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ARTICLE XXVIII

Submission by Switzerland

The following submission has been received from the delegation of Switzerland, with the request that it be circulated to members of the Negotiating Group.

Switzerland has already submitted an initial proposal for improving the functioning of Article XXVIII (see document MTN.GNG/NG7/W/11 of 29 June 1987).

In the light of the contributions made by other participants in the Group, Switzerland submits herewith a second proposal aimed at resolving problems concerning the application of Article XXVIII which have been identified in the course of the Group's work.

I. Formula for the determination of additional supplier's rights

1. Analysis of the present situation

Article XXVIII grants negotiating rights to two categories of contracting party: firstly, the contracting party having an initial negotiating right, and secondly the contracting party recognized as the principal supplier. The contracting party authorized to negotiate as principal supplier is the one that has the largest share of imports on the market of the party intending to modify the concession (see interpretative note 4 ad Article XXVIII:1).

Article XXVIII provides that any contracting party having a "substantial interest" in the concession has a right of consultation. Once again, the criterion for defining this "substantial interest" is the share of the import market (see note 7 ad Article XXVIII:1).

In addition, interpretative note 5 ad Article XXVIII:1 specifies that exceptionally a contracting party may be recognised as having a principal supplying interest on the basis of the significance of the trade affected in relation to its total exports. This note 5, which is very imprecise, only provides the possibility and not the right of obtaining an additional negotiating right. Of little practical use, this note has virtually never been applied.

Over the last few years, negotiating rights have become increasingly concentrated on an ever smaller number of contracting parties. The creation of large regional groupings and the method of multilateral tariff negotiations are partly responsible for this trend. The situation, which is considered unsatisfactory and unfair, could be improved by revising the notion of "substantial interest".

2. Proposal

One or more additional consultation rights would be granted to any other contracting party establishing a substantial interest, on the basis of a criterion that takes account of the effects which the withdrawal of the concession has on a given country's economy.

These effects can be determined by two factors, namely:

- the importance for the country concerned of exports of the product concerned as a proportion of total exports (exports of all products);
- the share of exports in the gross domestic product (GDP) of the country concerned.

A new definition of substantial interest, providing eligibility for consultation rights, must take account of these two elements to be economically justifiable. It is the earnest of an outward-looking economy, which is in keeping with GATT philosophy. To do otherwise would mean:

- favouring countries for which foreign trade represents a minor part of the domestic economy;
- favouring countries which have an undiversified economy.

(a) Definition of "substantial interest" (see Annex)

Switzerland proposes that substantial interest should be determined by means of a formula that takes account, firstly, of the affected exports in relation to total exports, and secondly, the importance of exports for the domestic economy.

$$F = z x / x * \sqrt{x / GDP}^1 * 100$$

F = factor determining the additional consultation right(s)

z x = exports affected by the modification of the concession

x = total exports (exports of all products)

x/GDP = weighting factor

¹The effects of the square root are very small: it was introduced so that the GDP weighting factor should not be overestimated. The decisive factor in the formula remains the volume of exports.

The weighting factor

The "GDP" weighting factor is necessary to determine the importance of the external sector in a country's economy. If the proportion of affected exports in relation to total exports (zx/x) is the same for two countries, the GDP weighting factor will allow the supplier's right to be attributed to one rather than the other by taking account of the share of exports in the country's economy.

(b) Consultation rights for parties having a substantial interest

Experience has shown that it is in practice hard for a country to exercise a negotiating right which it has been granted if that country does not account for a substantial share of the imports of the country intending to withdraw or modify a concession. Furthermore, a multiplication of negotiating rights would be likely to complicate the procedures for the application of Article XXVIII.

We therefore propose that the two contracting parties with the highest (F) factor should have a consultation right on grounds of substantial interest.

II. New products

Article XXVIII of the General Agreement authorizes a contracting party, following negotiations, to increase the rate of a bound duty by offering in exchange compensation on another product.

Article XXVIII is also sometimes invoked to increase preventively a duty which a party plans to apply to what are called "new products", in other words a product that is just beginning its "career" on the market. So far, this problem has only been approached from the standpoint of compensation.

However, to determine the compensation that is due, under current practice, account is taken of the three previous years which are considered most representative in terms of trade flows. This element is lacking in the case of new products, for which no statistics are available. Furthermore, how can the parties holding negotiating rights under Article XXVIII be determined?

It must be recognized that Article XXVIII was not designed to deal with new products, simply because the problem did not arise at the time when the General Agreement was drafted in the same way as it does today. These are times of intense creative activity on a scale that did not exist in 1947. However, major interests are at stake, and it is therefore necessary to establish suitable rules in this area.

The methods advocated so far in this Negotiating Group to evaluate compensation rights are, in our view, based on criteria that are too static or too vague to be operational (estimation of production, amount of investment made in the industry in question, etc.). In all cases these criteria leave far too much room for subjectivity.

We therefore propose a different approach. It is based on the principle of greater discipline as regards the creation of a tariff line for new products.

