow the creation of market economies and the integration of these countries into the multilateral system represented by GATT. Supported by other members, he went on to say that the retention of the margins of preference offered in free trade agreements could cause problems for the Baltic countries when they began the negotiations of the Protocols of Accession to the GATT. Their ability to conduct tariff negotiations for their accession should not be hindered by the existing preferences to Finland through these Protocols. The representative of Finland noted that the arrangements did not contain any provisions that would limit the ability of the Baltic States to conduct tariff negotiations for their accession.

10. The same member noted that the application by Finland to become a member of the European Communities could give rise to a situation where overlapping tariff preferences were being granted by Finland to the Baltic countries and to the European Communities. He asked whether these Protocols allowed Finland to grant preferences to the European Communities, for example, in the agricultural sector in the context of the European Economic Area.

11. The representative of Finland said that his country hoped to be able to retain its free trade agreement with the Baltic countries. How this could be achieved was, however, a question of negotiation. In practice, there already existed substantial free trade between the European Communities and the Baltic countries as a result of the GSP treatment given by the Communities to the Baltic countries on industrial goods, textiles and some agricultural products.

II. Examination of the provisions of the Protocols

12. The Working Party proceeded with a detailed examination of the provisions of the Protocols, taking into account the questions and answers circulated in document L/7196.

13. With regard to the scope of the Protocols, several members noted that agriculture had not been covered in the original Protocols and that separate arrangements on this issue were still being negotiated. The exclusion of agriculture, an important area of trade, from liberalization would mean that the requirement in Article XXIV:8(b) that duties and other restrictive regulations of commerce be eliminated on "substantially all the trade" would not be fulfilled. In the view of these members such conformity with Article XXIV was not measurable solely in terms of an overall level-of-threshold.

14. The representative of a group of countries supported by some other members noted that Article XXIV:8(b) required the obstacles to be eliminated "on substantially all the trade" and not "on trade in substantially all products". In any case, this notion meant less than all trade. In his opinion this gave latitude to the parties of a free-trade area in respect of some products and did not preclude the exclusion of a sector of economic activity provided that the overall trade coverage of the agreement met the criterion laid down in Article XXIV:8(b).

15. The representative of Finland stated that it had not been possible to include the products falling in HS Chapters 1-24 in the Protocols during their initial negotiations due to the instability of the economic situation in the Baltic countries. In order to avoid any delay in the signing of the Protocols, products in HS Chapters 1 to 24 were excluded while negotiations on the issue continued. The Joint Commissions had held discussions with regard to the measures to be taken on these products and this process had been concluded with regard to Estonia. The Joint Committee between Finland and Estonia had signed on 8 October 1993 Decision No. 3/93 amending the Protocol between the two countries to cover also certain products of HS Chapters 1 to 24 (L/7130/Add.2). Discussions were continuing with Latvia and Lithuania. Finland would communicate the results to the Working Party upon the conclusion of its negotiations with the latter countries. One member expressed her delegation's abiding concern regarding the extent to which free trade agreements covered substantially all the trade between the parties including the trade in agriculture, a sector in which the requirements in Article XXIV were applied on a selective basis. She hoped that the information to be provided would allow a more complete examination as to what extent the Protocols fulfilled the requirements of Article XXIV:8(b).

16. In response to a question on the share of trade in agricultural products in the total bilateral trade between Finland and each of the Baltic countries, the representative of Finland stated that, according to preliminary figures for 1992, trade in agriculture between Finland and Estonia accounted for about 7.8 per cent of their bilateral trade, FM 112 million out of total bilateral trade of FM 1,444 million. Trade in agriculture between Finland and Latvia accounted for about 9.5 per cent of their bilateral trade, FM 26.8 million out of bilateral trade of FM 276 million. Trade in agriculture represented about 17 per cent of bilateral trade between Finland and Lithuania reaching FM 28 million out of total bilateral trade of FM 167 million. In view of his delegation, these trade figures gave clear evidence that the Arrangements already met the requirements in Article XXIV:8(b) on "substantially all the trade".

17. The representative of a group of countries stated that the trade data supplied by Finland confirmed his delegations' view that the coverage of the Protocols extended to substantially all the trade in terms of Article XXIV:8(b), since the volume of trade in agriculture between Finland and the Baltic States represented a small proportion of total trade.

18. One member drew attention to the treatment of rules of origin, noting that duties and other regulations of commerce which included rules of origin, should not be higher or more restrictive as a result of the formation of a free trade agreement. The representative of a group of countries sought

assurance that the rules of origin in force in the Baltic countries were effective, well considered and equivalent to the system existing within the EFTA Agreement.

III. Conclusions of the Examination of the Protocols in the light of the relevant provisions of the General Agreement

19. The Working Party welcomed the information provided by Finland in accordance with Article XXIV:7(a).

20. There was wide sympathy within the Working Party with regard to the rationale for the Protocols which were seen as an appropriate response by Finland to the economic, social and political situations in the Baltic countries, given the geographical proximity of these countries and the need to strengthen the traditional trade and economic links between them and Finland.

21. The Working Party also noted that the Protocols would consolidate favourable conditions of market access already provided by Finland to the Baltic countries and thus would encourage the emerging economic liberalization in these countries and facilitate their transition towards market economies.

22. The Working Party recognized that the Protocols would provide a framework of rules for the conduct of trade between Finland and the Baltic countries, thereby supporting the underlying objective of the Protocols to contribute to the process of integrating these countries into the European and world economies.

23. The Working Party noted the confirmation by the delegation of Finland that the tariff preferences granted in the Protocols would not limit the ability of the Baltic countries to conduct tariff negotiations in the context of their protocols of accession to the General Agreement.

24. The Working Party welcomed that with respect to products covered by the Protocols all duties and charges of equivalent effect, as well as quantitative restrictions and measures of equivalent effect, except for a few export restrictions applied by Finland and Latvia, had been eliminated with the entry into force of the Protocols.

25. The Working Party took note of the information provided by Finland relating to the bilateral arrangement between Finland and Estonia covering certain agricultural products. It also noted that negotiations of separate bilateral arrangements in this sector between Finland and Latvia and Lithuania were still under way and that Finland would provide information on the outcome of these negotiations upon their conclusion. Several members of the Working Party expressed concern that the agricultural sector was excluded from the Protocols which, in their view, meant that the requirement in Article XXIV:8(b) that duties and other restrictive regulations of commerce be eliminated on "substantially all the trade" was not fulfilled. These members concluded that there were questions about the consistency of these Protocols with Article XXIV. In this regard three members of the Working Party reserved their rights under the General Agreement. Other members noted that the compatibility with Article XXIV:8(b) should be assessed in the light of the Protocols in their entirety and not only in the context of one or more parts of them. The percentage of trade on which obstacles had been eliminated by the Protocols should therefore be considered as determining whether the provisions of Article XXIV:8(b) have been respected. These members considered that, in the light of the trade data presented, the requirements in Article XXIV:8(b) were fully met.

26. The Working Party agreed that the Protocols were generally in conformity with the relevant provisions of the General Agreement in so far as they did not raise barriers to the trade of third parties and eliminated obstacles to trade between the Parties to the Protocols. However, some other members

considered that the selective treatment of agricultural trade under separate arrangements, albeit still under negotiation, would probably prevent full conformity of the Protocols with the General Agreement.

27. Finland is invited in accordance with the decision of the CONTRACTING PARTIES (BISD 18S/38), to furnish biennial reports on the operation of the Protocols, the first such report to be submitted in the first half of 1995.