

## Lesson 5: International Trade Law

### Principle of no discrimination: The Most Favored Nation Treatment

- Content: Every WTO Member must offer imports from (and exports to) any other WTO Member the **best-available treatment offered to any other country**.
- First known application in the 11th century: in the Charter of the town of Mantua the Roman Emperor pledged to afford Mantua all the benefits granted to «whatsoever other town».
- It's a common clause in commercial treaties since the 17th century.
- Coming closer to our times: the United States insisted on its inclusion in the GATT, with the aim of getting rid of all the colonial preferences of the European countries.

It is expressed in GATT Article I:

- **With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation** or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to **all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 (taxes) and 4 (internal regulation) of Article III,\*any advantage, favor, privilege or immunity granted by any contracting party to any product originating in or destined for any other country** shall be accorded **immediately and unconditionally** to the **like product** originating in or destined for the territories of **all other contracting parties**.
- **The GATT enshrines the MFN clause in its broadest meaning:** the benefit granted is unconditional and immediate.
- **Unconditional MFN:** if State A has a MFN obligation in favor of State B, then, any advantage it (State A) affords to State C, it must also grant to State B;
- **Conditional MFN:** if State A has a MFN obligation in favor of State B, then any advantage it (State A) affords to State C, it must also grant to State B but only on the condition that State B affords to State A advantages similar to those State A gets from State C
- it promotes further liberalization of trade, favors small States, provides for more relaxed trade relations among countries, simplifies custom operations, constrains the ability of lobbies to obtain preferential measures....
- ... but it also has its flaws: the worst is that it allows «**free riding**»: smaller trading nations may be tempted to profit from the concessions negotiated among others without giving anything themselves.

What could be the effects of free riding on the liberalization process?

- Small countries will liberalize less
- but also major trading countries will agree to less liberalization than if reciprocal concessions were required.
- A slowing down effect of the multilateral trade liberalization process in general
- To partly prevent the risk of free riding: major trading countries prefer not to make commitments unless a «critical mass» of countries has agreed in advance to make liberalization commitments.

- Notwithstanding this flaw of the system, WTO Members have been able to make progress in the telecommunication, information technology products and financial services sectors.

MFN covers both Border Measures (Tariffs/Quotas) and Internal Measures

- The non discrimination rule set out in GATT Article I covers a variety of measures: it covers duties and charges, but also the internal measures of Article III. It is then useful to compare how the rule is applied in the two cases:
  - Article III out rules the less favorable treatment of imported goods vis à vis like domestic products.
  - Article I out rules less favorable treatment of goods imported from a foreign country vis à vis like goods imported from another foreign country
- Both norms aim to protect those goods which are directly competitive with other goods (internal/imported) receiving a more favorable treatment.
- No reason to apply a different definition of like products.

MFN: Tariffs

- Here, the application of the MFN rule is more complicated.
- 1. Article II allows tariff protection: so, when applying to tariffs, the aim of Article I is merely to regulate the use of this means of protection in a way to limit its negative effects on trade.
- In other words, it cannot out rule the main tool of tariff protection, that is the policy of tariff classification: it can be necessary for WTO Members to master the distinction of products in different tariff lines in a way that is the most convenient for the economic interests of the country.
- Tariff negotiation is based on reciprocity of concessions: it is not easy to reconcile this with the non discrimination rule of Article I, which allows the practice of «free riding» (the opposite of reciprocity: taking advantage of commitments made by others without paying anything in exchange)

#### **How to reconcile reciprocity of negotiations with the non-discrimination rule of Article I?**

- States tend to wait until an advanced political agreement on the concessions to grant is met among the major trading nations (each one affording almost equal contributions) before proceeding in the negotiations (so to minimize free riding)
- Through finely designed product distinctions in their tariffs States manage to limit the benefit of tariff reductions to those countries that have granted equivalent concessions in return.
- {E.g.: the 1904 German tariff concession to Switzerland on «large dappled mountain cattle reared at a spot at least 300 meters above the sea level and having at least one m.

When is GATT Article I violated?

1. A trade policy or measure among those listed in Article I:1;
2. One country is granted an «advantage» compared to others;
3. This advantage is not accorded «immediately and unconditionally» to all WTO members;

#### 4. The advantage relates to «like products».

Does GATT Article I:1 cover discriminations not based on the national origin of the imported product?