1. Principles

- the creation of a tariff line for a new product must be based on the characteristics the product in question has in common with like products¹ of an existing tariff line;
- the tariff applied to the new product cannot be higher than the tariff applied to the like product bearing the lowest tariff;
- the new tariff may be unbound only after three years of trading in the product concerned following the creation of the tariff line;
- if the tariff is unbound after three years, the growth rate of trade for the product concerned must be taken into account to calculate compensation;

Naturally, if the conditions of Article XIX of the General Agreement are satisfied, a country whose domestic industry of the product in question is threatened may take safeguard action.

2. Advantages of this method

This approach:

- ensures that a new product is not shut out of the market before it has even had a chance to win a foothold;
- resolves the problem of compensation, since the prohibition of any unbinding during the first three years of trade will ensure that the necessary data are available to determine both the holders of supplier's rights and also the amount of compensation.

¹The term "like product" shall be interpreted to mean a product which is identical, i.e. alike in all respects to the product under consideration, or in the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the product under consideration (see Article 2 of the Anti-Dumping Code and Article 6 of the Code on Subsidies and Countervailing Measures).

III. Retaliatory action

Article XXVIII, paragraph 3, authorizes contracting parties to take retaliatory action if they have been unable to reach agreement on the amount of compensation with the contracting party responsible for the unbinding. As things stand, Article XXVIII authorizes the injured contracting party to take retaliation erga omnes, and these measures can only be based on concessions which it has itself initially negotiated with the contracting party at which the retaliatory action is aimed. This system has two major drawbacks:

- It has the result that third parties which have nothing to do with the dispute are doubly injured: first by the measure leading to the withdrawal or modification of a concession, and a second time when the parties which have been unable to obtain the compensation to which they were entitled decide in turn to withdraw a concession, as provided for in Article XXVIII:3. These drawbacks also mean that any contracting party authorized to apply Article XXVIII:3 will hesitate to take, or even forego taking, such retaliatory action even though it is necessary to restore the balance which has been broken to its disadvantage. This is particularly true in the case of small and medium-sized trading nations.
- Small trading partners are placed at a disadvantage since, given their economic weight and bargaining power, they generally have only a small number of initial rights. This further limits their room for manoeuvre in the negotiations.

Switzerland therefore proposes:

The introduction of an interpretative note to Article XXVIII:3 explicitly authorizing contracting parties, where the parties have been unable to reach agreement on compensation, to take retaliatory action on a bilateral basis against the contracting party which initially withdrew its concession. The injured party shall freely determine the concession to which the retaliatory action will apply. It shall inform the CONTRACTING PARTIES but shall not be obliged to obtain their prior approval. However, if the action taken goes beyond what is required to restore the balance of advantages, the CONTRACTING PARTIES may request that it be adjusted.

IV. Tariff rate quotas

The establishment of a tariff rate quota is a procedure by which unlimited bound tariff concessions are turned into tariff concessions limited to a certain quantity of the imported product (a quantity expressed in units, weight or ad valorem). Once imports exceed the specified quantity, exporters must pay a higher duty.

Without prejudging the question of the consistency of tariff quotas with the General Agreement, it is necessary to avoid encouraging the use of such measures, while at the same time recognizing that simply prohibiting

them might well have even worse consequences for world trade. The best means available for mitigating the adverse effects of the introduction of a tariff rate quota remains compensation. However, the methods envisaged so far for determining the amount of compensation are based on unreliable criteria that leave too much room for subjectivity. Here the same problem arises as in the case of new products (see above).

In order to ensure that tariff rate quotas are introduced on an exceptional basis, while at the same time averting the danger of more frequent recourse to complete unbinding, compensation must:

- exceed the amount of the trade actually affected by the partial unbinding; and
- not be so burdensome as to make it more advantageous to unbind the entire tariff heading.

The basic data used in the calculation of compensation would consist of:

- all the affected trade, together with the average growth rate for the three previous years considered to be the most representative;
- 50 per cent of the trade not affected by the tariff rate quota.

Example

	Year		
	1	2	3
Imports	800	1,000	1,200

Tariff quota: 1,000

Affected trade: $(1,200 - 1,000) + (200 * r)$

r = growth rate of exports (in our example about 22.5%)

Amount of compensation: $1,000/2 + 200 + (200 * 22.5\%)$
 $500 + 200 + 45 = \underline{745}$

Results of the Formula

Formula: $F = \frac{(zx)}{(x)} \cdot \sqrt{\frac{(x)}{(GDP)}} \cdot 100$

	$\frac{(zx)}{(x)}$	$\frac{(x)}{(GDP)}$	<u>Result</u> (F)
A	1%	50%	0.7
B	1%	25%	1.5
C	1%	10%	0.3
A	3%	50%	2.1
B	3%	25%	1.5
C	3%	10%	0.9
A	5%	50%	3.5
B	5%	25%	2.5
C	5%	10%	1.6
A	10%	50%	7.0
B	10%	25%	5.0
C	10%	10%	3.0
A	20%	50%	14.0
B	20%	25%	9.0
C	20%	10%	6.0