

**MULTILATERAL TRADE
NEGOTIATIONS
THE URUGUAY ROUND**

RESTRICTED

MTN.GNG/NG7/7

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Group of Negotiations on Goods (GATT)
Negotiating Group on GATT Articles

NEGOTIATING GROUP ON GATT ARTICLES

Note on Meeting of 25-27 May 1988

1. The Negotiating Group on GATT Articles held its seventh meeting on 25 and 27 May 1988 under the chairmanship of Mr. John M. Weekes (Canada). The Group adopted the agenda contained in GATT/AIR/2567 with the addition under "Other Business" of:

- (i) Chairman's report on the consultations relating to the provision of background material by the secretariat;
- (ii) Requests for additional papers by the secretariat;
- (iii) Dates of future meetings.

Agenda Item A: Consideration of issues arising from the examination of special Articles

Article XVII

2. In an extended statement on this Article one participant maintained that the Uruguay Round presented a vital opportunity to improve both Article XVII and other provisions related to state trading which had largely lost their effectiveness. The weakness of these disciplines sprang in the first place from the lack of a clear understanding about the enterprises and activities covered by Article XVII and about the obligations it entailed. The Article should be understood to impose additional disciplines on contracting parties operating state trading enterprises, not to sanction activities on their part which would distort or impede trade. The lack of understanding as to the definition of enterprises covered had led to sporadic and uneven notifications by contracting parties. Since 1972 less than twenty contracting parties, on average, had responded during any of the last four triennial reporting periods. The Group should consider ways to ensure full compliance with notification requirements. Other contracting parties, including several countries where the state was generally recognized to play a considerable part in commercial affairs, had simply declared that Article XVII did not apply to their enterprises. There also appeared to be considerable confusion between government procurement and general state trading activities.

3. The Negotiating Group should seek a common understanding about the obligations in Article XVII. In particular it should provide a conclusive interpretation as to whether the primary obligation to operate on a nondiscriminatory basis should incorporate both the most-favoured-nation obligation of Article I and the national treatment obligation of Article III. It should also clarify the meaning of the requirement that these enterprises should conduct their activities solely in accordance with commercial considerations. The use of countertrade, particularly government-mandated countertrade, must also be addressed, to clarify how Article XVII might contribute to creating an effective discipline for countertrade activities, which could distort trade and infringe GATT principles. Other trade-distorting activities of State-owned and State-directed enterprises could be addressed under Article VI and XVI of the GATT but there could also be scope for the principles of Article XVII. Effective procedures to ensure compliance might include reverse notifications by third countries of entities in other countries which in their view engage in State trading.

4. A number of participants expressed similar views on the need for stricter disciplines and greater transparency in the operations of state-trading enterprises. In this connection it was suggested that periodic reviews of state-trading activities might be included in the arrangements for surveillance of trade policies under consideration in the Negotiating Group on the Functioning of GATT. One participant emphasised the importance of detailed review of the provisions of Article XVII, in order to reduce the negative effects of the activities of state trading enterprises on the liberalization process and counterbalance the negotiating advantage enjoyed by countries which had such enterprises.

5. Other participants, while they accepted that Article XVII could be improved in certain respects, felt that past experience of its operation had not been such as to warrant wholesale revision. While Article XVII did not give precise definitions, it contained sufficient guidance on the type of enterprises and activities covered to enable contracting parties to decide what they should notify. Nevertheless, the notification obligations were not well observed, and greater transparency would improve the observance of the non-discrimination and "commercial considerations" obligations.

6. It was also said that the great changes which had taken place in this area in the past forty years had rendered the text of this Article inadequate - even in relation to state-trading activities in the market economies. The fact that Article XVII should be seen as a supplementary provision, not as providing an exception from any other GATT obligations, was confirmed by the drafting of paragraph 1(b) "...having due regard to other provisions of GATT..." and by recent panel decisions.

7. In discussion of the applicability of the principle of non-discrimination several participants said that Article XVII encompassed the MFN principle but not that of national treatment, which seemed

irrelevant to the activities of some state enterprises. It was pointed out that it was difficult to reconcile the grant of monopoly status to certain government enterprises with the requirement to accord national treatment to competing imports, and it was suggested that some of the concerns expressed in relation to the activities of state monopolies might more easily be met by a code of conduct for such enterprises than by the amendment of Article XVII. However, the point was also made that in order to prevent trade distortions arising through state trading practices it would be necessary to prevent discrimination as between foreign and domestic products, not merely as between different foreign suppliers. One delegation said that a clarification of the meaning of the phrase "having due regard to the other provisions of this Agreement" in Article XVII:1(b) was thus necessary. The Secretariat was requested to provide information on the applicability of Article III to State Trading Enterprises.

