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DRAFT REPORT^{*} OF THE
SPECIAL COMMITTEE ON PREFERENCES
ON ITS ELEVENTH SESSION

held at the Palais des Nations, Geneva,
from 3 to .. May 1982

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^{*}/ Further portions of the draft report will be issued as addenda to the present document.

Introduction

1. In accordance with the calendar of meetings adopted by the Trade and Development Board in decision 251 (XXIV) of 19 March 1982, the eleventh session of the Special Committee on Preferences was held from 3 to .. May 1982, in the course of which the Committee held ... plenary meetings. The present report contains an account of the proceedings of the Committee in those meetings.
2. In an introductory statement at the opening of the session, on 3 May 1982, the representative of the Secretary-General of UNCTAD said it seemed advisable for the Committee's plenary meetings to be devoted to issues of a general character, in keeping with the terms of its mandate (Decision 179(XXVIII)), while private meetings ~~were~~ held for informal consultations between preference-giving and beneficiary countries.
3. He made general comments on the GSP and the functioning of the Special Committee on Preferences and highlighted the principal features of the concept of graduation or differentiation. He made some suggestions aimed at improving the operation of the GSP, including technical assistance matters connected with the operation of the system.
4. In his general comments, he said that, because of its autonomous and intrinsic nature, the GSP had operated as a system outside the multilateral framework of mutual rights and obligations of the international trading system. That sui generis feature, a direct outcome of the way in which the preference-giving countries had decided to administer their individual schemes, had involved a number of important consequences that called for analysis, both in the light of the experience gained in operating the system over more than a decade and in the light of recent events regarding a number of the schemes and of allied factors in the so-called special relations between various categories of countries.
5. To begin with, as a result of the autonomous nature of the schemes, various elements had been introduced unilaterally into the generalized system of preferences and would never have been accepted, or would at best have been tolerated, on an exceptional basis under clearly defined circumstances, in other areas of trade relations. He referred to such measures as quantitative limitations or ceilings and competitive need limitations. Such elements were already inherent in the preference schemes, either because they had been introduced by a preference-giving country in its original schemes or because they had been included in the new schemes.

Initially, the purpose of such measures seemed to be to rule out the possibility that imports under the preference scheme might cause some form of injury to domestic industry. Indeed, some preference-giving countries had taken the view that, without unilateral safeguard measures of that kind, the basic elements of their own GSP schemes would have been less liberal. The expectations, however, were that those safeguard measures would in time be liberalized. In fact, those measures were now being applied much more rigorously, something which had increased the instability of the GSP. More recently, such measures have even been justified by such subjective notions as that of graduation, which made for even more uncertainty in the system of preferences.

6. Since its inception, the Special Committee's activity in reviewing the operation of the GSP had been conducted in isolation from major developments in the international trading system. The GSP had been approached as a technical subject, as if it bore little relation to the general objectives of trade policies. Obviously, that was not the most desirable approach. For that reason, he focused on some of the basic issues in the world trading system that had very important implications for the GSP.

7. One of the central concerns of the international community dealing with trade matters at the present time was to impose or try to restore some discipline in the face of the abuse of various types of trade measures all aimed at safeguarding domestic industry from the "injury" or "prejudice" or "market disruption" caused by import competition and to prevent them from being applied unilaterally, particularly when such a course tended to be taken arbitrarily and even in a veiled fashion. The efforts being made under the MTN agreements, the renewal of the MFA and the current negotiations on safeguards, together with the forthcoming GATT Ministerial Meeting and UNCTAD VI, were to be viewed against that background and all had attached the highest priority to those topics. The Special Committee on Preferences could not cut itself off completely from that international debate.

8. In connection with the concept of graduation or differentiation, he said that it had virtually become a compulsory topic in the part of the international community that watched over trade activities. Because of its connotations and its importance, the concept of graduation had a very special and direct bearing on the GSP. Nevertheless, its application was not confined to the preferential framework of the system of preferences, and still less to other areas of international trade policies.

In fact, the concept went beyond trade and impinged decisively on monetary and finance policies. The distinguishing feature of the concept of graduation in the context of the GSP was that it was becoming increasingly associated, and one could almost say confused, with yet another safeguard mechanism. He drew attention to that phenomenon, for two reasons. The first was obviously the significance of the concept of graduation for the future of the GSP, but no less important were its implications in the context of international trade relations in general, and in particular it affected the trade interests of the developing countries, both in the present and in the future.