- The Belgian Family Allowances case (1952) shows that a preference not based on the national origin of a product, but on policies in place in the exporting country is out ruled by Article I:1
- The EC-Seals case (dealing with PPMs) clarifies that under Article I:1 we do not examine whether a condition is justifiable, we only examine its impact on the competitive opportunities on the marketplace for like imported products.

Does GATT Article I:1 cover discriminations not based on the national origin of the imported product?

- Legitimate regulatory distinctions could play a role either: - before (likeness of the products. According to article I, like products can not be discriminated) or - later (GATT Article XX exceptions. Art XX provides exemptions)

Non discrimination and government procurement

- Government agencies often need to purchase goods and services with public resources and for public interests to fulfil their function. Such purchases are generally referred to as public/government procurement.
- These purchases amount to a considerable size (often 10-15% of the GDP), but are related to the exercises of activities in the general interest of the country: for this reason they have been carved out from the application of the GATT (Article III:8(a)) and of the GATS (Article XIII:1).
- Express carve out only refers to National treatment (Article III), but in 2005 a panel report (in EC-Measures Affecting Trade in Commercial Vessels) extended the effects of GATT Article III:8(a) to the MFN rule (Article I).
- The exclusion of the public procurement market from the application of the general GATT regime has its drawbacks: Members can use this policy-space for protectionist purposes.
- During the Uruguay Round government procurements became the object of a plurilateral agreement, whose signatories are today 49 Countries (27 of which are Members of the EU). There are then 36 more WTO Members and 4 international organizations as observers
- In 2012 the text of the Agreement has been revised and since 2014 the new GPA is in force.

Scheme of GPA

- Nondiscrimination: Parties of the GPA commit to opening markets covered by the Agreement to the suppliers of goods and services of other GPA Parties. Article III of the GPA provides for both a MFN and national treatment obligations
- Transparency: Parties must respect minimum standards for the publication of all new procurement legislation so that also foreign interested companies are informed.
- Procedural fairness: Parties must also guarantee independent national review of complaints.

Chapter 11, pg 19: ([https://www.fedlex.admin.ch/eli/cc/1959/1745\\_1807\\_1812/it](https://www.fedlex.admin.ch/eli/cc/1959/1745_1807_1812/it))

- Allowed to make distinctions (it is possible to apply the “special tariff” only for soccer balls made without child labor). All conditions written in the schedules extend to all other member iff products are “alike”. Soccer balls made without child labor can be compared to soccer balls made with child labor? If I consider both products are like products, then the same tariff regime should be applied. The only criteria I could use to refute the fact that these balls are alike is “consumer’s taste” since they won’t like to buy soccer balls if they knew that they were made by child labour.
- Doesn’t matter if Indireland wants part of the WTO. If Palubistan wants part of the WTO, it couldn’t have appealed to the panel.
- If the terms would have not been introduced in Moralia’s schedule, but it just passed a law, then we would need to present the case under **Article III (it would be a lawful internal regulation if there is no discrimination within the domestic and foreign products).**

### Lesson 5, part 2: The Ban of Quantitative Restrictions

- While the GATT regulates tariffs in a way that allows means of protection to the members without infringing too much on the liberalization goal of the WTO, quantitative restrictions have been given a different treatment.

GATT Article XI provides for an **outright ban on them**.

#### General Elimination of Quantitative Restrictions:

- **No prohibitions or restrictions other than duties, taxes or other charges**, whether made effective through quotas, import or export licences or other measures, **shall be instituted or maintained** by any contracting party **on the importation** of any product of the territory of any other contracting party **or on the exportation** or sale for export of any product destined for the territory of any other contracting party.