8. In relation to the problems of definition under this Article and the related difficulty of complying with notification requirements, the Secretariat was requested to provide clarification on a number of points:

- the meaning of the footnote to Article XVII:1 concerning the rules applicable to different types of marketing boards;
- the relationship between the obligations of State Trading Enterprises and those of private enterprises. (It was suggested that examination of the drafting history, and notably of the proposals tabled at the New York and London conferences concerning contracting parties maintaining a complete or substantially complete monopoly of trade, would throw light on these matters);
- the decisions taken by the CONTRACTING PARTIES in 1960 and 1962 on which the current arrangements for notifications under Article XVII are based;

9. Some delegations expressed interest in the idea of discussing countertrade in the context of Article XVII. It was said that lack of multilateral surveillance of this growing phenomenon was a weakness of the system. However, other delegations doubted the relevance of countertrade to Article XVII and to the work of this Group. Most countertrade was undertaken by private enterprises, not by governments, and was therefore difficult to subject to multilateral disciplines. Often countertrade was undertaken because normal trade flows were impossible, and was therefore trade-creating. Moreover, even countertrade mandated by governments should not be regarded as distortive per se: to establish this it would be necessary to show that the "commercial considerations" obligation had been disregarded. Article XVII did not treat state-trading enterprises as objectionable in themselves. It was recalled that countertrade, like Restrictive Business Practices, had not been accepted as part of the Uruguay Round agenda. Other speakers argued that countertrade was often used as a means of marketing abroad products which could not otherwise be exported and that long-term obligations to engage in countertrade could create significant distortions.

10. A number of points were made in reaction to some of the questions raised in Chile's submission on Article XVII (MTN.GNG/NG7/W/1). As remarked above, different views were expressed on the desirability of including an explicit obligation to grant national treatment. On the relationship between government procurement and state-trading activities, it was suggested that this should be taken up in the Code on Government Procurement. On the question of increased obligations to notify, it was suggested that the need to preserve commercial confidentiality would have to be borne in mind. On the means of negotiating improved access to markets in areas where state-trading involves an import monopoly or import restrictions, it was pointed out that in the past minimum import commitments had been negotiated and that the secretariat paper NG7/W/15 described the available procedures for negotiation. Concerning the applicability of rules on subsidies, including any new rules to be negotiated in the Uruguay Round, to state-trading enterprises, the point was made that any new disciplines applying to private enterprises should apply equally to state-trading enterprises.

Article XXIV

11. In introducing the discussion on Article XXIV, the Chairman urged a forward looking approach, and said that although an analysis of the past was necessary, the Group should keep particularly in mind the relevance of its work for future developments, taking into account the evolving nature of agreements which had been put in place under this article.

12. One participant said that Article XXIV represented a major derogation from the MFN principle: though its trade-creating effects were not denied, strict discipline and review were needed to preserve market access for third countries and prevent the creation of a system of economic blocs. Though it had been said that retroactive examination of agreements would be difficult, it was necessary to clarify the status of such agreements within the GATT and to define clearly the obligations of their signatories, both because new agreements could well be notified and because most existing agreements were "interim agreements" and should be closely monitored.

13. It was suggested by other participants that the need for a review stemmed in particular from the proliferation of preferential trade agreements, resulting in a large and increasing proportion of trade being carried out on a non-MFN basis and the attendant adverse consequences, in terms of reduced market access, for non-members. The failure to agree on the GATT consistency of most existing agreements constituted another pressing reason for review.

14. Referring generally to Article XXIV, several delegations saw it as a general exception to the MFN principle while others viewed it not as a derogation but as one of the ways of promoting the objective of increasing trade liberalisation enshrined in the General Agreement.

15. In the course of the discussion delegations sought clarification of various concepts contained in Article XXIV; participants also made specific proposals in respect of some of these. These concepts are treated in the following paragraphs.

16. Some participants asked whether revenue duties were covered in the phrase "duties and other restrictive regulations of commerce" contained in Article XXIV:5 and 8. In reply a participant observed that the practices with respect to revenue duties varied in the different preferential trade agreements: revenue duties which had a trade-restrictive impact needed to be identified and eliminated but this proposal might be difficult to apply in practice.

