

**GENERAL AGREEMENT
ON TARIFFS AND TRADE**

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**WORKING PARTY ON THE FREE TRADE AGREEMENTS
BETWEEN SWEDEN AND ESTONIA, LATVIA AND LITHUANIA**

Draft Report

1. The Working Party was established by the Council at its meeting on 14 July 1992 with the following terms of reference: "to examine, in the light of the relevant provisions of the General Agreement, the Free Trade Agreements between Sweden and Estonia, Sweden and Latvia, and Sweden 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/7132/Rev.1.
3. The Working Party had before it the following documentation:
 - (i) Communication from Sweden (L/7036)
 - (ii) Texts of the Agreements (L/7036)
 - (iii) Questions and replies (L/7207)

I. **General Statements**

4. The representative of Sweden stated that the Baltic countries were of special interest to his country because of geographical proximity, historical ties and security concerns. Sweden wanted to support Estonia, Latvia and Lithuania in their transition towards market economies by facilitating their integration into the multilateral trading system. The Free Trade Agreements would contribute to this integration by providing the Baltic countries with improved access to western markets. The opening of these new markets would result in greater economic development for the Baltic countries and in an increase in reciprocal trade with their trading partners. Foreign investment would be drawn to the Baltic countries as a result of the Agreements, further stimulating their economic growth.
5. Before their participation in these Free Trade Agreements, the Baltic countries had virtually no experience of the multilateral trading system. Therefore, the negotiation process of the Free Trade Agreements as well as the meetings of the Joint Commissions had provided an important stimulus to move in the direction of the multilateral trading system. In its effort to facilitate the integration of the Baltic countries into the multilateral trading system, Sweden had provided technical assistance to the Baltic countries' preparations for membership to GATT. Eurocustoms had undertaken the development of the customs administrations in the Baltic countries and this was expected to be carried out as a Nordic or as a bilateral initiative.
6. The Agreements covered HS Chapters 25-97 as well as some specific products within HS Chapters 1-24. Rules on intellectual property, state aid, competition and public procurement, which

were not yet developed in the Agreements, would be based on the system existing within the EFTA Agreement. Separate arrangements had been established to cover free trade with respect to specific unprocessed agricultural, specific processed agricultural, and specific fish products. They entered into force in Estonia and Lithuania on 1 July 1992 and had been applied in Latvia as a transitional measure since 1 July 1992.

7. Trade between Sweden and the Baltic countries had expanded rapidly since the entry into force of these Agreements. The Agreements covered 93 per cent of bilateral trade between Sweden and Estonia, with corresponding coverage of 90 per cent and 95 per cent for Latvia and Lithuania respectively. Thus, "substantially all the trade" was covered by the Agreements, fulfilling the requirements of Article XXIV of GATT. Further details on trade in agricultural products would be provided to the Working Party when available.

8. One member stated that his government supported the transition of the Baltic countries to market economies. These Agreements 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.

9. The representative of a group of countries said that his delegation supported these Free Trade Agreements and Arrangements on agriculture and fishery products, seeing in them an appropriate response by Sweden to the economic, social and political situations of the Baltic countries. A special relationship existed between this group of countries and the countries signatories to these Agreements since Sweden 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 Agreements were a logical evolution of the geopolitical situation now existing in Europe.

10. Another member expressed his delegation's satisfaction with the Agreements concluded by Sweden 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 the European Free Trade Association for such agreements, which was to respond to economic difficulties as well as 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 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 working parties should focus essentially on two aspects: to ensure 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 Agreements between Sweden and the Baltic States fulfilled those requirements in Article XXIV, and in particular paragraphs 4 and 8(b).

11. 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. He went on to say that the retention of the margins of preference offered in free trade agreements could cause problems when the Baltic countries 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 preference offered to Sweden through these Agreements. The representative of Sweden stated that no provision existed in the Free Trade Agreements that would prevent the Baltic countries from making tariff concessions to third parties.