9. Recent developments in some individual GSP schemes afforded sufficient illustration of how those concepts had become intertwined, to such an extent that they had considerably affected most, if not all, of the beneficiary countries under those schemes. For instance, under one major scheme, so-called sensitive products were being administered by means of tariff quotas for the beneficiaries deemed to be more competitive, and through tariff ceilings for all other beneficiaries except the least developed countries. Those bilateral quotas or ceilings corresponded to the maximum country amount limitations, so that the countries which had been affected by limitations in the past were now all subject to individual tariff quotas.

10. Under another scheme, the preference-giving country had adopted the policy of phasing out and eventually eliminating preferential treatment for the more economically advanced developing countries. Again, other preference-giving countries had adopted measures to exclude a particular beneficiary from preferential treatment for particular products. Consequently, the criterion for differential application under the preferential treatment scheme was not only product-specific but was also directly country-specific.

11. It was clear that the application of the principle of graduation, viewed in that way, was not only inconsistent with the fundamental principles underlying the GSP, which had been agreed on multilaterally, but it was also clear that confusion of that principle with the safeguard concept was completely distorting the GSP and was severely undermining the action intended to achieve its fundamental objectives.

12. He said that many developing countries had expressed concern about the arbitrary and discriminatory fashion in which some preference-giving countries were operating their schemes. They had argued that the exclusion of products exported by them under the schemes on the grounds of so-called graduation was totally and absolutely inconsistent with the relevant provisions of the enabling clause agreed upon in the MTN. They had also pointed to the provisions in the enabling clause that required modifications in the GSP schemes to respond positively to the development, financial and trade needs of the developing countries. In their view, the exclusion from GSP schemes of products from certain countries would undoubtedly lead to an increase in supply through domestic producers or exporters in industrialized countries, rather than through other developing exporters not affected by the exclusion measures. For all those reasons, the developing countries had stressed the importance of introducing transparency and objectivity into the GSP, and removing the elements of uncertainty in it. It was known that some beneficiary countries had sought to test the practical usefulness of the enabling clause, but so far such attempts had not proved successful. Surely, there was scope for re-evaluating the approach adopted to date, so as to work out new initiatives.

13. The preference-giving countries had based their arguments that the graduation principle was a process of adjustment primarily on the grounds that it made for a wider and hence more equitable spread of the benefits of the GSP. It had been claimed that if the share that went to the more competitive countries was reduced, the share available for the other preference-receiving countries would increase proportionally. At the same time, it had been argued that the adjustment was tied in with the "difficult economic situation" faced by some of the importing countries. Those arguments in support of the graduation system could be viewed as a conceptual platform for defending the concept as a permanent feature of the GSP, since there would always be differences in the levels of development of the developing countries, regardless of whether or not "difficult circumstances" existed for certain countries.

14. To date, the secretariat had found no evidence that would at least back up the claim of a "switch" of benefits towards an increasing number of developing countries. There was no direct link between the graduation of a beneficiary country with regard to a particular product and an increase in trade in that product on the part of another beneficiary country. As the secretariat had pointed out, in many instances the aim and the effect of graduation measures, far from achieving a more

equitable spread among an increasing number of beneficiaries, was to reduce the share of GSP benefits for those countries which were certainly in a position to take advantage of the system. The argument about spreading the benefits of the GSP was more in the nature of a smoke-screen designed to distract attention from the real motivation underlying the graduation concept.

15. The representative of the Secretary-General of UNCTAD said that it would first be useful for the Special Committee on Preferences to direct its attention, separately, to the concept of safeguards and concept of graduation and then proceed to look into the difficulties that arose when the two concepts became intertwined. Safeguard clauses, regardless of how they were called, whether "emergency action", "escape clauses" and so on, existed throughout the international trading system. In GATT, the safeguard clause (article XIX) was directly tied in with concessions or other obligations under that multilateral agreement; it was part and parcel of the over-all balance of rights and obligations. In article XIX, the economic and the legal criteria were dealt with separately. It was the economic criterion, an increase in imports which caused or threatened to cause serious injury, that justified resort to safeguard action, in other words, the imposition of restrictive trade measures. On the other hand, it was the legal criterion that governed the application of such measures, in other words, they had to be applied on a non-discriminatory basis. A further important element was that the countries which were affected by the outcome of the consultations and were not satisfied with the compensation had the right to withdraw concessions from the party concerned, not as a retaliatory or punitive measure, but for the purpose of restoring the over-all balance temporarily affected. It could be argued that the GSP involved no contractual obligation whatsoever on the part of the preference-giving country. That absence of legal status could rule out any obligation analogous to the second part, in other words, the legal part of article XIX of GATT, but that was no reason not to include the economic aspect in the GSP schemes. It might even seem essential, if the GSP was to be turned into a dynamic instrument to promote increased exports by the developing countries, for a safeguard clause to be constructed in such a way that it afforded clear and objective economic criteria for the withdrawal of GSP benefits in connection with the products covered by the various schemes. That might, to some extent, compensate for the uncertainty caused by the fact that, in itself, the GSP had no contractual status. A clause of that kind would ensure certainty and predictability for exporters and would considerably facilitate the operation of the schemes by the preference-giving countries.