The **prohibition is not an absolute one**, and the main exceptions are set out in :

- GATT Article XI:2, **export restrictions allowed to deal with shortages of food /essential products**; or **import restrictions** of agricultural or fisheries products to remove a temporary **surplus**.
  - GATT Article XII, allowing for import restrictions to protect **the balance of payments** of member states (e.g. to stop a sudden reduction of the country's monetary reserves)
  - GATT Article XIX, permitting **temporary safeguard measures**, including, under specific conditions, import quotas.
- When consented, quantitative restrictions must comply with the **non-discrimination rules** under GATT Article XIII
- The prohibition provided for in Article XI has been expanded lately by the Agreement on Safeguards, whose **Article 11:1(b) forbids measures of voluntary export restraint**, marketing arrangements or similar measures on the export or the import side which have been quite popular in the past.
  - A Footnote to that provision gives some **examples**: export moderation, export-price or import-price monitoring systems, export or import surveillance, compulsory import cartels, discretionary export or import licensing schemes, any of which afford protection.
  - We find an application of this rule in the **Agreement on Trade Related Investments Measures-TRIMs**: Public measures that allow a company to import only a certain amount of products, to be determined based on how much that same enterprise can export are prohibited.
  - A further expansion of scope of the quantitative restriction's ban is due to the 1994: **Agreement on Textiles and Clothing**. Quotas and restrictive measures had always been much used in the textile sector, but during the Uruguay Round it was finally decided to gradually phase them out. On January 1, 2005 when the Agreement on Textiles and Clothing expired, all special rules on covered products ceased to exist, and textiles and clothing goods started to be regulated by the general provisions of the GATT.
  - Quite a similar roadmap was agreed on in the Uruguay Round to put an end to the special treatment of **agricultural products**. Here, the traditionally applied quantitative restrictions had only to be converted into **tariff measures**: a sort of compulsory tariffication process ending up with the almost complete assimilation of agricultural

products to all other general goods. With an exception acknowledging the sensitive nature of this sector of the economy a Special Safeguard mechanism has been provided for by Article 5 of the Agreement on Agriculture. This allows Members to temporarily impose duties higher than bound tariffs, in the event that import volumes of agricultural products rise beyond a certain threshold or prices fall under a certain amount.

- Quantitative restrictions are **non tariff barriers**. It is negative definition. What about a positive one?
- **They may vary a lot:** from embargos to quotas, to export restraint agreements, to ...imaginative measures like the one applied by France in the 1980s to limit imports of videocassette recorders (VCRs) from Japan Given this great variety, it may be difficult sometimes to assess if a measure is a **quantitative restrictions** (banned) or **an internal regulations** (subject to non-discrimination).
- A doubt may arise for import licences. They are justified for goods such as arms or alcoholic beverages, but they could also serve protectionist aims.
- The **Agreement on Licensing Procedure:** regulates the recourse to these measures in a way to avoid that licensing requirements be used as trade barriers and applied in a discretionary way. Even an **automatic licence** (where the approval is granted) «shall not be administered in such a manner as to have restricting effects on imports» (Article II:2(a)). Restricting effects are **presumed** if the licence is not approved within a maximum of 10 working days

#### **Tariff rate quotas**

- These are rules imposing a ceiling to the number of products that can be imported at a certain tariff rate. Despite the name (quotas) they are regulated under GATT Article II (they maneuver tariff, not quotas). • But to them applies the non-discrimination rule provided for by Article XIII.  
Case Japan/USA semiconductors
- Under the agreement: The government of Japan would monitor the prices of goods exported to the US and, if need be, prevent some exports; it **would also request (not by law. Therefore nothing "binding" for Japanese exporters)** Japanese exporters not to export to the US or third markets at prices below company specific costs.
- The EC challenged the agreement alleging among others, that its application amounted to a violation of Article XI.
- **Japan defense** was that there was no infringement of Article XI, because the measures could not constitute export restrictions as **they were not legally binding or mandatory**.
- On the contrary, **the Panel considered the measures to be quantitative restrictions** because, if lacking formal mandatory effect, **from a substantial standpoint they were operated in a manner equivalent to legally binding measures and were effective on Japanese exporters**.
- What matters is the "effect" that it arouses on the market, not the form.
- **Any form of limitation imposed on, or in relation to importation constitutes a restriction on importation within the meaning of Article XI:1.**

### Export restraints have to be temporary and related to essential products

- In the last decade there have been two cases on this issue, both lost by China and relating to export restrictions on raw materials.
- China triggers the waiver of Article XI:2(a): «critical shortages»
- According to the Panel /AB, to be excused: a measure must concern **essential products** (“deficiencies in quantity that are crucial”); **has to be temporarily applied**, meaning both applied for a limited duration and adopted in order to bridge a passing need. **China was not able to prove this.**
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