12. The same member noted that the application by Sweden to become a member of the European Communities could give rise to a situation where overlapping tariff preferences were being granted by Sweden to the Baltic countries and to the European Communities. He asked whether these Protocols allowed Sweden to grant preferences to the European Communities, for example, on agricultural products in the context of the European Economic Area. The representative of Sweden stated that his country intended to preserve its free trade with the Baltic countries. Negotiations would be carried out between Sweden and the European Communities to find the necessary solutions to technical issues arising in this context.

II. Examination of the provisions of the Free Trade Agreements

13. The Working Party proceeded with a detailed examination of the provisions of the Free Trade Agreements, taking into account the questions and answers circulated in document L/7207.

14. With regard to the scope of the Agreements, several members noted that agriculture had been covered under separate arrangements. The exclusion of agriculture, an important area of trade, from liberalization under the Agreement meant 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-trade threshold. Even though there was at this time only a small amount of trade in agricultural products between the Parties, this could change in the future, and was not in itself a valid basis for excluding agriculture from across the board liberalization under the free trade area agreements.

15. 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).

16. One member referred to the data for 1992 (Answer 1.1 in document L/7207) which indicated that the share of total trade accounted for by agricultural products was 7.5 per cent between Sweden and Estonia, 10.7 per cent between Sweden and Latvia and 16.1 per cent between Sweden and Lithuania. In the view of countries, exporters of agricultural products, these figures represented a significant share of trade. She further noted that the proportion of total trade accounted for by agricultural products for which duty free concessions were provided under the respective bilateral agreements was 0.7 per cent for Estonia, 0.2 per cent for Latvia, and 11.5 per cent for Lithuania. She asked to what extent the remaining proportion of trade in agricultural products was subject to duties and other measures on imports. In response, the representative of Sweden stated that this trade would be subject to normal most-favoured-nation treatment.

17. Another 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 made higher or more restrictive with the formation of a free trade agreement. In response to the assurance sought by the representative of a group of countries, the representative of Sweden confirmed 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.

18. In response to a question on the prohibitions or restrictions of imports and exports justified on grounds of "protection of the environment", the representative of Sweden noted that the term in Article 6 was a standard provision which was now being applied in many free trade agreements.

19. One other member stated that while tariff preferences might be created in the process of establishing a free trade agreement, the final objective of a GATT-consistent agreement should be the elimination of barriers to trade between the parties, not the continuation of these preferences. If a free trade agreement required parties to retain tariff preferences this meant that m.f.n. levels were being maintained at levels higher than were required for industry assistance reasons in terms of Article 16.

III. Conclusions of the Examination of the Free Trade Agreements in the light of the relevant provisions of the General Agreement

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

21. There was wide sympathy within the Working Party with regard to the rationale for the Agreements which were seen as an appropriate response by Sweden 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 Sweden.

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

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

24. The Working Party noted the confirmation by the delegation of Sweden that the tariff preferences granted in the Agreements 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.

25. The Working Party welcomed that, with respect to products covered by the Free Trade Agreements, all duties and charges of equivalent effect, as well as quantitative restrictions and measures of equivalent effect, except for a few minor export restrictions that would continue to be applied by Sweden and Estonia, had been eliminated with the entry into force of the Agreements.

26. The Working Party noted that the Agreements contained provisions on dumping and state aid and also provided a framework for the elaboration of rules on competition, public procurement, intellectual property rights, services and investment within a specified time-frame.

27. The Working Party noted that the agricultural sector was covered in separate arrangements between Sweden and the Baltic countries. Several members of the Working Party expressed concern that the agricultural sector was excluded from the Agreements which meant, in their view, 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 Agreements 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 Agreements 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 Agreements 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.

28. The Working Party agreed that the Free Trade Agreements 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 Agreements. However, some members considered that the selective treatment of agricultural trade under the Agreements prevented full conformity of the Agreements with the General Agreement.

29. Sweden is 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 1995.