17. With respect to the term "substantially all trade" contained in paragraph 8, whose interpretation had been questioned in one submission, a participant suggested that the term should be assessed in the light of the percentage of trade covered by the agreement and stressed that all participants in the preferential trade agreement should contribute to the liberalisation. Another delegation expressed doubts about the advantages to be derived from clarifying this term and others like "a plan and schedule" (paragraph 6), and "reasonable length of time" (paragraph 6), given the variety of situations encountered and the need to interpret these terms in the light of different circumstances; for example, the coverage envisaged under the term "substantially all the trade" would depend on whether the customs union was formed between developed countries or between developed and developing countries.

18. In the context of Article XXIV:6 one delegation thought that the Secretariat should provide a clarification on (a) the practice of countries unilaterally withdrawing an entire tariff schedule upon the formation of a custom union and subsequently renegotiating it and (b) the notion of "reverse compensation" in case of a reduced tariff incidence after the formation of a customs union. In response it was noted that renegotiations undertaken after the formation of a customs union should be balanced taking into account all changes in duties, including those of interest to the non-member countries involved in the renegotiation; on the issue of reverse compensation a participant wondered whether it had been a real issue in the past.

19. The exclusion of Article XIX from the exceptions granted in paragraph 8 of Article XXIV raised the question as to whether this entitled contracting parties to exclude from safeguard action imports from partners in a customs union or free-trade area. One representative suggested that a review of the drafting history of this article would be useful in understanding this issue.

20. In respect of the discussions on Articles XXIV:6 and XXIV:8 and on the meaning of "general incidence of duties" (XXIV:5 (a) and (b)), a delegation requested that a note be prepared by the Secretariat including previous interpretations of these provisions and of the different views held by delegations and the basis for them.

21. On the interpretation of the term "substantially the same duties and other regulations of commerce" in paragraph 8(ii) one delegation expressed the view that the requirement of a common quota for a customs union was a reasonable one.

22. Some delegations viewed the provisions of paragraph 12, as redressing an imbalance created by actions at sub-federal level violating federal commitments. One participant noting that the federal state was responsible for actions taken by regional authorities, also maintained that paragraph 12 did not limit the application of other GATT Articles like Article XXIII in instances where the failure of the State to live up to these responsibilities was established. One delegation suggested that the Secretariat note (MTN.GNG/NG7/W/13) should be updated to include in its discussion of Article XXIV:12 the finding of a recent panel (Panel on Import, Distribution and Sale of Alcoholic Drinks by Canadian Provincial Marketing Agencies - L/6304) that was adopted.

23. In discussion of the effects of the formation of customs unions and free-trade areas on third countries, several participants maintained that a reduction in market access was an important negative consequence in many cases. Others replied that any negative effects of this kind would be fully compensated by the general trade-creation effects of the creation of customs unions and free trade-areas. One participant observed that Article XXIV:5(a) contained a substantial obligation not to increase barriers to trade of non-members. However there had been no agreement on the manner in which the effects on non-members could be evaluated. Accordingly he proposed that the actual impact on non-members be measured either by identifying trade coverage on products for which duties had changed or in a more sophisticated manner using information on trade elasticities and quantifying the trade creation and trade diversion effects. The same representative suggested the preparation of a Secretariat note outlining various measurement techniques and the tools of economic analysis that could be applied. However, one participant said he was sceptical about the feasibility of isolating the relevant trade effects, however sophisticated the econometric methods used, given that many other factors had to be taken into account.

24. Also on the subject of effects on third countries, a participant considered it necessary to require positive action to improve market access for such countries rather than the existing passive requirement of not increasing barriers to their trade; this might take the form of an obligation on the part of constituent countries to grant non-members, on an MFN basis, a part of the concessions negotiated within the preferential agreement. Some delegations found this proposal unacceptable and contrary to the notion of preferential trade itself.

25. The notification and consultation procedures provided for in paragraph 7 were the subject of extensive discussion in the Group. One participant reiterated the need for an explicit approval of the contracting parties before any agreement could come into force; in the

view of others, prior authorisation was counter to the purpose of Article XXIV which, according to them, conferred an absolute right to enter into a customs union. According to a third view the entry into force of regional agreements should be made conditional on the completion of consultation procedures within the GATT. The need to strengthen consultation procedures, especially with regard to interim agreements, was expressed; some suggested that interim agreements should be made subject to a time limit after which the customs union or free-trade area should come into force. While concurring with the view that notification and review procedures for new agreements needed to be strengthened, a delegation noted that periodic reviews of existing agreements that had fully come into effect were not of much use; moreover the strengthening of surveillance procedures was already being undertaken in another Negotiating Group and there was no need to duplicate these procedures in the context of this Article. One participant suggested that the Group might give thought to the growing number of preferential agreements not notified under Article XXIV; there might be need for formal notification of all preferential agreements, including tariff schedules and trade coverage, for examination and consultations leading to a report. Another speaker suggested that comparison of trade flows under Article XXIV agreements and those under agreements negotiated under the Enabling Clause would be of interest. It was pointed out however that agreements negotiated under the Enabling Clause were already subject to notification and examination in that context and that in any case there was no relationship between them and Article XXIV.