16. Moreover, the concept of "graduation" was a highly subjective one. When it was confused with the objective economic concept of "injury" to domestic industry, the two concepts became meaningless. The absurdity of mixing up those two concepts of graduation and safeguarding could be illustrated by the following example. A developing country with a high level of per capita income was not necessarily more competitive than, for instance, a developing country with a lower per capita income. It would probably be the case that a country with a smaller per capita income where wages and overheads were lower would for those very reasons be more competitive, but it was not possible to conclude that, in consequence, the less developed countries were the most competitive of all.

17. Although mention was frequently made of the MTN "enabling clause" to justify graduation measures, the expression as such did not appear in the relevant text, which referred instead to "fuller participation of developing countries". Rather, a distinction was made between "differential and more favourable treatment" under the GSP in paragraph 2(b) of the decision, and increased participation by the developing countries (or co-called "graduation"), which was dealt with in paragraphs 5 to 9. As defined in paragraphs 5 to 9 graduation meant that, as the developing countries progressed and reached a more advanced stage, their capacity to make concessions would improve, they would agree to a higher level of obligations under GATT, and they would have less frequent recourse to the non-reciprocity provisions of article XXXVI of GATT (which were repeated in the enabling clause). There was no reference whatsoever to the withdrawal of preferential, more favourable or differential treatment in that context. That possibility was mentioned only in paragraph 4, which provided that such withdrawal could take place only to the satisfaction of the parties and not unilaterally. He believed that the background to the drafting of the decision on differential and more favourable treatment, reciprocity and fuller participation of developing countries would bear out that interpretation.

18. There was no room for the concept of graduation in the GSP. The only logical and fair basis for withdrawing such treatment from a country benefiting from a GSP scheme could be to arrive at a clear and precise determination of a jointly agreed criterion and to support the case by the production of relevant factual information to show that the imports concerned were causing some form of "disruption", damage or injury, etc., in the market of the

certain industrialized countries were due, in particular, to the failure to have applied in time the structural adjustment policies warranted by circumstances. In many cases, the recapturing of the internal market by domestic products had been given virtually free rein, but unfortunately it had been done through restrictions on imports, frequently applied in a selective manner. That was the same type of argument as had been adduced in the Sessional Committee of the Trade and Development Board in the discussion on structural adjustment.

23. The need for appropriate structural adjustments, both in exporting and in importing countries, was an implicit feature of the purposes and objectives of the GSP. It was necessary to refer back to the historical context in which the scheme of preferences for the developing countries had been agreed upon. The preferential tariff reductions under the GSP had been conceived as a first step in a broader process of trade liberalization which was to take place over a far longer period. That was why, at the time when the resolution on the GSP had originally been adopted, it had been recognized that that scheme should not constitute an impediment to the reduction or elimination of tariffs and other restrictions on a MFN basis; that stipulation was repeated in the "enabling clause".

24. He said that it was relevant to ask a further question: if it was not possible to make minor structural adjustments in response to comparatively weak competition resulting from the GSP, what real hope was there for a future substantial liberalization of trade on a multilateral basis?

25. With regard to improvements in the GSP, he said that the concept of graduation had a disturbing corollary which should also be discussed in plenary. In addition to freezing or reducing the benefits to be derived from the GSP, that concept had had the effect of virtually arresting or slowing down the process of improvement of the system. When the GSP had been agreed, it had been on the understanding that improvements would be achieved in a dynamic context. While it was true that trade covered by the GSP had increased during the previous decade to the point that it now represented 50 per cent of dutiable imports, it was also true that that was only an average, because effective coverage under some schemes was much smaller. There was therefore no doubt that there was considerable scope for improving the GSP.