Article XXVIII

26. In introducing the discussion of Article XXVIII the Chairman drew attention to a recent submission from Australia (MTN.GNG/NG7/W/42). He recalled that discussion on this Article had been extensive in the past, and particularly so at the previous meeting of the Group.

27. One delegation drew attention to the proposal already made with a view to improving the negotiating rights of smaller trading countries, and suggested that an additional principal supplying right should be created in favour of countries for goods which constituted a major part of their total exports: the exception in paragraph 5 of the interpretative note to Article XXVIII would thus become a recognized criterion rather than an exception. The proposal by Australia, in particular the idea of a "de minimis" clause for very small trade flows - which would simplify and accelerate negotiations - deserved careful attention. It would also simplify and rationalise Article XXVIII procedures if the three different mechanisms for entering into negotiations on the modification or withdrawal of concessions could be replaced by a single provision.

28. Several delegations said that they would welcome further discussion of the issues raised in the recent submission by Australia. It was suggested by a number of delegations that it would be helpful if the Chairman would produce a non-paper listing the issues raised and proposals made so far on Article XXVIII. One participant cautioned against allowing work on one Article to proceed too far ahead of others.

Agenda Item B: Other Businessi) Chairman's report on the consultations relating to the provision of background material by the secretariat

29. As promised at the previous meeting, the Chairman reported on his consultations concerning requests made to the secretariat for the production of factual information on three issues. On the first - a request for statistical information on the implications of different criteria proposed for the attribution of suppliers' rights under Article XXVIII - a paper could be made available at short notice. The second request was for factual information on the consultations held in the Balance-of-Payments Committee since 1974: delegations were aware of the sensitivity of this issue and of the difficulties encountered, but the Chairman wished to recognize the co-operative and positive spirit which all delegations had shown. It was the Chairman's understanding that the paper could now proceed, subject to any final comments on its precise scope and contents. The Chairman had therefore prepared a short text, which had been circulated informally in the Group, and which he believed should prove acceptable to all participants. He requested members of the Group to communicate any comments on this text by 6 June, when it would be his intention that the secretariat should go ahead with production of the paper. The third subject on which the Chairman had undertaken consultations was the proposed enquiry on the legislation and measures maintained under the Protocol of Provisional Application; he anticipated that with some minor amendments the letter to all contracting parties which delegations had received in draft would shortly be issued in final form. The Chairman emphasized that he saw these three requests as distinct and unrelated.

30. One participant regretted that his delegation had not been involved in informal consultations on a subject of great importance to his country. For this reason it would be difficult for his authorities to comment on the proposed contents of the paper on the operations of the Balance-of-Payments Committee within the short period proposed; he hoped that some flexibility would be accorded. It was agreed that the Chairman would discuss this point with the participant concerned.

ii) Requests for additional papers by the Secretariat

31. The Chairman recalled that one delegation had requested additional information in regard to Article XVII (paragraphs 7 and 8 supra). Other delegations also requested further work on various points relating to Article XXIV (paragraphs 18, 19, 20, 22 and 23 supra). It was the Chairman's understanding that there was no problem with these requests as they would result in the production of factual information. In some cases the precise nature of these requests needed clarification; he suggested that the interested delegations and the secretariat should make contact on these points. Informal discussions would be organised only if the need arose.

iii) Date and Agenda of the next meeting of the Group

32. The Group agreed that its eighth meeting would be held on 27 and 30 June and 1 July 1988. The Chairman said he expected that in this meeting attention would be focused on issues arising from Articles other than those discussed at the last two meetings (XVII, XXIV, and XXVIII). Since the number of Articles remaining was considerable and it was difficult for participants to prepare on all issues, he thought he should inform the Group that he had received indications from participants that they intended to refer to Articles XII, XIV, XV, and XVIII and to Article XXV:5. It should of course be open to all participants to raise any other issues.

Date of the Autumn meeting

33. Note was taken of the Chairman's suggestion to hold the ninth meeting of the Group on 20, 21 and 23 September 1988.