26. He referred to the comments which he had made at the previous two sessions of the Trade and Development Board, when he had drawn attention to a number of important developments in the international trading system, some of which were not only relevant to, but also had significant implications for, the GSP. One of those comments had emphasized the decline in the importance of fixed measures of protection, particularly customs duty levels. An examination of the tariff structure across various import sectors in the industrialized countries had shown that, for a substantial number of product categories, tariffs remained very high and hence constituted significant barriers to trade. In many cases, the products running up against such barriers were of major interest to the developing countries. A large number of those products were on the list of exceptions or the list of sensitive products of many of the preference-giving importing countries.

27. The secretariat's estimates of tariff protection levels for imports into selected developed, market-economy countries, had shown that tariffs applied to labour-intensive imported goods were much higher than the tariffs applied to imports from the world as a whole.

28. He said that efforts should therefore be made to redress that discriminatory treatment and those tariff disparities in respect of products of major interest to the developing countries, by including such products in schemes of preferences. Improvements to schemes should not be confined to the extension of product coverage but should also involve the removal of certain quantitative restrictions or, alternatively, an increase in the volume of preferential imports. Another important aspect was the need to simplify rules of origin and make them more flexible. In the latter connection, he said that the Committee would have the opportunity of hearing the report by the Chairman of the Working Group on the results achieved at the Group's meetings held the previous week. As to the matter of simplifying the rules, a problem of continuing concern to many exporters was the additional conditions of some rules of origin which required the use of certain specific manufacturing processes or the incorporation of elements of advanced technology in the final product for that product to be given the benefit of preferences (for example, textiles and electrical machinery). Obviously, the most significant improvement that could be made to the GSP would be the reduction of its intrinsic uncertainty.

29. With respect to the question of technical assistance, pursuant to the recommendations made by the Committee on Preferences at its previous session, UNDP had allocated funds to the GSP technical assistance project, and that had enabled UNCTAD to maintain the project as a focal point for the dissemination of information on GSP preference schemes. Moreover, the UNDP Regional Bureau for Asia and the

Pacific had agreed to extend the stay in the region of the GSP Adviser, who would continue to co-ordinate his work with the interregional project. All effective support and participation by the preference-giving countries, as well as by the preference-receiving countries, was not only welcome but also extremely useful for the continuation of activities under the project. In 1981, voluntary contributions had constituted 5 per cent of the funds allotted to the project by UNDP.

30. The project activities during 1981 were described in document TD/B/C.5/82. The schedule of activities had been relatively modest, owing to the limited resources available. The resources allotted remained modest for the planning of an extensive programme, particularly as far as training in the field was concerned. He said that the secretariat would continue its contacts with Governments with a view to meeting some of the shortfalls in resources on the basis of operational requirements.

31. He said that the Committee should also analyse certain important developments which had implications for the GSP. He referred to the so-called "Caribbean initiative", the proposal which the United States Administration had recently submitted to Congress in the form of the Caribbean Basin Economic Recovery Act. The main feature of that initiative would be to give authority to the President of the United States to grant duty-free treatment to 28 countries and territories in that region for a period of 12 years following enactment of the programme. All products would be eligible for preferential treatment, except for textiles and apparel subject to the MFA. Sugar imports would be eligible up to certain levels. The rules of origin would be the same as those applied under the United States scheme of generalized preferences, except that the minimum value-added requirement would be reduced from 35 to 25 per cent.

32. The United States had recently notified GATT of its intention to implement that proposal, for which purpose it would of course be necessary to obtain the relevant legal dispensation or approval from the contracting parties. He made two brief comments on that initiative. The first was that, although it had been publicly stated that it would be a one-way free trade scheme, there seemed to be a series of additional conditions which, prima facie, did not support that assertion. Secondly, such arrangements had in the past been justified as a means of avoiding serious disruptions of the trade flows which had been created with metropolitan countries under the colonial régimes. There was no doubt that the proliferation of trade agreements which, for one reason or another, discriminated between developing

countries was not in itself a welcome development, viewed from the standpoint of trade fragmentation. Politically and economically, the implications were far-reaching. The Committee might wish to examine the consequences of that initiative in terms of its consistency with the nature of the GSP.

* * *

33. At its 112th meeting, on 4 May 1982, the Committee observed a minute of silence in tribute to the memory of Mr. Mohammed Benyahia, Minister for Foreign Affairs of Algeria, who died in an aircraft accident on the previous day.